Special Feature 1

Year to start establishing dominant position in domestic and overseas convenience store operations

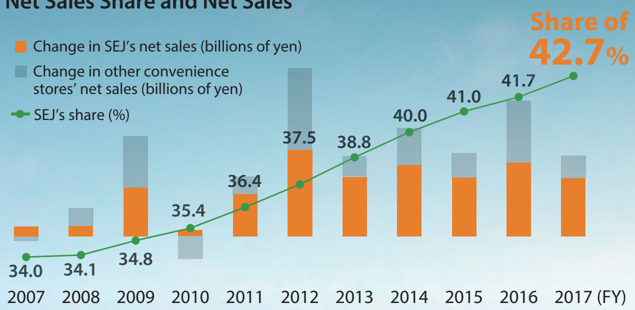
In greater pursuit of "close-by, convenient" concept for stores to meet customer needs

In Japan, the trend toward obtaining meals outside the home is inching steadily along against a backdrop of diversifying lifestyles—influenced by such factors as more working women, more seniors in the population and a decrease in the number of people per household—and less time spent cooking at home. Of note, demand for *sozai* prepared dishes, boxed lunches and other take-home meals is noticeable, fueled by convenience and economic reasoning. Market scale is likely to continue to expand. Under these conditions, competition is crossing business lines, as drugstores expand into the food business and food supermarkets enrich their selection of take-home meals.

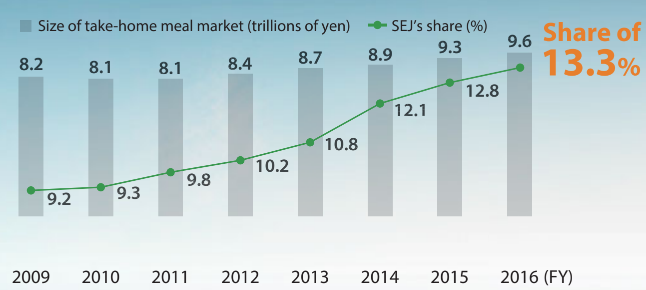
Seven-Eleven Japan (SEJ) has taken a flexible but aggressive approach to this situation and tirelessly seeks the "close-by, convenient" value. SEJ has capitalized on strengths, that is, locations, products and service—respectively, stores, the meticulous pursuit of quality and reasonable prices, and such aspects as product lineups, customer service and ATM access, which is indispensable in today's world—and carefully responded to changing customer needs. As a result, the number of women and seniors who visit 7-Eleven stores has markedly increased over the past few years, pushing SEJ's share of net sales in the domestic convenience store market to 42.7%, as of the fiscal year ended February 28, 2017.

Realignment in the domestic convenience store sector has accelerated in recent years. SEJ will continue to respond proactively to changes in the external environment amid increasingly fierce competition, with a 50% share of the market well within sight. Going forward, SEJ remains keen to embrace new challenges, including store creation that meets changing customer needs, support for store management and steps to boost productivity, and is sure of posting further growth.

Net Sales Share and Net Sales



Response to Market Opportunities (Higher demand for take-home meals)

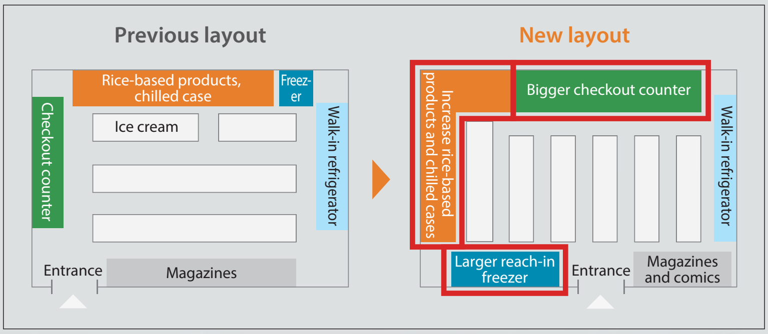


Creating Stores Matched to New Customer Needs

The way convenience stores are used is changing, fueled by more women and senior citizens in the customer base. Over the past 10 years, daily sales of frozen foods and checkout-counter products have soared, up 4.7 times and 2.6 times, respectively, while sales of alcoholic beverages, sundries and magazines have dropped. Not bound by past successes, SEJ is pushing through a process to revamp store layouts that will better meet customer needs under the "close-by, convenient" concept.

For example, consumers are increasingly looking for simplicity and convenience, paralleling the trend toward spending less time cooking at home. To address such changing demands, the new store layout will expand the capacity of refrigerated cases where boxed lunches and chilled products are displayed and frozen food showcases, while creating a bigger checkout counter area. These features will ensure that stores are well prepared to meet newly emerging customer needs as lifestyles continue to evolve.

