Porter Prize
Winners Selection Rationale

This report has been written based on: (1) the materials submitted by the winner for Porter Prize screening purposes; (2) interviews conducted by the Porter Prize Organizing Committee; and (3) publicly available information. It is being published with the winner's permission.

Selection Criteria

The essence of strategy is to do things differently from others. Based on this premise, the Porter Prize recognizes those companies and business units that have chosen to compete in a distinctive way in a particular industry by delivering a unique value proposition, based on innovations in products, processes, and ways of management.

First-stage Selection Criteria

1. Superior profitability
2. Unique value proposition
3. Consistency of Strategy over Time
4. Innovation that Enabled Strategy

Second-stage Selection Criteria

5. Utilization of capital analysis
6. Distinctive value chain
7. Trade-offs
8. Fit across activities

Note

In the analysis of capital utilization, the key focus will be placed on ROIC (Return on Invested Capital) and ROS (Return on Sales). The following report of the winners includes these numbers in comparison with the industry averages. A positive difference from the average indicates that the capital utilization of the company/business is better than the industry average. The five-year average is calculated by aggregating the numerators divided by the aggregated denominators. Thus, the derived five-year average is not equal to the simple average of the ratio for each year. The data used in calculating the industry average was obtained by carefully selecting truly comparable companies among those classified as being in the same industry.

PORTER PRIZE

Organizing Committee

Hitotsubashi University Business School
School of International Corporate Strategy

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Porter Prize 2017 Winners

Organizing Committee
Graduate School of International Corporate Strategy, Hitotsubashi University
2017 Sponsors
Mitsubishi UFJ Morgan Stanley Securities Co., Ltd.
P&E Directions INC.

KATITAS CO. , LTD (Rehabilitation and resale of pre-owned houses)

KATITAS CO. LTD (hereafter, Katitas) purchases, remodels and resells second-hand residential housing in rural communities throughout Japan. Katitas resells the houses at a low price—the monthly mortgage payment for a Katitas home is comparable to the amount paid as rent for an apartment in the same geographic area. The company grows its business by providing good-quality, freshly renovated pre-owned homes in areas where there is a limited supply of newly built homes.

Net Protections, Inc. (Deferred payment service)

Net Protections is a pioneer and the leading provider of a deferred payment service. The company's deferred payment service allows manufacturers to outsource the deferred payment service option offered to customers making purchases via their online sales channel. Net Protections' deferred payment service also helps small online sellers increase their sales. Net Protections reduces its own risk of delinquent accounts (or more precisely, the risk of shoppers not paying their invoices) by providing small loans to vast numbers of shoppers.

Pro-Ship Incorporated (Development and sales of packaged software for fixed assets management)

Pro-Ship has created the packaged software market for fixed assets management, and has sustained its leadership position by targeting large companies that manage complex fixed assets. By undertaking in-house all aspects of the operations (everything from product development to introduction and maintenance services), Pro-Ship achieves superior usability for customers as it pursues business operations centered on packaged software.

QB Net Holdings Co., Ltd. (Haircut service)

QB Net Holdings offers a 10-minute haircut service for 1,000 yen (US$9) at its chain of small barbershops ("QB HOUSE shops") in areas with high foot traffic. The unparalleled convenience of the company's services has generated a new pattern of consumer behavior—a quick stop for a haircut during the lunch break or on the way home. Despite competition from followers imitating QB HOUSE's value proposition, the company has achieved a sustained competitive advantage by increasing inimitability through the internalization of various activities, including the training of stylists and improvement of the fit among activities. QB Net's barbershops in overseas markets are showing growth and contributing to profit.

Selection Rationale (Recipients are addressed in no particular order):

KATITAS CO., LTD

KATITAS CO., LTD (hereafter, Katitas) purchases, remodels and resells second-hand residential housing in rural communities throughout Japan. Katitas resells the houses at a low price—the monthly mortgage payment for a Katitas home is comparable to the amount paid as rent for an apartment in the same geographic area. The company grows its business by providing good-quality, freshly renovated pre-owned homes in areas where there is a limited supply of newly built homes.

General features of vacant homes in Japan

There were 8.2 million vacant homes in Japan in 2013 (or 13.5% of the country's 60 million homes), according to the "Housing and Land Survey 2013," conducted by the Ministry of Internal Affairs and Communications, under the Statistics Bureau of Japan. [1] This survey shows that one out of every seven houses was unoccupied. The number of vacant homes has been rising steadily since 1963 (the year that such data started being compiled on a nationwide basis). The 2013 survey showed that vacant homes (including vacant properties neglected by the owners) increased by 630,000 units from the previous survey, taken in 2008. Single-family homes accounted for 79% of the increase in the overall number of vacant homes. The growth in vacant houses is primarily attributable to the fact that vacant homes are not being demolished or remodeled. The growing number of vacant and abandoned properties are recognized as a social problem because the scenery in a neighborhood is destroyed when a property becomes infested with weeds, and there is simultaneously a deterioration in security.

Since the commencement of the survey by The Japan Journal of Remodeling in fiscal year 2013, Katitas has ranked No. 1 in annual sales of used houses (on a unit basis) every year, for four straight years. [2]

Unique Value Proposition

Katitas purchases used houses mainly in rural communities with populations of 50,000 to 300,000. The company then remodels the houses and sells them. The selling price of a remodeled home ranges from 10 million yen (US$90,900 at 110 yen/$) to 15 million yen (US$136,364) per house. (In fiscal year 2016, sales of single-family homes accounted for 93% of the company's total sales. Fifty-five percent of the company's remodeled homes were priced between 10 million yen and 15 million yen. The average selling price was 13 million yen.) Katitas' main customers are couples with children and annual household incomes of less than 5 million yen (US$454,545). The company especially targets apartment dwellers who are buying their first homes. (Seventy-six percent of Katitas' customers have annual household incomes of less than 5 million yen. Regarding the geographic distribution of sales, 87% of sales were outside of Japan's three largest metropolitan areas of Tokyo, Osaka and Nagoya.)

In Japan, consumers usually must choose between newly built homes, pre-owned homes, and apartments. By offering remodeled single-family homes, Katitas has created a fourth option for consumers. The following are Katitas' five value propositions. The first value proposition is to offer good-quality, single-family homes at a reasonable price. For most buyers, the monthly mortgage loan payment is less than 50,000 yen, which might even be less than the amount they pay as rent for their apartment. So, Katitas has made it possible for families who normally wouldn't be able to afford a newly built home to become homeowners without taking on an additional financial burden. (Katitas' remodeled houses are about half the price of same-size newly built homes in the same location.)

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[1] http://www.stat.go.jp/data/jyutaku/2013/pdf/nihon01-2.pdf, http://www.stat.go.jp/english/data/jyutaku/2501.htm
[2] The Japan Journal of Remodeling, No. 1274, July 25, 2017.

The second value proposition is the provision of good-quality used houses. Most of the used houses are old, and many of these homes have termites. Sometimes the property lines are not clear. In some cases, the neighbors' piping runs below ground on their property. These are some of the reasons why many people prefer newly built homes to second-hand homes. On average, Katitas' homes are 30 years or older, and the properties have a variety of issues, including aging degradation. However, Katitas resolves all these issues, and then resells the home with a two-year warranty against defects. Katitas completely remodels the kitchen, the bath tub, and the lavatory. The company also upgrades the plumbing by installing new pipes. Katitas repairs the roof and the exterior walls. It improves the home drainage system, and carries out an anti-termite treatment. Katitas makes the house a more comfortable living space by changing the layout, and enlarging the area for parking, an essential feature of homes in suburban and rural locations. Katitas also resolves issues relating to rights and registrations, which include the confirmation of property lines and the removal of underground pipes that cross property lines.

The third value proposition is for the sellers. When homeowners sell their homes to Katitas, the company uses a simplified process for arranging the housing property's sale. Once both parties have come to an agreement, the deal can be executed much more easily than usual and in a shorter amount of time. The home inspection must be attended by the sellers. If the schedule for the appraisal itinerary is well managed, Katitas can determine the purchase price in as little as three days. After the seller has agreed to the price and submits the necessary documents (property registration documents, etc.), the soonest that Katitas can make payment is three weeks. Because Katitas conducts an appraisal before submitting a bid for the house, there will be no subsequent renegotiation of the price once a bid has been offered. In contrast, when a homeowner sells the property through a real estate agent, the owner is frequently required to attend the preliminary inspection of a listed property each time a new potential buyer asks to visit the home. When selling a home to Katitas, the seller transfers to Katitas all responsibility for any defects, such as leaks, and problems with the water supply and drainage pipes.

The fourth value proposition is for builders. Katitas outsources remodeling to 750 small and medium-sized builders with whom Katitas has established a partnership. Katitas enhances the stability of these builders' businesses because the company gives each builder a specified amount of work that corresponds to the builder's capacity. The opportunity for steady work is valued highly by builders who operate in communities where the local economy is sluggish. Builders are able to operate without having to commit much capital because Katitas provides in bulk the materials, fixtures and other equipment to be used in the remodeling projects. Katitas also helps builders maintain their skills and motivation. Builders are required to use the materials, fixtures and equipment supplied by Katitas. They must also comply with Katitas' work standards. However, the remodeling of a used home is always a unique experience, and one that requires much creativity.

The fifth value proposition is for the local community. By remodeling vacant houses, Katitas contributes directly to solving the problem of vacant homes.

The rural communities (with populations of 50,000 to 300,000) on which Katitas focuses are not the kind of market that attracts the attention of many real estate agents. The majority of houses are not listed with a real estate agent because of the low unit price and the low commissions. The small size of the local housing market means that the supply of newly built houses is limited. With the value proposition of remodeled pre-owned homes, Katitas has found new opportunities in such communities.

Unique Value Chain

Katitas' value chain is unique in its purchasing, construction management, and sales activities. The company most ensure that its appraisals are accurate, and correctly determine the home's purchase price. Otherwise, Katitas will have to spend more than expected on the home's remodeling. This would result in lower profitability for the company. Without proper construction management, Katitas could not successfully achieve both cost control and customer satisfaction. Without an effective approach to sales, Katitas would not

be able to sell its remodeled pre-owned houses (each of which is unique) within a fixed period of time and at a reasonable price.

Purchase

Katitas has two channels for procuring used homes. One channel comprises more than 100 branches in rural cities scattered throughout Japan, and homeowners who want to sell their homes are encouraged to contact a Katitas' branch office directly. The other channel consists of a network of "Core Agents," i.e. small- and medium-sized real estate agents operating in a quasi-franchise relationship with Katitas. In the fiscal year 2016, more than 30% of the homes were purchased directly from homeowners rather than through real estate agents. In order to increase direct purchases, Katitas aggressively runs TV commercials in select local markets, intentionally avoiding Japan's three largest metropolitan areas (Tokyo, Osaka, and Nagoya). Through the active use of TV ads, Katitas aims to reinforce the company's brand image: "Katitas—The first choice for anyone wanting to sell a home." Katitas positions itself as a trusted and reliable partner of homeowners. Anyone interested in selling a residential property is encouraged to contact Katitas directly. (In a survey conducted by Search Light in May 2017, survey respondents were asked, "Which company do you think of when you want to sell a house?" Katitas was ranked No. 1 as a buyer of used houses in unaided recall, placing above large real estate agents like Mitsui Fudosan Realty.)

A home inspection and appraisal are crucial for determining the right contract price for a home and minimizing unexpected renovation expenses. Costs would increase and the renovation work would overrun the work schedule if evidence of degradation, disrepair, or termites are discovered at a later date. If structural reforms later on prove to be more difficult than expected, or if there are any oversights regarding structural issues, this could cause the home remodeling project to exceed the budget, or delay the schedule. Katitas requires the presence of three parties: 1) Katitas employees, who conduct the appraisal to determine the home's value; 2) the builder, who determines the expenses that will be incurred in the home's remodeling and assesses the flexibility of the building's structure; and 3) the contractor, who inspects the property for termite damage. All three must be present at the time of the home inspection and appraisal. For Katitas, this practice has led to significant reductions in both the number of renovations that run over budget and the number of home remodeling projects that require an extension of the work schedule.

