COMPANY RESEARCH AND ANALYSIS REPORT

Tecnos Japan Inc.

3666

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Index

Summary

Posting upbeat results amid healthy IT investment demand accompanying corporate DX advances. Starting provision of an ordering and payment service on the proprietary platform business (CBP)

1. Company overview

TECNOS JAPAN INCORPORATED <3666> (hereafter, "the Company") is an independent, ICT systems services company that provides a wide range of system services, including corporate digital transformation (DX)*1 consulting, system grand design assistance combining a mission-critical system (ERP) *2, customer relationship management system (CRM) *3, and its own service (CBP) *4, business consulting, requirements definition, design, development, and maintenance, and is also focusing on expansion of global business. Its strengths include its high-quality consulting capabilities, technological capabilities, and the utilization of its proprietary templates. The Company has a track record of supporting the implementation of ERP, on the axis of SAP, for more than 220 companies, mainly in the manufacturing industries. Amid an accelerating digitalization trend, the Company is promoting DX business with a combination of ERP and CRM (company optimization) and its own CBP platform (inter-company collaborations) for industry-level optimization and value provision utilizing accumulated data (such as customer business reforms and contributions to a sustainable society).

*1 Refers to companies reforming products, services, and business models based on customer and societal needs using data and digital technologies in response to rapid changes in the business environment and also making changes in workflow, organization, processes, as well as corporate culture and atmosphere to establish competitive advantages.
*2 Abbreviation of Enterprise Resource Planning; refers to a framework for centralized and efficient management of corporate resources (people, goods, and funds).
*3 Abbreviation of Customer Relationship Management; refers to a system that manages customers and builds relationships.
*4 Abbreviation of Connected Business Platform; this is a new business platform for comprehensive optimization of business beyond inter-company frameworks.

2. FY3/21 consolidated results

The Company reported sales and profit increases in FY3/21 consolidated results with ¥8,197mn in net sales (+6.8% YoY) and ¥924mn in operating income (+227.2%), beating the initial estimate. In a market environment with a mix of positive and negative impacts from the novel coronavirus pandemic (hereinafter, COVID-19), it posted all-time higher sales in a third straight fiscal year due to upbeat corporate investments in ERP and CRM systems and the sales boost from a full-year contribution by ACK Co., Ltd. added to the Group in January 2020. In earnings, the Company realized a steep increase, despite continued upfront costs for the platform business (CBP), on a rebound from FY3/20 when profit dropped sharply on losses from a specific project (one-time factor), extra profit on the increase in sales, and curtailment of spending related to COVID-19. Operating margin improved to 11.3% (vs. 3.7% in FY3/20), a return to the level from FY3/19. Additionally, the Company moved forward qualitatively with the start of an ordering and payment service on its CBP, which is likely to become an important growth axis in the future, and other advances in May 2021.

3. FY3/22 consolidated results forecasts

With regard to the FY3/22 results forecast, the Company forecasts sales and profit gains with ¥8,750mn in net sales (+6.7% YoY) and ¥1,020mn in operating income (+10.4%). Despite taking a cautious view of the prolonged pandemic impact on investment activity, it forecasts higher sales mainly driven by assisting deployments of ERP and CRM systems amid anticipated pick-up in IT investment demand related to corporate DX promotion. In earnings, it expects to increase profits, even with its current positioning in an upfront investment stage in platform business (ordering and payment service), mainly on the positive effect of higher sales, and reach the ¥1bn level in operating (and ordinary) profits for the first time.