This is a foresighted approach that looks beyond current demand conditions to create stores that fit customer needs now and in the future. The new store layout should encourage customers to visit stores more frequently, leading to a potential increase of ¥30,000 to ¥40,000—or 5%—in daily sales per store. In the fiscal year ending February 28, 2018, the new store layout plan will be applied to 800 existing stores and 1,100 new stores, with the process continuing to roll out in the next fiscal year and onward.



Another objective is to improve profitability through enhanced product capabilities. For *SEVEN CAFÉ*, which has sold about 2.4 billion cups of coffee since the brand debuted in 2013, new coffee machines will be installed with new café latte options.

Previously, the iced café latte was made with ice milk beads—milk quickly frozen in bead form—but a type of milk was developed especially for *SEVEN CAFÉ* café latte that highlights the delicious consistency and flavor of milk. In conjunction, a new machine was developed with a built-in warming and steam function that brews up a perfect, hot café latte.

In February 2016, test marketing with this café latte machine began in Hokkaido, contributing to a double-digit increase in sales of *SEVEN CAFÉ* there. Seeing the potential, management plans to have the new machine installed throughout the domestic network, with all older machines to be replaced during the fiscal year ending February 28, 2018. Café latte sales are expected to grow on a nationwide basis in the current fiscal year, with an annual target of one billion cups set for the first time.

Special Feature 1

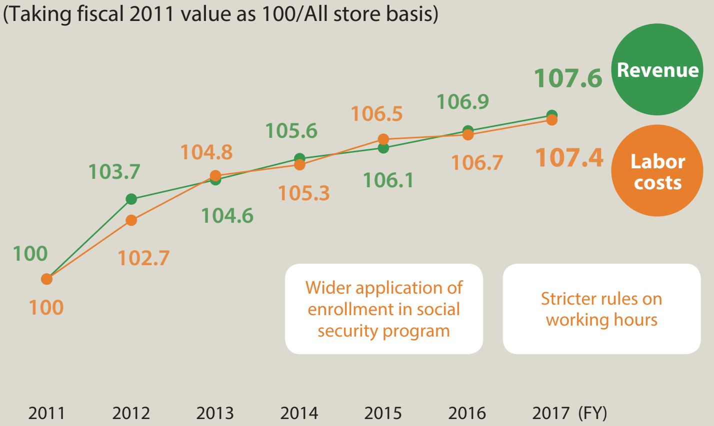
Labor costs have noticeably increased in Japan, reflecting such factors as a labor shortage resulting from a shrinking workforce and a hike in the minimum wage. Under these conditions, a special discount of 1% on "Seven-Eleven Charge" royalties will be implemented, effective September 2017, to enable franchisees—the ultimate partners in the franchise business—to keep a positive outlook on store management.

This measure had been repeatedly discussed for some time in a bid to overcome a challenging work environment, and the timing was deemed perfect to demonstrate synergy with other measures, including the layout change. As a result, SEJ's own results will show a revenue decrease of about ¥16.0 billion over 12 months, but each store should post an annual increase in sales of about ¥800,000. For franchisees, the portion of royalties thus saved can be applied elsewhere, for more robust product ordering or to offset skyrocketing labor costs, for example, and thereby reduce the possibility of lost sales, and help create an environment in which franchisees can concentrate on strategic store management. The measure has been extremely well received by existing franchisees and is sure to motivate store management by eliminating uncertainties about the future. In addition, the measure may encourage new owners to become franchisees and raise the medium-term share.

Reduced Royalties to Support Franchisee Owners in Store Management

Annual sales increase of about ¥800,000 per store anticipated

Revenue and Labor Costs at Franchised Stores
(Taking fiscal 2011 value as 100/All store basis)



Factors leading to 5%–6% rise in labor costs

Support for labor-saving store operations and enhanced front-line productivity is also vital if franchised stores are to achieve higher revenues.

For example, dishwashers improve operating efficiency at stores and, in an industry first, SEJ is promoting the installation of such appliances. The use of a dishwasher for equipment such as warmers for *oden* stew, which is commonly eaten in Japan, and the removable parts of fryers should save about an hour a day otherwise spent cleaning this equipment by hand, and thereby boost efficiency. From an environmental perspective, dishwashers could cut annual water consumption by about 20% per store—determined through store trials—and from a hygiene perspective, the high-sterilization effect of dishwashers addresses heightened customer awareness about food safety and reliability. Dishwashers are gradually being introduced at stores in Japan, with all locations to be equipped by the end of the fiscal year ending February 28, 2018.