The real estate markets in rural communities are less liquid than those in urban locales, and it is difficult to set a home contract price using the local market as a reference. That said, Katitas has been focusing on small and medium-sized cities in rural locations, and the company has worked hard to develop a deeper understanding of these rural real estate markets. The majority of branch managers are locally hired individuals who possess extensive knowledge about the local real estate market. Area managers, who oversee three to eight branches and understand market trends from a boarder perspective, back up the branch managers, providing a double-check of the home's contract price. Katitas transfers its personnel between the company's branches, but even when individuals are reassigned to different posts the company makes sure that either the branch manager or the area manager has extensive knowledge about the local market. The ability to set an appropriate price for its renovated homes helps Katitas achieve high profitability.

Remodeling planning

Katitas sets the sales price first, and then determines the upper limit for remodeling expenses. Katitas designs the remodeling plan, staying within the limits of its budget.

Katitas designs a remodeling plan by incorporating renovations that contribute to a "safe, clean, and comfortable" living environment. The company does not try to add value by using expensive materials or installing high-end fixtures.

Remodeling

Katitas outsources the remodeling work to its 750 "partner" builders. In order to realize a uniform level of quality and control expenses, Katitas shares its "Standard Specifications" with the builders. This document contains the specifications for each work item (the walls, floors, and the roof, for example). In accordance with

these standard specifications, remodeling will be conducted for each house based on the "Remodeling Guidelines," which builders sign before the works start.

Katitas purchases materials, fixtures, and large items like kitchen equipment and bath tubs directly from manufacturers and wholesalers, and provides these to the builders. Katitas can take advantage of volume discounts through the centralized purchasing of such materials, fixtures and other items. This also reduces remodeling costs by lessening the builders' operating capital.

As a result of these various arrangements, Katitas can finish the remodeling of a home in 1.5 months on average.

Sales of remodeled homes

Katitas contacts potential customers who have shown interest in the past. The company also actively lists properties on its website. The company frequently provides detailed information and updates on its homepage regarding houses that are in the process of being remodeled. The sharing of such information results in quick sales. Even pictures showing the space beneath the floor and other work in progress are posted in order to communicate Katitas' policy on remodeling. Customers can compare "Before & After" photos of the remodeled home. Detailed information about fixtures and other items is provided so that viewers can feel as if they are visiting the property. This information is periodically updated as the remodeling project makes a progress. These posting are conducted in accordance with the company's "Guidelines for Internet Postings," which is about 100 pages long. A sales representative from one of the company's branches takes pictures of a real estate property and writes some comments. A designated person at the headquarters checks the quality of postings periodically, and provides instructions on how to improve the postings. In fiscal year 2016, about 30 percent of sales contracts were signed before renovations had been completed. Many companies that provide remodeling services usually advertise renovated homes after all the remodeling work has been completed. In the past, Katitas used to rely on printed advertisements that showed completely renovated homes. The company then decided to reduce its reliance on newspaper inserts and flyers, and began expanding online advertising. By switching its main focus to online advertising, Katitas has been able to significantly reduce its advertising expenses.

Marketing

The sales representatives at Katitas' branch offices visit real estate agents and speak to the neighbors of a given property. They conducting interviews to gain a better understanding of customer needs.

Overall management

When a sales contract is going to be signed for a renovated residential property, a standard format email is sent to the top management team. The email message contains the following information: the sales price, the inventory turnover period, and the amount of profit. Based on this input, the top management asks the sales representative about the customer and why it took so long to sell the remodeled home. Top management's objective is to clarify the opportunities and risks being faced by sales representatives working in the field.

Katitas connects all its branch offices through an intranet computer network. The company holds a "Morning Meeting" once a week for one hour. All the company's branches participate in the meeting, which is convened online. During the meeting, the company's executives share information regarding changes in the Katitas' internal rules. Company officials discuss noteworthy matters. Top management shares examples of both best practices and failures, and then presents awards to branches that have achieved a strong performance. After the Morning Meeting, each employee is asked to fill out a questionnaire. Company officials evaluate the efficiency of its communications, listen to the requests of staff members, and answer questions. Afterward, top management reads all the questionnaires that have been filled out by staff members, and provides direct responses to their questions.

Human resources management

The same person is in charge of purchasing, remodeling, and reselling a single real estate property. Under such an approach, the opportunity to specialize in a single activity is sacrificed. However, Katitas is

able to minimize the loss of information about a particular property. (Information is lost as a project changes hands if different people take over the project as it evolves.) Having one person handle a real estate project from the initial purchase of the home through its remodeling and resale enables Katitas to maintain the high quality of its operations. Furthermore, because individual employees are held personally responsible for realizing the sale of the remodeled home that they had originally purchased from the homeowner, they are less likely to buy houses that would be difficult to remodel and resell.

Katitas' reward system is designed to: (1) achieve "the alignment of the company's interests and the individual's interests"; and (2) promote "sales activities that are well coordinated throughout the organization, rather than encourage various individual-led initiatives."

Fit among Activities

Katitas made four choices that are central to its competitive strategy: (1) The choice of product breadth (old, single-family homes in rural areas); (2) the choice of price range (a low price); (3) the choice of a remodeling policy ("safe, clean, and comfortable" living environments); and (4) the choice of the key performance indicator (inventory turnover). The KPI measures the efficiency and effectiveness of a business. In order to transform old houses in rural areas, Katitas has to remodel them and make them "safe, clean, and comfortable" living environments. The company must be able to sell these remodeled homes at a low price. In order to lower its procurement and sales costs for pre-owned homes in rural areas, Katitas works to improve customer recognition by utilizing TV ads, which are less expensive outside of Japan's large metropolitan areas. The company must also collect real estate market information from "partner" real estate agents who operate in rural areas, and make available online information on specific homes. Katitas is able to remodel homes at a low cost while ensuring good quality by: (1) arranging partnerships with builders in rural areas; (2) utilizing "Standard Specifications" and the company's "Guidelines for Remodeling"; and (3) supplying builders with centrally procured materials, fixtures and other equipment for all of the company's remodeling projects. Finally, in order to improve inventory turnover, Katitas maximizes the efficiency of its operations (specifically, the purchase, renovation and resale of pre-owned homes) by making one person responsible for the successful completion of all three of these operations for a single home. Furthermore, individuals who succeed in decreasing long-term stock are rewarded. (Please refer to KATITAS CO., LTD's activity system map, which appears at the end of this report.)

Innovation that Enabled Strategy

- Has created a fourth residential option (i.e. newly renovated pre-owned homes), targeting people who live in rural areas and do not own homes. Before that, options had been limited to newly built homes, pre-owned homes, or apartments.
- Has created a system by which to control the quality and cost of remodeling used homes. (The refurbishment of a home is a complicated project, and each home remodeling project is unique.)

Trade-offs

- Does not buy and remodel homes in metropolitan areas, such as Tokyo's 23 wards and Central Osaka. Although metropolitan areas have large populations and the residential housing market in those areas includes many pre-owned homes, the competition is intense. Any value that can be added by remodeling a home is not significant, considering the extremely expensive price of land. Customers in such urban areas would require even higher quality for both customer service and home renovations, and catering to the needs of such customers would drive up renovation costs and other costs.
- Does not enter the high-end segment, where customer needs are different from the needs of Katitas' target

customers. High-end customers would not be satisfied with the kind of materials, fixtures and equipment that Katitas centrally procures.

- Does not target used apartment units. It is difficult to add value to an apartment building by remodeling the apartments, simply because there is a limit to the renovations that can be done. Moreover, there is a low barrier to entry and intense competition. The ample supply of apartments makes for a liquid market. In such a market, it is difficult to set a higher price.
- Does not offer remodeling services only (without the ownership and resale of the property).
- Does not expand business by opening more branches because additional branches would increase fixed costs. Rather, Katitas expands its business by increasing its staff.
- Does not customize renovations, as this would increase the likelihood of work schedule disruptions, cancellations, and customer dissatisfaction in the event that renovations do not meet the customer's expectations.
- Does not undertake extensive remodeling. Katitas aims to create "safe, clean, and comfortable" living environments. The company does not offer a sophisticated design and special or unique features. Katitas does not try to make the home "new" again by replacing all the materials, fixtures and other equipment.

Consistency of Strategy over Time

The consistency of Katitas' competitive strategy is its focus on the purchase, renovation and resale of pre-owned single family homes in rural areas, and its commitment to making these homes available at a low price (the 10 million yen to 15 million yen price range).

In 1998, the amendment of the Civil Execution Act made the procurement of auction property easier. Yasuragi Co., Ltd., the predecessor of Katitas Co., Ltd, started purchasing, remodeling and reselling used, single-family homes. This business grew in rural areas, where there was less competition.

In 2012, a private equity investment fund, Advantage Partners LLP, acquired Yasuragi, Co., Ltd., which became a wholly owned subsidiary of Nihon Jutaku Saisei Co., Ltd., a holding company created by Advantage Partners. Upon the acquisition, Advantage Partners examined Yasuragi's competitive strategy and decided to maintain the commitment to the company's existing strategy. A plan to enter a higher-end segment was considered, but later rejected for being inconsistent with the activity system in place.

Katitis has maintained Yasuragi's original strategy, but switched its procurement route for pre-owned homes from auctions to direct purchase transactions with homeowners. Changes in the market are what prompted this switch in the company's inventory procurement strategy. The number of auction properties peaked in 2009. There was a surge in supply during the economic downturn that followed the global financial crisis, which started in 2008. However, when the SME Financing Facilitation Act came into force in December 2009, the supply of auction properties declined because the law required banks to make concessions on the repayment of loans when requested by small and medium-sized companies. Meanwhile, from about 2010, there appeared new entrants (small-scale competitors) who began trading in auction properties, and this pushed up the price of auction properties. The company has responded by switching its procurement channel from auctions to direct purchases from homeowners. Then, in 2013, the company changed its name from Yasuragi to Katitas, and began actively investing in TV commercials to raise brand awareness of Katitas as a buyer of pre-owned houses. About 90% of the company's inventory was procured from auctions in 2012. By 2016, 90% of Katitas' pre-owned homes had been purchased directly from homeowners.

Katitas has also changed its sales activities. In 2013, Katitas made online marketing its primary sales activity. Newly added activities include the posting of property information on real estate portal sites and on the company's homepage. Before 2013, Katitas relied primarily on flyers inserted in newspapers once a

remodeling project had been completed. Katitas employees also made sales calls to people who had attended the company's sales events. Sales grew from 2,415 houses in 2012 to 3,451 houses in 2016, marking a 140% increase over a four-year period. In contrast, online sales increased by 630% over the same period.

Profitability

Both the five-year average of the return on invested capital (ROIC) and the return on sales (ROS) exceed the industry average, and the ROS exceeds the industry average by a wide margin. (Profitability analysis was conducted by PwC Japan.)

Return on invested capital (ROIC) (Unit=percentage point)

Difference from industry average					
5Yrs Avg.	2012	2013	2014	2015	2016
1.1 %P	-5.0 %P	-4.4 %P	-3.6 %P	5.0 %P	10.2 %P