4. The growth strategy

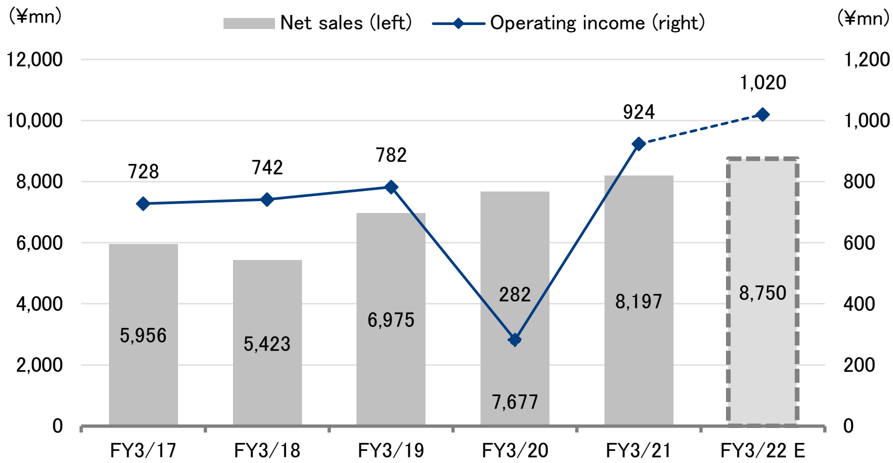
The Company's growth strategy has a direction (vision) of "LEAD THE CONNECTED SOCIETY TO THE FUTURE" based on a mission of "Contributing to the development of society by connecting organizations, people, and data." In other words, in addition to deployment and switching of ERP (optimization at the individual-company level) using knowhow accumulated since its founding, it is strongly advocating the concept of an industry optimization-type platform business (optimization of the entire supply chain) that connects companies via data through collaborative creation with partner companies that have various cutting-edge technologies and deploying companies. It has also set three points for the future investment areas towards growth: "platform business," the "global business" and "human resources and organizations."

FISCO thinks the Company is sufficiently capable of achieving sustainable growth, despite lingering uncertainty about the impact by the prolonging of COVID-19, on application of ERP systems and platform business in DX implementations. Even with the continued possibility of a temporary downturn from COVID-19, structural reforms for realizing DX have become an issue that needs to be addressed by not only companies but also society. Finding solutions to social issues hence should be seen as a major opportunity for the Company to drive its own growth. It needs to make progress in full-fledged operation of platform business as a first step and then focus on creation of new value including collaboration with partner companies and others.

Key Points

- Realized higher sales and profits, exceeding the initial estimate, and set all-time high sales, despite COVID-19, in FY3/21
- Achieved strong qualitative advances with industrial-academic joint research aimed at improving efficiency in commercial flow and logistics and the launch of ordering and payment service (SaaS) on its own platform (CBP)
- Expects continued increases in sales and profits in FY3/22 driven by IT investment demand accompanying corporate DX promotions
- Pursuing a strategy that harnesses resolution of societal issues to drive its own growth by combining ERP (corporate optimization) and its proprietary collaborative-creation platform (optimization of the entire supply chain) with a goal of full-fledged development of DX

Results trends



Source: Prepared by FISCO from the Company's financial results summary report

Company overview

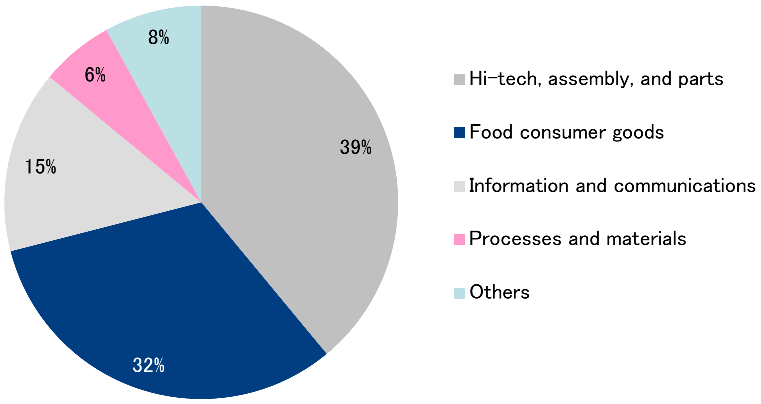
Mainly provides ERP and CRM implementation support and also focuses on DX promotion by building a proprietary platform.

1. Business overview

The Company is an independent ICT systems services company that provides a wide range of system services, including corporate digital transformation (DX) consulting, system grand design assistance combining a mission-critical system (ERP), customer relationship management system (CRM), and its own service (CBP), business consulting, requirements definition, design, development, and maintenance. Its strengths include its high-quality consulting capabilities, technological capabilities, and the utilization of its proprietary templates, and the Company has a track record of supporting the implementation of ERP, on the axis of SAP, for more than 220 companies, mainly in the manufacturing industries. The Company outlined a new group mission of "LEAD THE CONNECTED SOCIETY TO THE FUTURE" (contributing to the development of society by connecting organizations, people, and data) amid acceleration of the digitalization on a global scale. It is promoting DX business with a combination of ERP and CRM (company optimization) and its proprietary CBP platform (inter-company collaborations) for industry-level optimization and value provision utilizing accumulated data (such as customer business reforms and contributions to a sustainable society).