Working time	Washing by hand → Dishwasher	About 1 hour less
Labor costs	Reduced 1 hour/day	About ¥300,000 / year less
Water consumption (per store)	Reduction	About 20% less (SEJ's temporary calculation based on store trials)

Improving work efficiency while enhancing quality of customer service

Targeting Both Improved Productivity and Work Style Reforms

Ahead of the "Declaration of Plan to Introduce 100 Billion Electronic Tags for Products in Convenience Stores," formulated by the Ministry of Economy, Trade and Industry, SEJ announced plans to initiate trial tests in August 2017 to validate an energy-saving system for product inspection at stores using radio-frequency identification (RFID*).

When products are sorted at the distribution center, RFID IC chips are attached to each wheeled cart, designating the products on that cart. At stores, inspection only requires the cart to be wheeled past an RFID reader. This system dramatically reduces the time needed to inspect deliveries at stores, allowing staff to apply those saved minutes to other activities, particularly customer service and front-line operations, which leads to enhanced customer service. In addition, the use of wheeled carts and tail lifts on delivery trucks to load and unload products has reduced the burden on drivers. One vital role that SEJ seeks to play is to build a society that welcomes participation by a diverse workforce, including women and seniors, through the proactive creation of a comfortable work environment for everyone.

Initiate trial tests in August 2017 to verify energy-saving system for product inspection at stores using RFID*

Sorting at distribution center ▶ **Data transmitted to stores** ▶ **Trucks equipped with a tail lift** ▶ **Reduced product inspection time**

RFID IC chips are attached to link the product and the wheeled cart

Sorting data is forwarded to stores

Unloading with a tail lift

Cart wheeled past RFID reader for delivery and product inspection

Effects realized by using RFID

Effect of energy-saving system for product inspection at stores

Daily product inspection time **170 minutes → 8 minutes**

(Equivalent to reduction in labor costs of about ¥800,000 annually)

Effect on distribution of drivers' workloads

Major reductions in the work of sorting and loading at distribution centers, unloading from trucks to carts and unloading at stores led to the following:

1. **Promotion of employment of female drivers**
2. **Better working conditions for drivers**

* RFID is a technology for contactless reading of data from an IC chip through the transmission of radio waves

Large-Scale M&A in North America Heralds Further Growth

In North America, oil majors are withdrawing from the retail business of operating gas stations with convenience stores, sustaining a process of realignment among chains specializing in convenience store operations.

Against this backdrop, region-based 7-Eleven, Inc. (SEI) has pursued measures to strengthen sales of fresh foods, such as sandwiches, and hot foods, such as pizza, revise its store opening standards and expand its store network through M&As that will significantly contribute to enhanced convenience. Through these measures, SEI has seen daily sales grow, and operating income expanded a solid five times, from $137.0 million in the fiscal year ended December 31, 2003 to $704.0 million in the fiscal year ended December 31, 2016.

State of New York

Texas

Florida

Number of stores to be acquired

Number of Sunoco stores to be acquired
Number of existing SEI stores*
Total number of stores

Area	Number of Sunoco stores to be acquired	Number of existing SEI stores*	Total number of stores
Northeast area (including state of New York)	Approx. 450	Approx. 2,960	Approx. 3,410
Southeast area (including Florida)	Approx. 110	Approx. 810	Approx. 920
Southern area (Texas)	Approx. 550	Approx. 680	Approx. 1,230
Three-area total	1,108	Approx. 4,450	Approx. 5,560

Sunoco LP
Strategic withdrawal from retail business to concentrate on wholesale business

SEI
Higher sales and reinforced profitability over medium to long term through addition of more high-quality stores

*Number of SEI stores, as of December 31, 2016

A priority strategy for SEI is to reinforce take-home meal sales. In the United States, typical convenience stores were originally retail stores attached to gas stations that catered to gas station customers who were primarily interested in cigarettes and beverages. Consequently, the practice of buying a meal at a convenience store is not as firmly rooted in the United States as it is in Japan. In addition, the quality and selection of fast food, such as sandwiches and pizza, leaves considerable room for improvement when compared with the lineup at convenience stores in Japan. This presents a great opportunity for growth in North America. With these underlying factors in mind, it is essential for SEI to expand product lineups of fast food and improve quality through such approaches as product development matched to local characteristics, so that stores identify the latent needs of local customers, expand customer segments and encourage customers to visit more frequently. Cultivating a market concentration strategy will make this possible.

SEI's store-opening policy hinges on organic store openings, based on this market concentration strategy. Integrating M&A activity into the policy, SEI has built the largest network of single-chain convenience stores in North America, with 8,707 stores in operation as of December 2016. Since 2011, SEI has pursued a strategic and aggressive M&A program, which has driven sales increasingly higher.