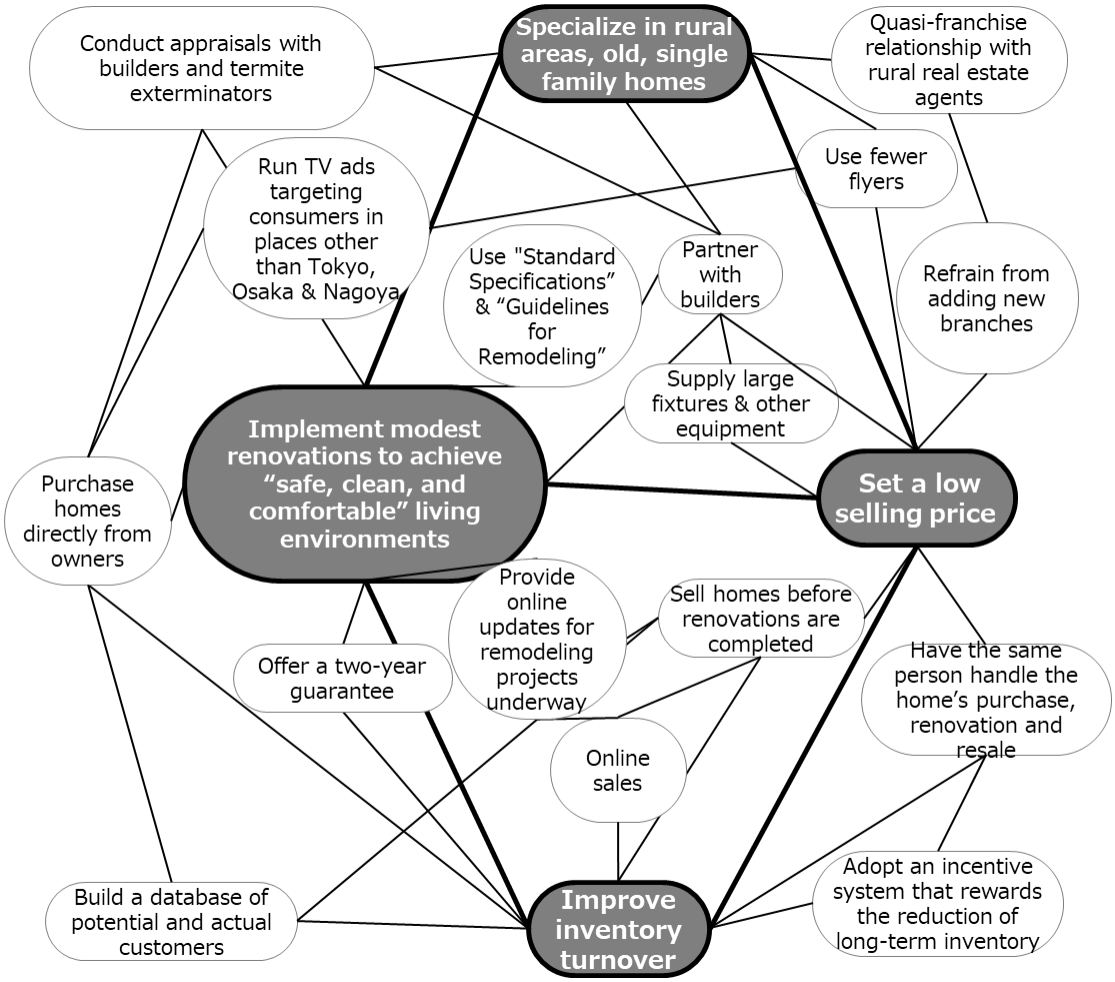
Inter quartile range (IQR) = 1.3 %P
Return on invested capital = Operating income / Average invested capital

Return on sales (ROS) (Unit=percentage point)

Difference from industry average					
5Yrs Avg.	2012	2013	2014	2015	2016
24.1 %P	11.4 %P	15.0 %P	13.6 %P	39.5 %P	29.3 %P

IQR = 1.0 %P
Return on sales =Operating income / Net sales

Activity System Map of KATITAS CO., LTD



Selection Rationale (Recipients are addressed in no particular order):

Net Protections, Inc.

Net Protections is a pioneer and the leading provider of a deferred payment service. The company's deferred payment service allows manufacturers to outsource the deferred payment service option offered to customers making purchases via their online sales channel. Net Protections' deferred payment service also helps small online sellers increase their sales. Net Protections reduces its own risk of delinquent accounts (or more precisely, the risk of shoppers not paying their invoices) by providing small loans to vast numbers of shoppers.

Industry Background

In Japan, payment methods for non-face-to-face shopping purchases include: credit card payments, payments with prepaid cards, cash on delivery (COD), advance payment (i.e. bank transfers and payment at convenience stores), and deferred payment (i.e. bank transfers and payment at convenience stores). In addition to these methods, the growing popularity of online shopping has prompted the introduction of other new settlement services, such as the online payments system PayPal. Increased online shopping from smartphones has spawned new settlement services that involve fewer steps and often do not require typing in credit card information to check out of the shopping cart. Shoppers register as members of their service by providing their name, address, telephone number, and, so often the case, credit card information at the time of registration.

Net Protections is the pioneer of deferred payment services in Japan. The company launched its own service in 2002. Transactions on a value basis exceeded 140 billion yen, and more than 30 million people were using Net Protections' deferred payment service in fiscal year 2016. Since its start, more than 100 million people have used the company's service. As of January 2016, 62% of the top 247 [3] online shopping companies had introduced deferred payment as one of the payment options. Net Protections' service was being utilized by 64% of Japan's online shopping companies, and Net Protections held the largest market share in the industry, according to a company survey.

Unique Value Proposition

It was Net Protections' vision to "build a payment settlement service that is hassle-free for all stakeholders and minimizes credit risk." The company provides two kinds of deferred payment services: (1) One service extended to mail-order companies and online shopping businesses that sell to individuals (BtoC); and (2) another service that caters to the corporate market (BtoB).

How does Net Protections' deferred payment service work? If operators of mail-order or online shopping sites (hereafter, sellers) adopt Net Protections' deferred payment service as one of the available payment methods and shoppers select this payment option, Net Protections will extend credit to the shopper, and request only the individual's name, address, telephone number, and e-mail address. Net Protections conducts an automatic credit evaluation, based on the company's accumulated transaction data, and promptly notifies shoppers whether they have been approved for credit. (Net Protections does not rely on data provided by credit information agencies.) The company can complete its credit evaluation within 5 to 10 minutes after receiving the transaction information. Net Protections is able to conduct a credit evaluation 24 hours a day, 365 days a year. Even in the event that a more detailed credit analysis is required, the company can let the seller know the results of the in-house credit evaluation within two hours because there is an hourly cutoff time for credit evaluations every hour between 10 a.m. and 5 p.m. on business days.

Net Protections controls credit risk by extending a low credit limit to numerous shoppers. The company

[3] From a ranking of the top 300 companies with the largest sales, reported by the newspaper Tsuhan Shinbun (August 4, 2016), "The 66th Mail-Order and Correspondence Course Sales Ranking." The 247 companies exclude companies that sell household appliances and luxury brands from the top 300 ranking.

sets a monthly credit limit of 54,000 yen (US$490) per shopper. It is easy for shoppers to start using Net Protections' service because Net Protections is willing to provide credit up to 54,000 yen to individuals who have no history of using the company's service.

After the shopper gets approved for credit from Net Protections, the seller ships the merchandise to the shopper, and sends Net Protections the invoice number. The next day, Net Protections send an invoice to the shopper [4]. After confirming that the merchandise has been delivered to the shopper, Net Protections pays the invoice to the seller within 5 business days in the shortest case, regardless of whether the shopper has sent a payment to Net Protections. The company makes a lump-sum payment to sellers weekly, twice a month, and once a month. Within two weeks after an invoice has been issued, shoppers send their payment to Net Protections, either through a convenience store or a bank transfer. Shoppers can arrange payment to Net Protections at a convenience store free-of-charge. For bank transfers, however, they must pay the bank a transaction fee.

Seventy-five percent of the Net Protections BtoC service customers are female. In terms of age, customers 35-45 comprise the largest share (27%). Next are customers aged 45-55 (25%), followed by those who are 25-35 (18%). In terms of online shopping device usage, 51% used PCs, while 49% used smartphones and tablets (2016). Net Protections has three target customers. The first is customers who want to pay after receiving their merchandise. The majority of these customers are female shoppers in their 50s and above. The second is customers who would rather not use a credit card for online shopping due to security concerns. Especially when buying from new sellers, shoppers prefer to use the deferred payment option rather than their credit card. According to a survey conducted by Net Protections, one out of five shoppers (or 20.4% of respondents) preferred deferred payment. [5] The third is individuals who do not have a credit card, are too young, or have had their credit card suspended. Net Protections makes it possible for these customers to do online shopping after completing a few easy steps. Shoppers can enjoy Net Protections' service for free, and they even receive points that can be exchanged for merchandise from a specified website or can be used to enroll in a competition for prizes. Compare this with the cash-on-delivery (COD) payment option, which often comes with a service fee and the psychological burden of having to prepare cash and be at home at the time of delivery.

Net Protections' other main customer is sellers (i.e. mail-order and e-commerce site operators). The first value proposition is the reduction of costs for deferred payment services. Net Protections eliminates the risk of delinquent accounts for sellers because it takes over the entire credit risk once it has approved a shopper for credit. The sellers are freed from all activities related to deferred payments, such as credit evaluations, the issuance of invoices and the collection of payments.

The second value proposition to sellers is an increase in sales. Introduction of the deferred payment option contributes to a seller's acquisition of new customers. It has already been said that one out of five shoppers prefer deferred payments when buying from new sellers. In the same survey, respondents indicated that if the deferred payment option is not available, 30% said that they would refrain from shopping, while 46% said they would go to other e-commerce sites.

The third is service quality. The main customers of Net Protections' deferred payment service are manufacturers who operate e-commerce sites to sell their own products and brick-and-mortar retailers who are expanding their online sales. Some have begun outsourcing the deferred payment service, while others are newly adding deferred payment as an option. Manufacturers and retailers who outsource deferred payment services often ask that the service be customized. They make many very specific requests so as not to inconvenience shoppers. Net Protections can satisfy such customers.

The fourth is the service's ease of introduction and ease of use. Sellers can start using Net Protections' service without much effort. Sellers have to notify Net Protections of the shopper's personal information (name,

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[4] Sellers can choose to enclose the invoice prepared by Net Protections in the package with the merchandise.

[5] Net Protections conducted online research, surveying 2,065 people nationwide. (Respondents ranged from teenagers to people in their 50s.) The survey was conducted on March 25 and March 26, 2016.

addresses, telephone number, and e-mail address), the merchandise that has been purchased, and the invoice number. In most cases, however, it is not necessary for sellers to develop new IT systems to automate these processes because Net Protections' service can operate with the 90+ systems that e-commerce operators use (e.g. the shopping cart, order management, and e-commerce construction package systems). Sellers can start using Net Protections' service in as soon as ten business days after Net Protections has received the application. Net Protections' fee structure is: (1) an invoice issuance charge; (2) a fixed monthly service charge; and (3) a commission (calculated as a percentage of seller's proceeds from monthly transactions). These fees are packaged in various combinations, taking into account the size of the seller's business.

Net Protections' BtoB service provides high value in industries where numerous customers exist. One of the examples is Japan's ramen noodle restaurants industry, where self-employed restaurant owners with only one shop form the majority. Sellers to this industry, which include noodle manufacturers and frozen food manufacturers, had been handling the accounts receivable owed from numerous customers by themselves. Net Protections' service can deal with face-to-face, online, mail-order, auto-renewable subscriptions, and pay-per-use transactions. After receiving the name of the buyer's company, the address, the telephone number, the e-mail address, and the transaction information, Net Protections will approve the extension of credit within 5 or 10 minutes. In the case that a more detailed credit analysis is required, Net Protections notifies the applicant (the seller) about the results of the credit evaluation within two hours if the application is made during business hours. Buyers do not need to take any additional actions. After receiving a monthly invoice issued by the seller, which has actually been prepared by Net Protections, the buyer is asked to pay the invoice within 30 days. The monthly credit limit per buyer is between 300,000 yen and 3 million yen. The value proposition in the BtoB segment is the same as the one in the BtoC segment, as explained above: control credit risk by providing small loans to numerous buyers; ensure the ease-of-use for buyers; make sure that sellers do not need to develop a new system to start using Net Protections' service; transfer the entire credit risk to Net Protections; entrust all the activities related to the deferred payment service to Net Protections. The profit model is also the same: charge only the sellers. The sellers are asked to pay a fixed monthly fee, a service fee that is proportional to the monthly transaction value, and an invoice issuance fee.

The fifth value proposition is the support that the service provides as a social infrastructure. Net Protections' deferred payment service helps small companies and self-employed individuals, both as buyers and sellers, deal with credit, which is the first obstacle encountered at the start of any new trading transaction.

Unique Value Chain

Net Protections designs its value chain based on the corporate philosophy: "Aim to develop a payment system that is hassle-free for all stakeholders and minimizes credit risk" and provide "the most versatile settlement service with the highest service quality." Unique human resources management activities support the entire value chain. Below is an explanation about the value chain for a BtoC service, NP Atobarai, the company's deferred payment system with the largest contribution to sales. The value chain for NP Kakebarai, a BtoB service, is designed in accordance with the same philosophy, and is similar to the value chain for NP Atobarai.

Credit evaluations

Net Protections' credit policy is "to give the benefit of the doubt." The company extends credit based on limited information—the shopper's name, address, telephone number, email address, and the merchandise purchased. When a shopper does not have a credit record with Net Protections, the company always extends credit. Only those shoppers who hit the credit ceiling and anyone who has an overdue bill will be rejected. In this way, Net Protections aggressively takes on credit risk and accumulates credit information. By keeping only those shoppers who make their payments on time, the company reduces its long-term credit risk. (Net Protections calls this process "data cleansing.") The company also evens out its credit risk and operating costs by increasing the volume and value of transactions for the vast number of small loans extended.