The composition of total net sales by industry (FY3/21 results) was hi-tech, assembly, and parts at 39%, food and consumer goods at 32%, information and communications at 15%, processes and materials at 6%, and others at 8%. At this point, the main customers are large manufacturers rebuilding their mission-critical systems with ERP. However, it might diversify to other industries, including logistics and retail, depending on progress in platform business that seeks to optimize the entire supply chain.

Composition of total net sales by industry (FY3/21)



Source: Prepared by FISCO from the Company's financial results briefing materials

The Company has only one business segment, "information systems solutions services," but in terms of the content of the services provided, it is divided into "core work systems and peripheral solutions" and "others." Moreover, the former is broadly divided into the mainstay ERP and CRM related business and the new focus field of the CBP promotion business. "Information systems solutions services" accounts for a high percentage of consolidated sales.

(1) The ERP and CRM related business

1) On the topic of ERP, which has been the Company' core business since its founding, the Company supports the implementation of ERP packages provided by various ERP vendors that distribute on a global scale based on a Best of Breed* strategy to realize optimal solutions for customer companies. Specifically, it accurately ascertains in a timely manner the flow of goods in the logistics management work (purchasing, production, and sales) of customer companies, and also ascertains results in a timely manner and future forecasts for accounting management work (financial accounting and management accounting), and it provides integrated services for the results management of globalized corporate groups, from the upstream (consulting) through to the downstream (maintenance and improvements). The ERP packages which the Company handles are centered on SAP S/4HANA and also include mcframe by Business Engineering Corporation <4828>, which is strong in production management.

* An approach of selecting the best hardware and software in each field and constructing systems by combining them.

For SAP S/4HANA, which is the axis, in September 1996 the Company concluded a partner agreement with SAP Japan (started handling products at the time of establishment in 1994), and it has a track record of supporting its implementation into more than 220 companies. The Company is also focusing its efforts into overseas-related projects, supporting roll-in and roll-out (implementation to the overseas subsidiaries of Japanese companies and the Japanese subsidiaries of foreign companies). Furthermore, by using the templates* it has created based on its previous experience of implementation, it is able to complete an implementation with a short delivery time and low cost, and to provide new added value.

* Refers to new packages with settings and additional functions that other companies deem necessary being created by the Company based on its track record of implementing ERP packages and other software. By combining these settings and functions with the ERP package, it is possible to reduce the time required for implementation and costs when making new implementation.

Alongside the implementation of ERP packages, there is a growing need for even more evolved total solutions (demand forecasts, marketing related, etc.) through combining peripheral technologies. In response to this, the Company is working on products including EPM*1/BI*2, EAI*3, etc.

*1 Abbreviation of Enterprise Performance Management (the management of a company's results). It refers to concepts and tools that enable a company to manage its results and create initiatives based on a strategy.
*2 Abbreviation of Business Intelligence. It refers to concepts and tools for the accumulation, classification, search, analysis, and processing of data inside and outside of a company and making this useful for business decision making.
*3 Abbreviation of Enterprise Application Integration. It entails the coordination of multiple systems to integrate data and processes.

2) In CRM (customer relationship management systems), the "other mission-critical area" along with ERP, the Company fully entered the market with its addition of Lirik, Inc., which handles SI business mainly in the US, to the group in June 2018. Through collaboration with ERP, CRM facilitates integration of customer information, in addition to management information within the company, and thereby enhances the efficacy of big data and AI utilization. It also plays an important role in development of platform business (optimizing the entire supply chain across companies) promoted in DX realization. The Company added ACK, which provides CRM cloud-related services in Japan, to the group in January 2020 and absorbed ACK with itself as the surviving entity on October 1, 2020.The core CRM product handled by ACK is salesforce.com Ltd.'s CRM platform, and the Company aims to promote even faster reinforcement of CRM business via the merger.