Against this backdrop, in April 2017, SEI decided to acquire

some of the convenience store and gasoline retail businesses of U.S.-based Sunoco LP, a transfer scheduled to take place in the second half of 2017. Sunoco has a large number of stores in Texas and along the U.S. east coast, and the fact that these geographic areas generally correspond to SEI's current store map is a major advantage in terms of implementing the market concentration strategy. In acquiring some of Sunoco's businesses, SEI seeks to enhance its supply chain through a more pervasive store presence. Indeed, SEI will expand operations in Texas to about 1,230 stores, with the addition of about 550 Sunoco stores to its own existing in-state network of about 680 stores. This will be complemented by 110 Sunoco stores in Florida and other parts of the southeast, where SEI currently has 810 stores, bringing the area count to about 920 stores. Meanwhile, in New York and other parts of the northeast, SEI will add about 450 Sunoco stores to its existing area network of 2,960 stores for a total of about 3,410 stores there.

Sunoco has honed a sharp competitive edge in North America, so access to the brand power of Sunoco gasoline is already an advantage. In Sunoco's retail business, gasoline sales hover around 5,100 gallons per day per store, which is close to 1.5 times more than the volume of gasoline sold at SEI's stores. Daily product sales are in the vicinity of $4,800 per store, which is equal to or greater than the SEI daily average. As part of the acquisition deal, SEI intends to sign an agreement under which Sunoco will supply its competitive-brand gasoline to the acquired stores for 15 years.

The emphasis that SEI has placed on strengthening the product lineups, particularly fresh foods, will be applied at the acquired stores, which will enhance product capabilities and drive up sales as well as the gross profit margin. Following the purchase of stores through the M&A process, SEI will boost profitability by switching signboards to the 7-Eleven brand and will promote franchising.

Also, in 2016 Warabeya Nichiyo Holdings Co., Ltd., acquired a 19.3% equity stake in Prime Deli Corporation, a Texas-based local product supplier to SEI. By drawing on the excellent product development capabilities of Warabeya Nichiyo Holdings accumulated in Japan and a dedicated production facility in Hawaii that supplies 7-Eleven stores exclusively, SEI will raise the quality of fresh foods and reinforce its infrastructure, including the supply of products. This is the first step toward setting up dedicated production facilities for 7-Eleven products in different parts of the United States, as in Japan, and building a structure that can ensure a stable supply of high-quality products.

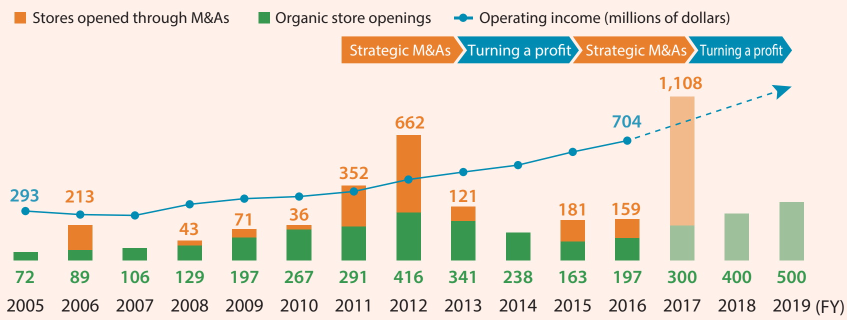
Through these activities, overseas convenience store operations should achieve targets of 10,000 stores, average daily sales of $5,000 and operating income of $1.0 billion by the fiscal year ending December 31, 2019. However, the impact of the Sunoco acquisition on performance results has not been factored into the earnings targets since it will probably take several years to turn a profit from those stores.

Outline of Sunoco LP's Retail Business (fiscal 2016)*

Product sales	About **$4,800** per day per store Equal to or greater than SEI average daily sales
Gasoline sales (volume)	About **5,100** gallons per day per store About 1.5 times higher than SEI volume

*Sunoco LP figures are extracted or estimated from its disclosure materials (10-K)

Number of Stores and Operating Income



Comparison of Cash Flows and Compound Annual Growth Rate (CAGR) of Operating Income before and after Strategic M&As

(Millions of dollars)	2005–2010 (annual average)	2011–2016 (annual average)
Capital expenditures	453	1,288
Operating income	320	553
Depreciation and amortization	398	506
Operating cash flow*	590	838
Free cash flow*	136	(449)
Operating income CAGR	5.3%	11.4%

Execute high-quality M&As
Build supply chain

Fiscal 2019 Targets
Number of stores: 10,000
Average daily sales: $5,000
Operating income: $1.0 billion

* Operating cash flow = (Operating income x 60%) + Depreciation and amortization
Free cash flow = Operating cash flow – Capital expenditure (simplified calculation)