Net Protections primarily conducts automatic credit evaluations using a computerized system that operates 24 hours a day, 365 days a year. A small percentage of these credit evaluations (about 5,000 cases a

day) require a more detailed credit analysis, which is conducted manually. The more shoppers that can be provided with credit, the larger the number of shoppers will who be able to take advantage of this deferred payment service. The result is increased sales for both the sellers and Net Protections.

Invoice issuance and payment collection

Net Protections has an automatic system for reissuing invoices and sending polite reminder emails. The communication takes a soft approach. By not giving a bad impression, the company is able to consistently achieve a high recovery rate. Net Protection rarely makes telephone calls or personal visits to customers for the collection of overdue payments.

Call center

Net Protections outsources call center operations, where inquiries from shoppers and sellers are answered. A response manual is provided to the call center's staff members. However, when unusual inquiries are made, callers will be transferred to a Net Protections' employee, who will provide a response that is consistent with the company's policies, the knowledge of which employees already share. The center has ten or fewer employees, who are assigned to handle the more than 30,000 inquiries for 3 million transactions.

Sales and marketing

In order to reach potential customers (sellers), Net Protections uses both online marketing (web-based advertisements) and offline marketing (exhibitions). These operations are outsourced to advertising agencies and event planning companies. Net Protections' employees focus on plan development and the management of these outside vendors. In order to cultivate potential customers, the company uses marketing automation tools to send emails and alerts about customers that are ready to be approached. The actual operations are handled by an outside marketing service provider who works in-house. Business negotiations with small and medium-sized customers are undertaken by the resident marketing service provider. Meanwhile, Net Protections' employees focus on large customers; address their more complicated requests; manage the advertising agencies and event planning companies; and systematize the sales process, which consists of the development and standardization of sales tools and educational programs.

System design, development, and maintenance

Net Protections has its employees focus on the planning and development of information systems for services such as credit evaluations and invoice management; as well as systems for improving operational efficiency, such as sales support tools and the customer relationship management systems that are used for sales and call center activities. Activities other than planning are outsourced to system integrators.

General management

Net Protections' corporate philosophy is to "create innovations that will become the norm in the future." The company's mission is "to be the kind of company that can think outside the box, one that can conceive of and provide new ubiquitous systems for Society."

The purpose of Net Protections' general management is to "develop an organization that can design services from a holistic perspective, not a functional perspective." For example, if its sales force were to optimize its function (by single-mindedly pursuing its own goals), this could increase the company's credit risk and costs. If too much customization is accepted for the sake of customer satisfaction, this could result in an increase in inquiries at the service department and deterioration in the quality of operations. If operations division adopts a stance on credit evaluations that is too strict (with the aim of reducing credit risk), it may reduce the number of corporate customers who can introduce the company's service or decrease the number of shoppers who can get credit. This would make the service less convenient for shoppers, and would not help to increase the number of shoppers who use the company's service. It would work against the company's risk management policy of diffusing credit risk over a vast number of small risks. In order to prevent functional optimization, Net Protections makes sure that all employees understand the overall structure of the business, and promotes a policy of human resources management that encourages the development of staff who can work to optimize the whole company rather than only one part of the company.

Human resources management

Net Protections hires mostly new graduates, and during their training impresses upon them the need to optimize the company as a whole. The management encourages them to create new services and improve current services by thinking outside of the box. In the case of mid-career hires, the company gives priority to individuals who can think about what is best for the company as a whole when viewing a given situation.

Net Protections' organization has a functional structure as its base. However, the company allows its employees to request work assignments in other functional areas. Employees can be assigned to multiple departments if they wish. People can be assigned to different departments within the same year. All the employees can volunteer to join a Working Group taskforce. Members of this taskforce are involved in the company's core operations, such as the hiring and training of new graduates, and the development of medium-term business plans. Employees can create a new Working Group if they think one is necessary.

Net Protections puts effort into sharing company-wide its philosophy: "Aim to develop a payment system that is hassle-free for all stakeholders and minimizes credit risk." The company's top management wants to ensure that all decisions will be made in line with this philosophy. (However, the company does encourage individual employees to act on their own initiative.) This philosophy is shared through the company magazine, issued by the Working Group, and through the workshops conducted for new graduates. The philosophy is also incorporated into the design of the recruitment and selection process.

Fit among Activities

Net Protections has made three decisions that are central to its competitive strategy. The first one is its service concept: "Build a payment system that is hassle-free for all stakeholders and minimizes credit risk." The second concept is its credit policy: "Diffuse credit risk over a vast number of small loans." The third is the company's long-term direction: "Improve service quality to ensure sustainability over the long term, and achieve optimization of the whole." All these choices were selected in accordance with the company's philosophy, which is to "create innovations that will become the norm in the future." (Please refer to Net Protections, Inc.'s activity system map, which appears at the end of this report.)

Below, the NP Atobarai's activity system for the BtoC segment is explained as follows. The goal of the company's activity system for its deferred payment service is to realize "a payment system that is hassle-free for all stakeholders and minimizes credit risk." Net Protections undertakes all the activities itself, everything from the issuance of invoices to the collection of overdue payments. It is the company's policy to: (1) Assume the entire credit risk. (2) Extend credit based only on limited information. (3) Conduct credit evaluations quickly and extend credit easily, giving shoppers "the benefit of the doubt." (4) Conduct credit evaluations using a computerized system. Undertaken credit analysis manually to investigate ambiguous cases, and make a quick decision about whether to extend credit. (5) Assure a high probability that credit will be extended. (6) Do not request membership registration. (7) Do not impose any financial burden on shoppers (other than the bank transfer fee that must be paid to banks).

In order to diffuse credit risk over a vast number of small loans, Net Protections has set a monthly credit limit of 54,000 yen per shopper. To increase the number of users and the transaction volume, the company makes it easy for shoppers to start using Net Protections services by: (1) choosing to give credit to first-time users; (2) assuring a high probability that credit will be extended; (3) eliminating membership registration as a requirement for shoppers to use the service; and (4) refraining from imposing a financial burden on shoppers.

In order to realize an improvement of service quality that is sustainable over the long term and achieve overall optimization, Net Protections undertakes the following activities: (1) Automate and use business process outsourcing (BPO) for operations; (2) have employees focus on planning and management; (3) cultivate a workforce of individuals who can work independently and work across functions for long-term optimization; and (4) invest in system improvements and marketing strategy implementation.

Innovation that Enabled Strategy

- A service concept that involves the company aggressively taking over the credit risk of small loans to a vast number of buyers. By improving the ease of use, the company has increased the number of buyers and sellers who use the company's service. (The company improved the ease of use by not requiring membership registration, by giving credit to first-time users up to the credit ceiling, and by extending credit to shoppers again after they have paid off their delinquent accounts.)
- Using machine learning for credit evaluations.
- Develop an IT system that handles nearly all of the settlement service operations.
- Use business process outsourcing (BPO) aggressively. The company designs operations by process rather than function, which has made possible the outsourcing of operations. Consequently, the company outsources sales activities, systems development, and call center operations.

Trade-offs

- Does not require shoppers to register as members. Not requiring membership makes it easier for shoppers to start using Net Protections' service, although this does make it more difficult to identify each shopper, which works against minimizing credit risk. By adding more shoppers to its service, Net Protections can quickly expand its accumulation of credit and shopping data.
- Does not rely on the credit agencies for credit evaluations. Using the data from credit agencies Net Protections would enable Net Protections to lower its credit risk from the outset. However, this would not help the company to accumulate shopping and payment data. Also, reliance the data from credit agencies would make it difficult to extend credit to individuals with lower credit ratings.
- Does not allow shoppers to defer payment beyond two weeks. By extending the lending period, Net Protections would be able to provide additional value (i.e. the postponement of the payment), but this would increase the credit risk because it would encourage people to shop without cash on hand. Net Protections aims to provide "a worry-free, safe and comfortable shopping experience." The company is not interested in extending loans.
- Does not conduct credit evaluations relying solely on a computerized system to provide real-time credit authorization. Indeed, relying 100% on an electronic system to immediately provide the results of the credit evaluation would improve the efficiency of operations for both sellers and Net Protections. However, relying exclusively on an automatic credit evaluation process would result in all ambiguous cases being accepted or rejected. There would always be a percentage of cases that are ambiguous, and an across-the-board decision to accept all such cases would increase the company's credit risk. If all ambiguous cases were to be rejected, this would cause some shoppers to form a negative impression of Net Protections' deferred payment service. For this reason, Net Protections has the credit analysis conducted manually, after which a quick decision is made about whether to extend credit for each individual ambiguous case.
- Does not fall into a function-based organization. Too strong an orientation toward functions gets in the way of a holistic view, which is necessary for the payment settlement services.
- Does not focus solely on skill sets in the recruitment of mid-career hires. Does not hire individuals who cannot work with people engaged in other functions, or who do not possess a long-term perspective, or whose mindset and behavior are restricted to a single function, even if that person has a high-level skill set.
- Does not pursue shoppers who are happy to pay with credit cards. People who shop with credit cards most likely do not have a strong desire to make deferred payments, as they are already enjoying the convenience of real-time settlement. For this reason, they are less likely to start using the deferred payment option.
- Does not introduce a new service brand for the provision of OEM services in principle. The provision of

OEM services would grow the business, but it would also require separate user touchpoints, such as invoices and call centers. This would increase the company's operational costs.

Consistency of Strategy over Time

Net Protections was founded in January 2000. The company introduced "NP Atobarai," a deferred payment service for mail-order shoppers that did not require membership registration. In April 2011, the company launched "NP Kigyokan Kessai," a deferred payment service for the BtoB segment. Like NP Atobarai, this service had no membership registration requirement. In July 2015, the company debuted "NP Atobarai air," a BtoC deferred payment service for service providers who visit customers at their homes (i.e. like moving companies and food home delivery services). In June 2017, the company introduced "atone" (pronounced a-to-ne), a new BtoC deferred payment service that requires membership registration, but allows shoppers to settle the bill with a lump-sum payment every month. The once-a-month settlement of payments makes the deferred payment service more convenient for both sellers and shoppers.

Since the service was launched in the year 2000, Net Protections has consistently maintained the core of its competitive strategy—starting with NP Atobarai, and continuing with the introduction of NP Kakebarai (its BtoB deferred payment service). The core components of this strategy are: (1) Aggressively take on all the credit risk, and simultaneously accumulate credit information. Reduce the company's credit risk over the long term by having shoppers with a history of delinquent payments leave the system. (2) Diffuse credit risk and level operating costs by increasing both the volume and value of transactions for the vast number of small loans that constitute the company's credit obligation. (3) Undertake all the activities involved in the settlement service. In other words, do not outsource collections, credit guarantees or any other activities.

Net Protections included both the BtoB and BtoC segments in its growth plan. The company started with the BtoC segment, because there was an evident need for a deferred payments option, especially among customers who had previously used deferred payments for their mail-order purchases and clearly preferred this method of payment. Net Protections knew that taking market share away from credit cards would be difficult. However, recognizing the evident need for such a system, the company decided to focus on demonstrating the feasibility of its service concept and developing its operations. Net Protections entered the BtoB segment next, which proved more difficult. The credit risk in this segment is larger, as the value of each transaction is higher. The operation of such a system is more complicated because customization is required.

Profitability

Both the five-year average return on invested capital and the return on sales exceed the industry average by a wide margin. (Profitability analysis was conducted by PwC Japan.)