(2) DX promotion business

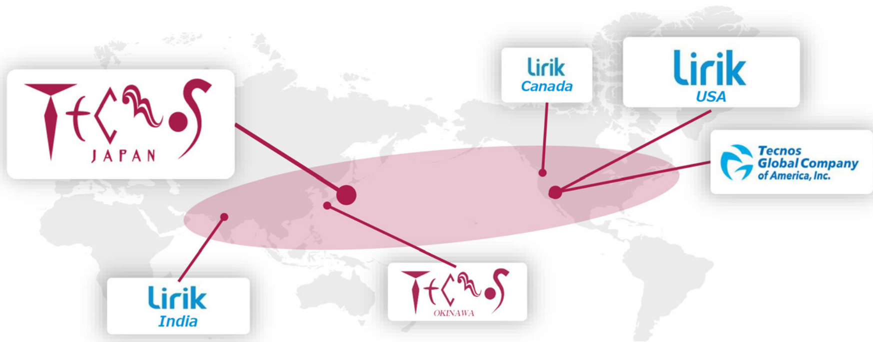
Amid the acceleration of digitization on a global scale, the Company is responding to needs to switch to DX-compliant ERP* and is also promoting business for DX realization (optimization of the entire supply chain) by extending knowhow regarding standardization and overall optimization within corporate groups cultivated in ERP business to the entire supply chain and actively constructing its proprietary platform (CBP) that utilizes CRM and cutting-edge digital technologies (including IoT and blockchain) and connects them seamlessly among companies. It will promote business reforms to its customers by using AI and other technologies to utilize to the greatest possible extent the big data accumulated on the platform, which will also enable the Company to secure a stable source of earnings as an asset business.

* SAP has shown a positive stance toward DX-compliant ERP and announced that it intends to discontinue support for conventional ERP by 2027 (it extended the deadline from the original plan for discontinuation in 2025).

2. The Group's business structure

In addition to the Company, the Group is comprised of 5 consolidated subsidiaries (as of March 2021). The consolidated subsidiaries are Okinawa Tecnos Incorporated, established as a nearshore base; Tecnos Global Company of America, Inc. (TGCA), which is located in America's Silicon Valley, and also Lirik, which was acquired via TGCA in June 2018, and its subsidiaries, Lirik Infotech Private Limited (an Indian global delivery center) and Lirik Software Services Canada Ltd. Therefore, the Group's business structure is that it is developing businesses in the Japan and North America markets and also utilizing Okinawa (nearshore) and India (offshore) for IT human resources.

Overview of the Tecnos Group



Source: The Company's financial results briefing materials

3. History

The Company was established in April 1994 with the aim of providing high-quality SI services using a small number of highly talented personnel. Since then, it has partnered with several ERP vendors, starting with SAP Japan but also including Business Engineering <4828>, Oracle Japan <4716>, and Infor Japan. It has expanded its business scale while establishing and enhancing its business to support the implementation of ERP. Based on a business management structure that does not rely on the products of specific vendors, it has acquired an excellent reputation among both vendors and users for its high-quality consulting capabilities, technological capabilities, and project-management capabilities, generating growth in results. It was listed on the Osaka Stock Exchange JASDAQ (standard) market in December 2012 (following the change of this market in June 2015 to the TSE 2nd Section, it was listed on this market, and its listing was then upgraded to the TSE 1st Section in September of the same year).

Following its listing on JASDAQ in 2012, the Company developed a strategy to make the big data business its second business pillar after the ERP business. In September 2013, it established TGCA*1 with the aims of collecting information and discovering venture companies in the United States. Then in October of the same year, it established the current Tecnos Data Science Engineering (TDSE)*2 as a group of data scientists responsible for the big data business and started to construct the foundations of a new business. In 2015, it launched sales of artificial intelligence products and also concluded a series of business partnership agreements with salesforce.com <CRM> and Microsoft Japan Co., Ltd., and it accelerated the strategy aimed at strengthening foundations toward expanding the big data business. Also, in 2018 it established a structure toward business expansion in the North America market through acquiring Lirik, a US company. Conversely, it sold some of its share in TDSE following this company's listing on the TSE Mothers Market, and as a result, it was removed from the scope of the Group. The Company added ACK (headquartered in Osaka), which provides cloud-related services for Salesforce.com CRM in Japan, to the group as a wholly owned subsidiary in January 2020 and absorbed ACK in October 2020.