Return on invested capital (ROIC) (Unit=percentage point)

Difference from industry average					
5Yrs Avg.	2012	2013	2014	2015	2016
13.9 %P	14.8 %P	24.0 %P	7.6 %P	12.0 %P	9.8 %P

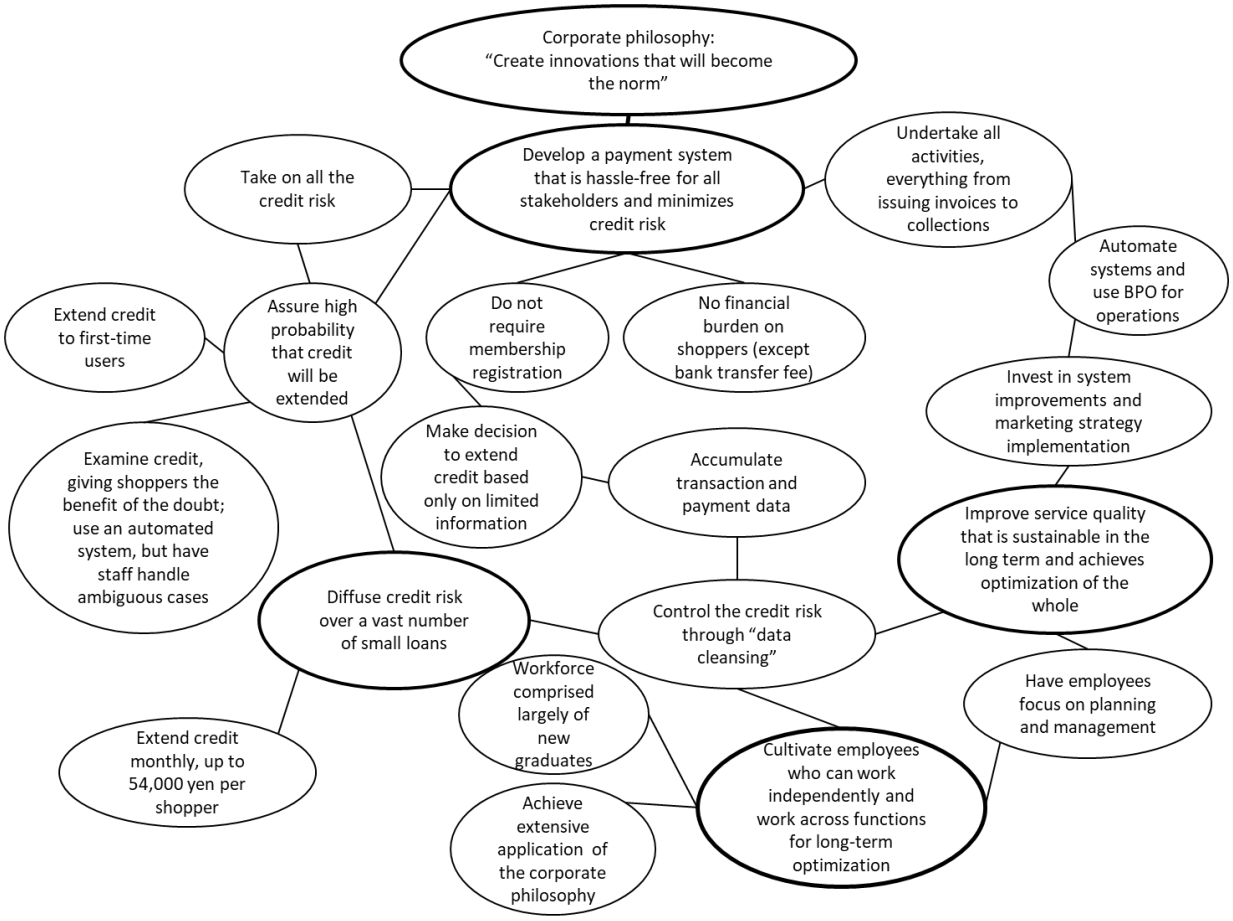
Inter quartile range (IQR) = 4.1 %P
Return on invested capital = Operating income / Average invested capital

Return on sales (ROS) (Unit=percentage point)

Difference from industry average					
5Yrs Avg.	2012	2013	2014	2015	2016
6.2 %P	7.9 %P	9.9 %P	3.1 %P	7.0 %P	6.5 %P

IQR = 0.8 %P
Return on sales =Operating income / Net sales

Activity System Map of Net Protections, Inc.



Selection Rationale (Recipients are addressed in no particular order):

Pro-Ship Incorporated

Pro-Ship has created the packaged software market for fixed assets management, and has sustained its leadership position by targeting large companies that manage complex fixed assets. By undertaking in-house all aspects of the operations (everything from product development to introduction and maintenance services), Pro-Ship achieves superior usability for customers as it pursues business operations centered on packaged software.

General features of the fixed assets management software

Fixed assets management software is used for financial accounting, the payment of taxes, and business management. Financial accounting is subject to changes in the institutional accounting standards, such as J-GAAP and IFRS. J-GAAP has experienced frequent changes—recent examples from the last ten years include the introduction of asset-impairment accounting in 2005, a new lease accounting standard in 2008, accounting for asset retirement obligations in 2010, and prospective amortization in 2011. Those companies that switch to IFRS will need to change the fixed assets management system. The payment of taxes is subject to changes in national and local taxes. In 2007, the national tax abolished the residual value for fixed assets and changed the rules of amortization in 2007 (a 250% declining balance method from 2007 to 2012; a 200% declining method from 2012 onward). The depreciable assets tax in the local tax code requires conformity with the local tax portal system—eLTAX. Finally, management accounting began putting greater emphasis on return on assets (ROA) analysis and the transparency of financial reporting, in response to the Ito Report and the Stewardship Code in 2014 and the Corporate Governance Code in 2015. Moreover, there could be mutual effects between different areas such as changes in the reporting of tax effects under tax-effect accounting. Developers of fixed assets management software must understand the mutual effects and reflect them in the software. It is not easy to update the software in time for the introduction of changes in institutional accounting standards while maintaining compatibility with integrated business process management systems, such as enterprise resource planning (ERP) packages.

Pro-Ship is the leader in fixed assets management software, with more than 4,500 Japanese companies on its client list.

Unique Value Proposition

Pro-Ship's target customers are large corporations. The company develops packaged software for fixed assets management and provides its customers with introduction services. The company does not target small and medium-sized companies, which far exceed large corporations in terms of the actual number of companies. Pro-ship does not expand the scope of business beyond fixed assets management.

For most companies, fixed assets management software does not increase sales. In a sense, it is quite an inconspicuous product. Still, it requires highly specialized expertise, considerable effort, and a substantial financial investment to develop software that can respond to the changes in institutional accounting standards mentioned above.

The size of the market for fixed assets software is much smaller than the market for ERP software. Many people in the software industry believed that it would be impossible to develop a business focused entirely on fixed assets management software. At the same time, fixed assets management software has a high barrier to entry, as it requires specialized knowledge and frequent upgrades.

Pro-Ship's target customers are large, publicly listed companies and their group companies. These companies tend to have extensive fixed assets and operational issues proportional to the amount of fixed assets.

These large companies have a need for sophisticated services that require a high degree of specialization. Also, large companies are able to pay for high value-added services supported by a high level of specialization. In contrast, small and medium-sized companies tend to consider Pro-Ship's products to be too expensive, with an excessively high level of quality.

Pro-Ship enables large companies and their group companies to manage the fixed assets of various business units and overseas subsidiaries with one packaged software. More and more companies want one unified system that can be used group-wide to accelerate the settlement of consolidated accounts and tighten internal control. Pro-Ship's product ProPlus can satisfy this need for a unified system. ProPlus incorporates as a standard feature an amortization calculator, which can be used for filing tax forms in 24 countries. As of April 2017, ProPlus was being used by 113 companies in 17 countries. (The majority of these overseas companies are subsidiaries of Japanese companies.) Competitors focus on the development of industry-specific packages (called "industry templates") for industries like the financial, medical, and automotive industries, with the aim of covering various market segments. For this reason, competitors are unable to provide comprehensive services (i.e. product development, introduction, and maintenance services) like Pro-Ship can.

Although ProPlus is a packaged software, it is updated frequently to respond to changes in institutional accounting standards. It is also customized to meet the client's specific needs. That is to say, clients benefit from the efficiency of packaged software for the needs shared by large companies, while also taking advantage of ProPlus' responsiveness to changes in accounting standards and the option for customization. ERP software, which covers broad operational areas, does not offer such advantages. Pro-Ship undertakes both on-premises installation (the packaged software is installed on the client's servers and network equipment) as well as cloud-based installation (the application is installed in the cloud, which clients can access and use through the Internet).

Pro-Ship charges for licensing fees and introduction fees depending on the number of users and the amount of fixed assets at the client company. This pricing system charges larger companies with a larger amount of fixes assets higher fees, because these are the clients who benefit most. In addition, the company always concludes maintenance contracts with clients, and Pro-Ship is able to turn its business transactions with these new clients into contracts for recurring services. On top of this, the company ensures the value of the long-term validity of its products by maintaining responsiveness to accounting and tax system changes, achieved through the provision of intimate maintenance services. As a result, leading companies in most industries use ProPlus. The cutting-edge needs of these good customers serve as a management resource for Pro-Ship, fueling software development and contributing to the acquisition and maintenance of specialized expertise. Such expertise makes it difficult for competitors to challenge Pro-Ship's dominant position in the market.

Unique Value Chain

Pro-Ship, by maintaining a clear focus on fixed assets management, outcompetes rivals with its ability to provide a quicker and more precise response to the client company's rapidly changing needs. By continually ensuring its client companies' ability to respond to change, Pro-Ship provides a long-term value that does not depreciate. The value chain that supports this value proposition is unique because Pro-Ship conducts in-house the core activities of product development, software introduction services, and maintenance services. The outsourcing of business activities is a common practice in the software industry, and internalizing these activities is sometimes more expensive than outsourcing them. However, by internalizing the entire value chain, Pro-Ship creates a feedback loop, which helps it to gather feedback from the market and incorporate changes in its products and services in a timely manner.

Marketing (Identify the latest market needs and gather information regarding possible upcoming changes to institutional tax and accounting standards)

Pro-Ship's customer base consists largely of the leading companies from every industry and every

business field, companies that require sophisticated solutions and have specific needs pertaining to fixed assets management. As part of its efforts to identify customers' needs, Pro-Ship collects information about business requirements, computer system requirements, and any developments regarding changes to institutional accounting standards in Japan and other countries. Client companies provide feedback to Pro-Ship, and expect that their needs will be incorporated into the standard features of the company's packaged software and standard services, ultimately producing beneficial results for their own companies. They do not hesitate to provide feedback because, as leading companies, they put value on contributing to other companies through the sharing of their needs and know-how. Such input from leading companies is a unique asset for Pro-Ship (one that would be difficult for competitors to obtain) and one that differentiates it from other companies.

Pro-Ship uses two routes for understanding customer needs. One consists of routine activities, and the other involves a quick-response route. The routine activity route includes listening to customer feedback during business interactions; sampling a few companies and arranging client visits to conduct interviews afterward; and sending surveys by direct mail. This feedback is confirmed by conducting comprehensive surveys during User Group meetings, convened several times a year. As for the quick-response route, Pro-Ship calls for a meeting with the client company's CEO and directors when a company employee, during the course of providing introduction or maintenance services, notices the same "customer need" three or more times. Together they decide if the issue in question should be resolved in future products and services.

Product development: Superior packaged software is designed by drawing on a thorough understanding of the client's business operations. Products must allow for scalability and maintenance. Through its over 40 years' of experience developing packaged software, Pro-Ship has created a proprietary product development process and product framework. In addition to improving the operational functions, Pro-Ship builds into its packaged software a variety of mechanisms (such as redundancies to ensure the efficiency of its introduction services, and a system for collecting the log information required for maintenance services) based on expertise gained through in-house product development, introduction and maintenance services.

Pro-Ship's policy toward technology is to select mature technologies rather than adopt the latest technology. With mature technologies, it is easier for a company to: (1) achieve and maintain the high quality of its products; and (2) attract a sufficient number of individuals with technical expertise (specifically, mid-career software engineers). This is especially true for Pro-Ship's partner software companies.

Pro-Ship upgrades ProPlus three to five times a year in order to respond to changes in tax accounting systems or to enhance functionality. The definition of specifications and the choice of development priorities are centralized in a specialized unit at headquarters. As a result, the company can leverage its broad knowledge, noticing, for example, that it can respond to Hong Kong's tax system without much investment if it combines the specifications for Indonesia's tax system for the declining balance method of amortization with the tax treatment for special depreciation under Malaysia's tax system. Applying such knowledge would be difficult if a company had made the decision to localize the definitions of specifications and product development on a country-by-country basis.

Introduction services

Pro-Ship's customers are large companies that require complicated solutions for fixed assets management and IT systems. Although 80% of the customers use the standard ProPlus product, 20% of these customers require additional development for customization. In order to respond to this need for customization, employees engaged in introduction services must be knowledgeable about business operations, IT systems, and the scalability of ProPlus. Although customers pay additional development costs for customization, Pro-Ship retains the intellectual property rights for the newly developed software. This enables Pro-Ship to utilize the know-how it has gained through customization. The company will not accept a client's order if that client does not agree to allow Pro-Ship to retain the intellectual property rights. This is an unusual practice in the software industry, where the intellectual property that results from development undertaken for customization is usually transferred to the client or an intermediary.

In order to ensure high-quality introduction services, Pro-Ship defines the output for each step of the introduction process (i.e. "documentation and coding standards" and "standards for collecting evidence for testing"). These standards are applied to all introduction projects. Meeting these standards is a milestone for moving the project from the introduction phase to the customer support department, which handles maintenance services. The data recorded in accordance with introduction work procedures upon completion of introduction services helps staff members respond more efficiently to inquiries in the maintenance phase. This approach to the introduction method not only enables the company to achieve high quality, but also facilitates the career development of personnel. At Pro-Ship, engineers with a three-year tenure at the company can lead introduction projects. The industry average is about five years to achieve the same level. The introduction method is revised as needed.

Sales

Pro-Ship's sales activities focus on potential customers who have demonstrated interest by responding to advertisements or attending seminars. To these potential customers, Pro-Ship provides detailed explanations while demonstrating the software using actual equipment at an early stage. The company determines whether the packaged software matches the customer's needs, and drafts proposals that sometimes include additional development work for customization. Although it is the norm within the industry for engineers to accompany the sales staff and provide detailed explanations of product and proposals, Pro-Ship has its sales staff conduct demonstrations and explain proposals in most cases. Sales staff who can respond promptly to questions with detailed explanations and make reference to past projects involving other client companies demonstrates Pro-Ship's high level of specialization and reinforces its brand image as a company with a high degree of expertise.

Maintenance services

Maintenance services are provided to ensure stable operation by customers. These services include responding to inquiries, making software upgrades to accommodate system changes, and conducting an analysis of usage.

Pro-Ship develops a database of the inquiries that customers have made and the answers. By utilizing this database and the support provided by its own system for customer relationship management, the company can respond to 99.7% of inquiries with a preliminary answer within one hour. In the industry, there are cases in which packaged software makers respond to inquiries, while intermediaries answer inquiries for the customized components because they handled the introduction services. This makes the problem-solving process longer and more complicated. Pro-Ship manages a customer database that covers both packaged software and customized components, and undertakes generation management for each client company. This system enables Pro-Ship to respond promptly to customer inquiries.

Pro-Ship always wants to be the first in the industry to release new modules for upgrading the company's software whenever any changes are introduced to institutional accounting standards.

ProPlus keeps a record of the access log and operational log information for maintenance purposes. Through the statistical analysis of this data, Pro-Ship can propose ways to improve system usage regarding issues of which customers may be unaware. Pro-Ship does not wait for customer requests—it proactively makes proposals through its maintenance service, which increases the usage value of its packaged software.

Procurement

Pro-Ship experiences fluctuations in demand. There tends to be a large volume of introduction projects ahead of the implementation of tax and accounting system reforms. Pro-Ship's employees lead the introduction projects, with the employees of the company's business partners participating in some capacity. In the busiest season, business partners' employees comprise more than 40% of the introduction team. In order to ensure quality, Pro-Ship selects business partners who agree with Pro-Ship's strategy, possess a high level of technical expertise, and will contribute their specialized expertise. Partner companies join the projects, forming teams with their own employees. Teams are made up of more experienced members and less experienced members. This enables the less experienced members to upgrade their expertise and helps reduce costs. Pro-Ship has

been working with the same partner companies for 10 or 20 years.

Human resources management

Pro-Ship gives employees in their early stages opportunities to accelerate their career development. Because the development and sale of packaged software is done in-house, employees with the necessary capabilities can take part in introduction projects for large companies, regardless of their length of employment at Pro-Ship.

Pro-Ship aims to create an organization in which management policies and strategies are shared with employees. Amid a healthy level of stress, there is a competitive environment inside the company, with employees learning from one another while experiencing growth, confident in the knowledge that they are contributing to the organization. In order to evaluate the contributions of the individuals who participate in projects, Pro-Ship conducts employee performance reviews. Each and every person, from the CEO to front line employees, are assigned to a position for one year. Eager to make sure that the right person is in the right position at the right time, Pro-Ship will have bosses and their subordinates switch places in some departments every year.

With the aim of continually ensuring that its talented staff members have satisfying work, Pro-Ship offers stratified education training, internal study meetings, and individual meetings with the CEO. The company employs a specialist system, encourages the observation of "No Overtime" days, and recognizes the performance of employees and teams by naming monthly MVPs and giving project awards. In addition, Pro-Ship defines its skill standards and operational process standards to improve productivity.

General management

Pro-Ship manages license fee income, maintenance fee income, and the project cost rate as key performance indicators (KPI) to improving the efficiency of operations. At the right time, Pro-Ship shares these performance indicators with employees to commence new PDCA (plan, do, check, act) cycles.

Fit among Activities

Pro-Ship puts the highest priority on continuously demonstrating a high level of specialized expertise in the area of fixed assets management. This strategic goal is realized by targeting the kind of sophisticated solutions required by large companies, and by providing a comprehensive package of services, comprised of product development, introduction and maintenance services. These three are Pro-Ship's core strategic choices.

In order to continually demonstrate a high level of specialized expertise in the area of fixed assets management, Pro-Ship chose not to develop ERP software. Instead, this focus on fixed assets management has enabled Pro-Ship to optimize all of its operations, and has made it possible for the company to develop a specialty and respond promptly to changes in institutional accounting and tax standards. Other companies that develop ERP software allocate attention and effort to ensuring the integrity of the software. This would result in an organizational structure and business processes that are very different from Pro-Ship's. In order to continually demonstrate its high level of specialized expertise in the area of fixed assets management, Pro-Ship has released a new product that features a responsiveness to changes in the accounting system, marking a first in the industry. The centralization of product development activities at the headquarters and the collection of market information at every touchpoint helps the company to achieve the earliest possible release of a new product. The demonstration of a high level of specialized expertise is not possible without people who possess specialized knowledge. In order to develop people who possess a deep understanding of the clients' business operations and IT technology, Pro-Ship has selected a human resources management system that: (1) utilizes performance-based evaluations; (2) puts a priority on making sure that the right person is in the right place at the right time; (3) gives employees one-year work assignments; and (4) encourages engineers with short tenures at the company to quickly develop their skills and expertise.

In order to respond to the needs of large companies, Pro-Ship keeps up with changes. The company

collects market information at every touchpoint; provides comprehensive services (i.e., product development, introduction, and maintenance services); undertakes sophisticated customization development; and frequently upgrades its standard systems and services. The decision to target large companies makes sense because such companies have a willingness to invest in IT systems. Also, the package software's adoption by these companies has had a positive impact on the company's new customer acquisition.

Through the provision of comprehensive services (specifically, product development, introduction, and maintenance services), Pro-Ship can collect market information at every touchpoint and maintain its responsiveness to changes in the operating environment. Thus, Pro-Ship can continually demonstrate a high level of specialized expertise in the area of fixed assets management, and can respond to the needs of large companies. The provision of comprehensive services that cover product development, introduction, and maintenance include high-level development for customization and the application of know-how developed through customization of the company's packaged software, which is possible because Pro-Ship retains the intellectual property rights for its programs, and takes a proactive approach to maintenance services. These activities are supported by having one person in charge of all processes, from introduction to maintenance services; centralizing product development at the headquarters; and establishing long-term relationships with partner companies. (Please refer to Pro-Ship Incorporated's activity system map, which appears at the end of this report.)

Innovation that Enabled Strategy

- Focuses on the fixed assets management system for large companies. Pro-Ship has differentiated its fixed assets management system from accounting systems by highlighting the difference in the speeds at which these systems can respond to changes in market needs. By uncoupling the fixed assets management system from the other systems, Pro-Ship has been able to specialize in fixed assets management.
- ProPlus is the only fixed assets management system that can be used by multinational companies uniformly across their global operations. The majority of accounting systems and production management systems have achieved a unified system for the company's global operations. With regard to systems for fixed assets management, most multinational corporations have installed separate local packages out of the belief that systems integration is difficult because "different countries have different tax systems." Pro-Ship has selected 24 countries, taking into account the needs of Japanese multinational companies, and has developed features that correspond to the requirements of the tax systems of these countries.
- Employs a unique introduction method. Pro-Ship conducts several hundred introduction projects every year which utilize a proprietary method that is revised periodically according to necessity. Under this method, employees with less tenure at the company lead introduction projects. This approach helps Pro-Ship to quickly upgrade the skills and expertise of its engineers while simultaneously stabilizing the quality of operations.
- Utilizes a unique pricing scheme. When determining the price it will charge its clients, Pro-Ship takes into account the number of users as well as the amount of fixed assets in the client company's possession. This practice of taking into account the amount of fixed assets when setting the price is unique to Pro-Ship.

Trade-offs

- Does not develop an integrated software like ERP.
- Does not target small and medium-sized companies.
- Does not outsource introduction services to an intermediary.

Consistency of Strategy over Time

In 1980, Pro-Ship entered the market for fixed assets management software by introducing FASPAC-I. Since then, Pro-Ship has stayed loyal its original strategy choices: (1) develop in-house fixed assets management software; and (2) undertake direct sales to the target customer—large companies.

Pro-Ship was founded in 1969 as a consulting company. As clients moved toward the computerization of operations, Pro-Ship began offering customized development services for IT systems in 1971. Observing the growing popularity of packaged software in the U.S., a leading market for IT systems, the company released its first packaged software—accounting system software—in 1978. The company had planned to offer a lineup of products: packaged software for accounting, funds management, and fixed assets management. However, Pro-Ship found that the fixed assets management packaged software it introduced in 1981 quickly attracted customers. Although customized development was popular among Japanese companies, Pro-Ship was able to persuade customers that packaged software would be good enough for fixed assets management because there was not much difference among companies in business processing operations, which must conform to tax laws. As the fixed assets management software grew to become the company's strongest-selling product, Pro-Ship redirected the majority of its resources to that product.

Pro-Ship selected large companies as the target customer because only large companies could afford to own general-purpose computers, which cost between several hundred million yen and several billion yen in the 1980s. For this reason, not only Pro-Ship but also the majority of software developers targeted large companies in the 1980s. However, the 1990s saw the downsizing of hardware and the open-sourcing of technologies. Against this backdrop, a market for packaged software for small and medium-sized enterprises (SMEs) was formed. Software developers moved their target to the SME segment. Despite this trend, Pro-Ship has repeatedly chosen not to change its target customer, and has instead maintained its focus on large companies.

Pro-Ship introduced a new product brand, ProPlus, and released the ProPlus Fixed Assets Suite in 1995. This product marks a major shift in skills, because the company switched over to personal computer-based technology for its software, as did many other industry players. The emergence of the packaged software market for SMEs accelerated the influx of new rivals into the market for packaged software development. In the process, packaged software gained broad market recognition. As the number of companies installing ProPlus reached 300, Pro-Ship started being approached with offers from competitors seeking an alliance or partnership with the company. In the industry, whispers could be heard about "informal collaborations" and "quarreling while shaking hands" as competitors discussed the possibility of becoming collaborators. However, Pro-Ship remained firm in its decision to keep the development, introduction and maintenance activities in-house, rather than collaborate with competitors.

As the year 2000 approached, many large Japanese companies began using ERP packaged software like SAP and Oracle (developed by overseas players). Once these companies learned that the fixed assets management components of the ERP packaged software did not meet the needs of Japanese customers, overseas ERP venders approached Pro-Ship about working with them. Pro-Ship provided the standardized interface for Oracle's ERP, so that Oracle Japan could introduce ProPlus to its clients. Still, even under this arrangement, Pro-Ship formed contracts directly with customers, retaining the company's brand name, and had its own staff provide introduction services. Thus, Pro-Ship was able to maintain the core of its strategy. Similar arrangements have been made with other major ERP venders, so that Pro-Ship's fixed assets management system can work well with any accounting system the client may choose.

After 2005, many changes were made to the institutional accounting and tax standards for fixed assets management. Pro-Ship received even more proposals from other companies. Leading system integrators asked Pro-Ship to provide a fixed assets management component for its ERP software, to be supplied on an OEM basis. A large consulting firm offered to provide a sales channel, with an eye toward a capital tie-up. A package vender who targets SMEs proposed the mutual sharing of customers, an arrangement that would allow the

package vender to gain access to the large company segment while enabling Pro-Ship to enter the SME segment. Pro-Ship accepted none of these offers.

Pro-Ship's strategy has always maintained a focus on large companies and fixed assets management, and the company has been continually demonstrating its high level of specialized expertise, developed by undertaking direct sales of its products and services for the entire course of its history.

Profitability

Both the five-year average return on invested capital and return on sales exceed the industry average by a wide margin. (Profitability analysis was conducted by PwC Japan.)