*1 The company name when it was first established was Tecnos Research of America, Inc. (TRA). It changed its name to its current name, TGCA, in April 2017.
*2 Its company name when it was first established was Tecnos Data Science Marketing Co., Ltd., (TDSM). It changed its name to its current name, TDSE, in April 2016.

The Company's features

Strengths include that it utilizes its proprietary templates and its consulting capabilities.
Also Promoting new value creation with platform business

1. The foresight to read the future

The sources of the Company's strength can be said to be its ability to forecast future trends and the foresight to act ahead of other companies. It predicted the future potential of ERP in the mid-1990s, when it was still not in widespread use. Within the industry, it was the first to quickly focus on establishing a foundation for and expanding ERP-related business, starting with SAP. Therefore, the Company has accumulated an abundance of results and expertise. For the DX promotion business, amid the acceleration of digitization and with an eye to companies' business reforms, the Company has also been working to construct a proprietary platform business by utilizing new technologies, including IoT, blockchain, and AI.

2. Utilizing its proprietary templates with an abundant track record of ERP implementation

As previously explained, the Company has accumulated a track record for many ERP implementations by acting ahead of other companies. It has implemented it into more than 220 companies, mainly in the manufacturing industries, such as electrical and electronic equipment, precision machining, machinery, and chemistry. It has also accumulated expertise from this abundant track record and experience, which it has consolidated into the Fact Series, its proprietary templates customized to industry and work task. It uses these templates to provide functions with no waste that are tailored to meet the needs of each industry at low risk, in a short period, and at low cost, which is a factor that significantly differentiates it from other companies. The templates also function as a bridge between ERP and big data for peripheral solutions, and they go beyond the boundaries of ERP and generate various effects, such as improving work efficiency, speeding up processes and reducing costs. It can be said that this has led to its excellent results. For example, the Company has continually received awards from major vendors.

3. A workforce that supports the high-quality consulting capabilities

For workforce that supports the Company's consulting capabilities, which is another of its strengths, it focuses on developing multitalented employees who are fluent in other languages, have a global mindset, and are able to multitask, as well as always keeping in mind global business development (supporting the overseas business development of customer companies) in addition to providing high-quality services. It is also maintaining the number of staff who hold certifications from various vendors* at an extremely high level.

* The Company has 221 SAP certified consultants (as of the end of April 2021).

4. Realizing high profitability while also conducting upfront investment for the future

Utilization of proprietary templates and high-quality consulting capabilities mentioned above underpin the Company's robust productivity and added value, and the Company achieves profit margin exceeding the industry average while covering upfront costs that invest in the future, such as reinforcement of big data and related areas and construction of a proprietary platform. In other words, its high profitability is the source of the funds for the developments that will be the next earnings drivers, and it is establishing an ecosystem toward realizing sustainable growth.

5. Operations that comprehensively support corporate DX

It is said that the key to the successful digital transformation, which will determine the success or failure of companies in the future, is linking it to ERP and CRM. Therefore, the Company's many achievements and expertise in the ERP and CRM fields are considered to be a major advantage for it in terms of the utilization of big data and the development of the DX promotion business. In particular, the Company is one of only a select few companies in the industry in Japan to have established a comprehensive support structure by integrating the ERP and CRM and big data fields. Starting with industry-optimization platforms (CBP), it is highly likely that this will be a differentiation factor toward business expansion for the Company in the future.

Results trends

Realized higher sales and profits, exceeding the initial estimate, in FY3/21
Investments in corporate ERM and CRM continue to be strong

1. Overview of FY3/21 consolidated results

The Company reported sales and profit increases in FY3/21 consolidated results with ¥8,197mn in net sales (+6.8% YoY), ¥924mn in operating income (+227.2%), ¥958mn in ordinary income (+211.5%), and ¥661mn in net income attributable to owners of the parent (+407.1%), beating the initial estimate.

In a market environment with a mix of tailwind for the DX trend in digital demand through efforts to address COVID-19 and curtailment of IT investments on concerns about weaker economic activity, it posted all-time high sales in a third straight fiscal year due to upbeat corporate investments in ERP and CRM systems and the sales boost from a full-year contribution by ACK Co., Ltd. added to the Group in January 2020.