Return on invested capital (ROIC) (Unit=percentage point)

Difference from industry average					
5Yrs Avg.	2012	2013	2014	2015	2016
9.8 %P	9.8 %P	9.7 %P	10.8 %P	7.0 %P	8.9 %P

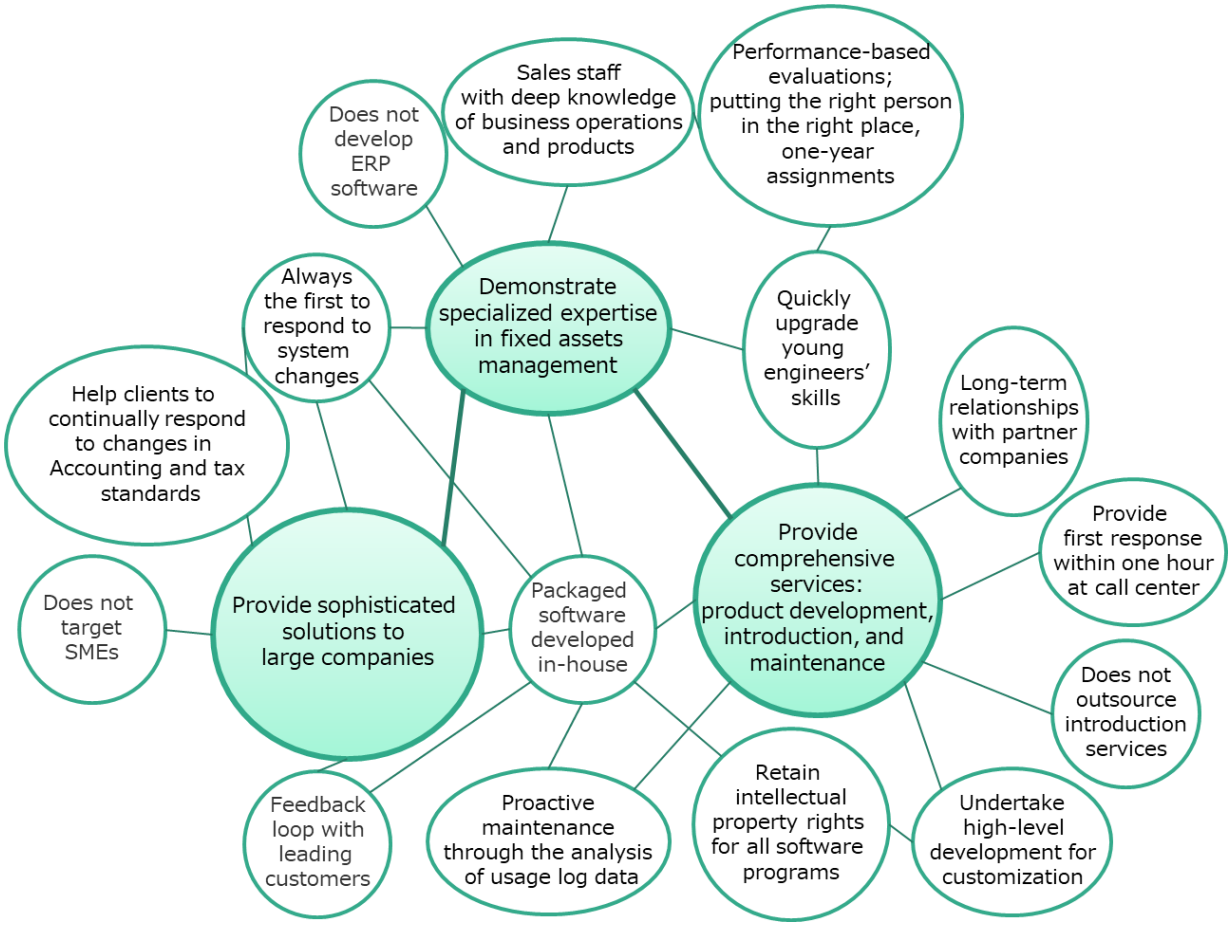
Inter quartile range (IQR) = 9.9 %P
Return on invested capital = Operating income / Average invested capital

Return on sales (ROS) (Unit=percentage point)

Difference from industry average					
5Yrs Avg.	2012	2013	2014	2015	2016
23.5 %P	16.7 %P	20.0 %P	24.2 %P	26.5 %P	25.3 %P

IQR = 12.8 %P
Return on sales =Operating income / Net sales

Activity System Map of Pro-Ship Incorporated



Selection Rationale (Recipients are addressed in no particular order):

QB Net Holdings Co., Ltd.

QB Net Holdings offers a 10-minute haircut service for 1,000 yen (US$9) at its chain of small barbershops ("QB HOUSE shops") in areas with high foot traffic. The unparalleled convenience of the company's services has generated a new pattern of consumer behavior—a quick stop for a haircut during the lunch break or on the way home. Despite competition from followers imitating QB HOUSE's value proposition, the company has achieved a sustained competitive advantage by increasing inimitability through the internalization of various activities, including the training of stylists and improvement of the fit among activities. QB Net's barbershops in overseas markets are showing growth and contributing to profit.

General features of the haircut services in Japan

In Japan, only barbers or beauticians certified by the Minister of Health, Labor and Welfare can provide haircut services because of the public health concerns related to haircutting. Each shop has to be registered as either a barbershop or as a beauty salon. Although these businesses are subject to different laws and regulations, both barbershops and beauty salons alike must meet specified sanitary standards from a public health perspective. Traditionally, barbershops are where men have gone for grooming (haircuts and shaves). Beauty salons are where people go to improve their aesthetic appearance. Barbers can use razors, but there are some limitations regarding the perming of hair. Beauticians, on the other hand, can perm hair, but there are some limitations regarding their use of razors. [6] However, the line separating barbershops and beauty salons is becoming blurred, because barbers have started offering new types of perms (such as the so-called "iron perms," which do not violate the regulations). In order to reflect this reality, perming hair at barbershops and cutting hair at beauty salons became officially permitted in 2015. [7] Still, barbers and beauticians are not allowed to work in the same shop, and beauty salons have some limitations regarding the use of razors.

There are reasons why the barbershop industry has been shrinking. One is that barbers were not providing the kind of hair styles that young customers wanted. Young customers were going to beauty salons to have their hair cut by beauticians. On top of that, in the mid-1990s, middle-aged men, the main customers of barbershops, were visiting barbershops less frequently—they were becoming more frugal after the bursting of the bubble economy in Japan. Meanwhile, the number of beauty salons also showed a continuous declining trend, albeit a gradual one. The number of beauty salons peaked at 145,000 in 1986, remained at the 140,000 level from 2000 onward, and then dropped to 137,000 in 2007. [8] The market size for beauty salons is about 1.6 trillion yen, and barbershops is 700 billion yen, for a combined total of 2.3 trillion yen. Although customer demand remained robust and the industry did not experience a deep dive in sales like other industries experienced during the economic downturn that was triggered by the financial crisis in 2008, the industry's market size in terms of value declined due to deepening polarization (the trend toward lower prices vs. the pursuit of differentiation through increased value added). [9]

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[6] Notification No. 149 Environmental Health Director, Ministry of Health, Labor and Welfare, December 5, 1978.
[7] Ministry of Health, Labor and Welfare, July 17, 2015, No. 0717-2, "Regarding application of the laws for barbers and beauticians."
[8] Ministry of Health, Labor and Welfare, Health Service Bureau, Environmental Health Division. "The reality of the beauty salons business, and direction for improvement." March, 2012, p.38. http://www.mhlw.go.jp/seisakunitsuite/bunya/kenkou_iryou/kenkou/seikatsu-eisei/seikatsueisei22/dl/h22/riyou_housaku.pdf
[9] Yano Research Institute Ltd. "Press Release: Research on the barber shop and beauty salon market has been conducted (2017)." April 21, 2017. http://release.nikkei.co.jp/attach_file/0443205_01.pdf

Executive Summary

The first QB HOUSE barbershop was opened on November 11, 1996, in the bustling Tokyo business district of Kanda-Mitoshirocho, where office buildings with reasonable rents and restaurants are located. Targeting business people who are pressed for time, QB HOUSE came up with the service concept of a "10-minute grooming service" that offers haircuts only, using "convenience" as the value proposition. Before QB HOUSE, the activities of barberhops in Japan were being guided by an industry association. As a result, all the barbershops had almost the same business hours, were closed on the same days, and were charging about the same amount as the service fee. They offered a nearly identical set of services, which included shampooing before and after the haircut, the shaving of facial hair, and a quick massage. Thanks to QB HOUSE, business people have developed a new pattern of customer behavior—making a quick stop for a haircut in their spare time, like during their lunch break or on their way. (QB HOUSE barbershops were located at train stations). As of June 30, 2017, QB Net Holdings was operating 542 shops in Japan and 117 overseas. The average number of seats per shop is 3.5.

Unique Value Proposition

QB HOUSE's main target customer is business people who are pressed for time. To these busy individuals the company offers "Five Conveniences": (1) a low price; (2) a 10-minute haircut; (3) accessibility (shops are conveniently located in places with high foot traffic); (4) a haircut-only service; and (5) no reservations accepted.

1) Low price: When the first QB HOUSE opened in 1996, the average price for a haircut at a barbershop was above 3,000 yen. After QB HOUSE introduced haircuts for 1000 yen, the barbershop industry experienced a polarization of prices at the high and low ends.

2) Short time: Traditional barbershops provided a full set of services that included shampooing, the shaving of facial hair, and a massage. This all took a long time. Even when customers ordered only a haircut, it would take more than 30 minutes because barbers tried to add value by consulting with the customers about their preferences. The barbers eventually persuaded customers to request more services and spend more. In contrast, QB HOUSE proposed "just a trim," (i.e. cutting back the hair to the length of the previous haircut). Trimming the hair requires much less time than a new hair style would, and minimizes the stylist's risk of failing to meet the customer's expectations. Also, by just trimming the hair, QB HOUSE could get customers to visit the company's shops more often.

3) Accessibility (the shops were located in places with high foot traffic): QB HOUSE shops are located in places with high foot traffic (i.e., inside train stations, outside train stations, and in shopping centers). Because QB HOUSE shops do not provide shampooing services, these shops do not need facilities that can ensure access to a massive supply of water. This gives the company more options with regard to its choice of locations. QB HOUSE shops are designed to be small, with only three or four seats, so they can be located in small spaces that are normally not suitable for commercial use. This enables the use of dead space within the train station (i.e. spaces that are no longer being used, places like the old Stationmaster's office, the night-duty rooms and the stockrooms). This way, QB HOUSE provides customers with the convenience of having their hair cut at the train station they always use. This gives railway companies the opportunity to turn dormant real estate into profit-making assets. Having shops in places with high foot traffic contributes to brand building and the reduction of advertising expenses. Traditional beauty salons, on the other hand, tend to choose larger spaces for their shops. In order to save on rent, beauty salon operators tend to select a street-level shop facing a road with less traffic, or a shop on the second floor or higher. This does not improve customer convenience.

4) Haircuts only: Many barbershops try to increase sales by selling haircare products, while many beauty salons will offer nail services and a kimono dressing service. In contrast, QB HOUSE limits its services to haircuts. Instead of shampooing, QB HOUSE uses an "Air Wash" (a special vacuum cleaner that the

company has developed). There is no cash payment—payment is made at a vending machine, where the customer, upon arrival, buys a ticket with a number on it, and gets into the waiting line. In this way, QB HOUSE minimizes the time hair stylists spend doing things other than giving haircuts.

5) No reservations accepted: Conventional beauty salons would run the risk of making customers wait for a longer time if there were no reservations, because each customer service would take longer. To avoid having to make customers wait and minimize opportunity loss, many beauty salons take reservations. Even without a reservation system, QB House customers will not have to wait too long because the company's hair stylists finish the haircut in such a short time. The opportunity cost for QB HOUSE is minimal too. For customers, this approach is more convenient because they do not have to be bound by any time restrictions. They can also make efficient use of any free time that suddenly becomes available. Each of QB HOUSE's shops has a sign that indicates how long customers will have to wait. This helps customers decide whether to wait or not. Customers can check the length of waiting time at neighbor shops by accessing the company's website on their smartphones. If they see that their first-choice shop is crowded they can go to another nearby QB HOUSE shop.

Unique Value Chain

QB HOUSE's value chain has realized "Five Conveniences."

Store development

QB HOUSE' shops are located in places with high foot traffic, places that customers frequent during the course of their daily lives, such as train stations and shopping centers. The Store Development Team analyzes locations, and identifies good spaces for the company's shops. The team negotiates with real estate developers to achieve favorable rental terms and conditions. In the case of small dead spaces in train stations, such as the old Stationmaster's office, the night-duty rooms and the stockrooms, railway companies are not aware that such spaces can be utilized for commercial purposes. The company's staff approaches the management of these facilities directly, and proposes the opening of QB barbershops. The design and layout of individual shops take into account the features of the particular space in question, including the characteristics of the physical surroundings and the scenery of the neighborhood, with the aim of optimizing the usage of space and the placement of equipment. Less than 1% of QB HOUSE shops are closed within the first year due to poor business performance.

Haircut services

QB HOUSE provides a haircut in a short amount of time (10 minutes), with uniform quality. Customers pay in advance by buying a ticket at a vending machine, and then wait for their turn. A sign outside of each shop indicates the length of time that customers will have to wait for a haircut. Customers can also check on the congestion at nearby shops by using their smartphones. QB HOUSE tries to minimize any mismatch between the customers' expectations and the actual results. "Trimming" minimizes this risk. ("Trimming" does not require a change in hairstyles; the stylist just cuts back the hair to the length of the previous haircut.) When customers want to change their hairstyles, they can refer to the ten hairstyles shown on QB HOUSE's smartphone application. This helps the stylist to immediately understand the kind of haircut the customer has in mind. After the haircut, there is no shampooing—the stylist removes the hair clippings using a special vacuum cleaner (called the "Air Wash").

Store operations

QB HOUSE has developed its own store management system. The company collects and analyzes the following data: daily sales; the number of customers; the average time required for a haircut, broken down by time of day, age, and gender; new or returning customers; average waiting time; and seat utilization rates. The company periodically arranges for a third party to undertake "mystery shopping" to conduct surveys and determine the level of customer satisfaction at each shop. Based on these results, the company improves shop operation through a fast-moving PDCA (plan-do-check-act) cycle. Shops at the train stations get crowded

during lunchtime and evening hours, while shops at shopping facilities get congested in the afternoon. QB HOUSE can predict the flow of customers to each shop with precision, and moves stylists between shops on an hourly basis to meet these fluctuations in the demand.

R&D

QB HOUSE has developed original equipment, such as the "Air Wash" (a special vacuum cleaner that eliminates the need for shampooing); signals to notify the public of congestion at stores; and furniture that can store everything a stylist would need (such as an Air Wash device, a sterilizing unit, a closet, and a monitor). The company has also developed its own original approach to haircutting, as well as proprietary training programs. In addition, QB House has revised its shop operation manual to improve its services.

Human resources management

QB HOUSE hires not only experienced stylists but also individuals who have no experience (and no certifications). The company will also hire people who have taken time off for maternity leave or parenting leave, and people who have left the industry to pursue a career in another industry.

QB HOUSE develops stylists at its in-house training program, called the "LogiThcut School." Customized training is provided, depending on each stylist's amount of experience and capabilities. LogiThcut Schools are located in Tokyo, Osaka and Nagoya, where designated educators, called "trainers," teach the stylists. Employees without any experience can develop the necessary skills within six months. Experienced stylists, who are tested as part of the interviewing process, will focus on upgrading their skills to meet the company's standards.

QB HOUSE does not have a retirement age, and its turnover rate is low. Stylists at QB HOUSE can expect to have a stable income because QB HOUSE experiences less seasonality in demand, and there is no practice of designating stylists. This decision to depart from the standard industry practice of using designated stylists helps individuals who would prefer a flexible working style for various reasons, such as raising children.

Fit among Activities

Each of QB HOUSE's "Five Conveniences" mutually strengthens the others. Because only a haircut is provided, the service can be done in a short time, and at a low price. Because the shops are located in places with high foot traffic and the price for a haircut is low, customers visit QB HOUSE barbershops often. The more frequently customers visit QB HOUSE, the higher the occupancy rates will be for the shop as a whole and for the seats. This high occupancy rate is what enables QB HOUSE to maintain a low price. When we look into each activity that supports the "Five Conveniences," many of the activities contribute to more than one convenience. This is a sign of a good fit among activities. (Please refer to QB Net Holdings Co., Ltd.'s activity system map, which appears at the end of this report.)

Innovation that Enabled Strategy

- Realization of the unique value proposition of the "Five Conveniences": (1) one low price; (2) a 10-minute haircut; (3) accessibility (shops are opened in places with high foot traffic); (4) a haircut-only service; and (5) no reservations accepted.
- Use of an "Air Wash" (a special vacuum cleaner), an approach developed as a substitute for shampooing.
- Use of a ticket vending machine, and the requirement of advanced payment. (Eliminates the need for staff to work at cash registers.)
- Use of furniture in which all the necessary tools for haircutting services can be stored. This furniture surrounds the stylist's seat, which reduces the distance that stylists will have to walk and helps them to save time. (The design for this furniture is registered.)

- Development of the smartphone application, “Cut Karte,” to help stylists quickly get an idea of the kind of cut the customer wants.
- Use of signals to indicate the length of time customers will have to wait for a haircut. The company’s system measures how long it takes for a customer to be seated at a stylist’s station after purchasing a ticket at the vending machine. This indicates the degree of congestion. The signals use three different colors to show three levels of crowdedness.
- Turning dead space in train stations into shops, to help the company minimize expenditures for rent, while taking advantage of strong demand in places where foot traffic is high traffic areas. Such prime locations contribute to reductions in advertising expenses.
- Use of “QB shell-type” shops, a type of pop-up shop that can be easily assembled and dismantled. This innovation has made it possible to set up temporary shops.
- Development of its own “Theory on Haircuts,” which is easy to understand.
- In-house training centers (“LogiThcut Schools), which produce a large number of stylists who can offer haircut services with a uniform level of quality after only six months of training.
- Store management system that accumulates extensive data, including the time required to complete a haircut. This data is used for the evaluation and assignment of stylists.

Trade-offs

- Does not target customers who want high quality. QB HOUSE targets customers who put a priority on convenience.
- Does not provide full services. (No shampooing, hair coloring, perming, shaving, or styling.) The decision not to provide a shampooing service has a major impact on the value proposition. By foregoing shampooing, QB HOUSE’s shops eliminate the need for large-scale water operations. This gives the company a broader choice of shop locations, shortens the time required for haircuts, and significantly reduces water and electricity costs.
- Does not set different prices for stylists of different ranks.
- Does not encourage stylists to develop skills based on craftsmanship, which is often dependent on a subjective (and very individual) sense about the desired level of quality to be attained. Instead, QB HOUSE provides stylists with a standardized technique that is based on theory.
- Does not choose spaces that are too large, and does not make the shop interiors too showy.
- Does not adopt the practice of designating stylists.
- Does not take any reservations.
- Does not use cash registers.

Consistency of Strategy over Time

QB HOUSE opened its first shop on November 1, 1996 in Kanda-Mitoshirocho. This shop provided only the haircut services that customers would have difficulty doing themselves. With the service concept of a “10-minute grooming service,” QB House shops offer customers the value proposition of convenience. Next, the company redefined “convenience.” Instead of “convenient price,” the company began focusing on “Five Conveniences,” and the store location strategy evolved. Still, by improving customer convenience, the company has been able to maintain the core component of its strategy, which is to raise its seat occupancy

rates.

Since the beginning, QB HOUSE's target customers have been business people with busy schedules. The company has opened shops in locations with high foot traffic to achieve high seat occupancy rates and increase customer awareness. QB HOUSE quickly opened shops in places with high foot traffic by: (1) arranging franchise contracts with the subsidiaries of railway companies that manage the real estate properties of their parent companies; and (2) consigning the operation of shops to independent stylists.

In the mid-2000s, large shopping malls were opened after the Large-scale Retail Store Law was changed. Although QB HOUSE had developed a brand image as "QB HOUSE shops at railway stations," the company aggressively began opening wholly owned shops inside shopping centers. Wholly owned shops, which at one time had accounted for less than 30% of all QB HOUSE shops, exceeded 70% in 2009, and have continued to show a slight upward trend. The customer portfolio was expanded to include children and elderly men in addition to businessmen. This has spread demand throughout the day, and helped to alleviate somewhat the high concentration of demand during evening hours on weekdays. In the fiscal year ended June 2016, the average number of customers per shop did not fall below six customers between 9am and 8pm on weekdays, and did not fall below 10 customers on weekends between 9am and 7pm. Opening shops at shopping centers leveled demand, increased sales, and improved profitability.

Meanwhile, a growing number of barbershops were being forced to close as the shop owners got older, lost customers, and had greater difficulty in hiring barbers due to a decline in the number of newly certified barbers. Similarly, the beauty salon industry experienced slower growth as consumers visited beauty salons less frequently because they were becoming more frugal, and female customers were less inclined to pay for perms and hair coloring. The competition intensified and the average price decreased. QB HOUSE recommended that female customers use different salons depending on the service required. They could go to beauty salons for hair coloring or a perm. However, customers do not need to get a coloring or perm every time. If they didn't go to a beauty salon, they would have the option of going to a haircut-only shop to get their hair trimmed. Accompanying the increase in the hiring of female stylists, QB HOUSE has seen a rise in female customers, who accounted for about 20% of all customers at the end of 2016.

QB HOUSE has entered overseas markets by focusing specifically on large cities with a high population density in economically developed countries. The company's overseas expansion has been fueled by the belief that the haircut business has no borders. The company entered Singapore in 2002, Hong Kong in 2005, Taiwan in 2012, and the U.S. (Midtown Manhattan, New York) in 2017. The company offers the same value proposition in all of these countries, namely, a haircut-only service offered at a low price, and in a short time. (The price varies, depending on local cost of living and the living environment. The same 10-minute haircut service costs 12 Singapore dollars, 60 Hong Kong dollars, 300 New Taiwan dollars, and 20 U.S. dollars.) By operating its business overseas, QB House has succeeded in strengthening its business while maintaining the core components of its strategy. For example, the company has had to develop from scratch its training programs for stylists. In the Asian countries where the company operates, stylists are not required to become certified because there is no national certification system. The company has redefined what stylists should learn, and has fundamentally redesigned its training program. This has resulted in a training program that is easier to understand. This program is now being taught at LogiThcut Schools, the company's in-house training centers that have been operating in Japan since 2013. The higher rents in Hong Kong have resulted in the development of "QB Shell Shops," pop-up shops which have only one seat. In Asian countries, where haircut-only, low-priced barbershops are very common, QB HOUSE distinguishes itself from the competition by providing clean shops with good taste, highly skilled stylists, and a nice personal touch. The brand image of QB HOUSE is a haircut shop with good customer service skills and good taste. In Manhattan, where "a low price" is often assumed to be "low quality," QB HOUSE has emphasized the convenience of its haircut services to business people for whom the opportunity cost of time is very high. The company's experience in New York will be applied when the company enters other parts of the U.S. and Europe where the barbershop and beauty salon industries are mature and there are a significant number of very busy people with a high level of income.

Profitability

Both the five-year average return on invested capital and the return on sales exceed the industry average by a wide margin. (Profitability analysis was conducted by PwC Japan.)

Note: QB Net Holdings Co., Ltd.'s predecessor is QB Net Co., Ltd., which was established in 1995 by the founder. In 2010, the company's ownership changed to JAFCO Co., Ltd., one of Japan's oldest venture capital firms, through a leveraged buyout (LBO). Then in 2014, Integral Corporation, one of the leading investment firms in Japan, gained ownership through an LBO. Therefore, QB Net Holdings' financial statements include the loans to fund the LBOs and the goodwill that was recognized at the time of the LBOs. The Porter Prize evaluates how a business can create profit from invested capital, and the analysis below excludes the influence of the LBOs.

Return on invested capital (ROIC) (Unit=percentage point)

Difference from industry average					
5Yrs Avg.	2012	2013	2014	2015	2016
12.3 %P	18.3 %P	5.3 %P	8.1 %P	12.9 %P	20.5 %P

Inter quartile range (IQR) = 1.3 %P
Return on invested capital = Operating income / Average invested capital

Return on sales (ROS) (Unit=percentage point)

Difference from industry average					
5Yrs Avg.	2012	2013	2014	2015	2016
6.4 %P	6.7 %P	7.1 %P	6.0 %P	7.5 %P	7.0 %P

IQR = 3.3 %P
Return on sales =Operating income / Net sales

Activity System Map of QB Net Holdings Co., Ltd.