In earnings, the Company realized a steep increase, despite higher personnel costs related to bolstering human resources* and continued upfront costs for the platform business (CBP), on a recovery from FY3/20 when profit dropped sharply on losses from a specific project (one-time factor), extra profit on the increase in sales, and curtailment of spending related to the pandemic (mainly due to activity restrictions). Operating margin improved to 11.3% (vs. 3.7% in FY3/20), a return to the level from FY3/19.

> * Consolidated employees climbed to 511 people in FY3/21 (+82 people versus end-FY3/20), mainly on robust hiring of new university graduates (about 40 people) and aggressive hiring of IT personnel aimed at strengthening the CRM business at consolidated subsidiary Lirik Infotech Private (India-based development site).

In fiscal conditions, total assets expanded 9.4% versus end-FY3/20 to ¥6,550mn on increases in cash and deposits, accounts receivable - trade, and investment securities (valuation gain). In shareholders' equity, meanwhile, the equity ratio increased to 75.6% (vs. 72.6% at end-FY3/20) on 13.8% YoY expansion to ¥4,950mn due to build-up of retained profits and increase in valuation difference on available-for-sale securities.

Overview of FY3/21 consolidated results

(¥mn)

	FY3/20 results		FY3/21 results		Change		FY3/21 Initial estimate		FY3/21 revised estimate (2021/1/29)	
	Amount	Composition ratio	Amount	Composition ratio	Amount	%	Amount	Composition ratio	Amount	Composition ratio
Net sales	7,677		8,197		519	6.8%	7,900		8,000	
Cost of sales	6,081	79.2%	5,764	70.3%	-317	-5.2%	-	-	-	-
SG&A expenses	1,313	17.1%	1,509	18.4%	195	14.9%	-	-	-	-
Operating income	282	3.7%	924	11.3%	641	227.2%	800	10.1%	900	11.3%
Ordinary income	307	4.0%	958	11.7%	651	211.5%	820	10.4%	920	11.5%
Net income attributable to owners of the parent	130	1.7%	661	8.1%	530	407.1%	554	7.0%	630	7.9%
Total assets	5,990		6,550		560	9.4%				
Shareholders' equity	4,348		4,950		601	13.8%				
Equity ratio	72.6%		75.6%		3.0pt	-				

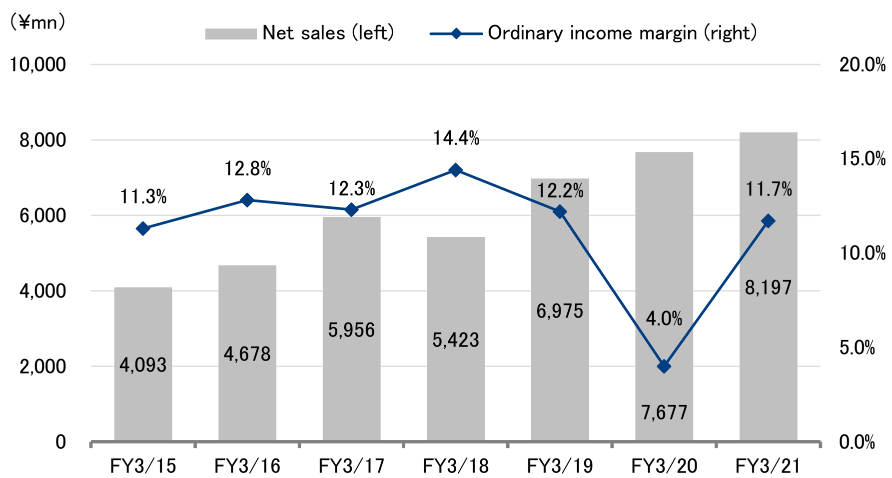
Source: Prepared by FISCO from the Company's financial results summary report, financial results briefing materials, securities reports, and releases

Sales and profits steadily improved in FY3/20 excluding special factors

2. Past results trends

Looking at past consolidated results, growth accelerated from FY3/16 on the ramp-up of big data business and expansion of overseas sales. Sales declined temporarily in FY3/18 because TDSE was removed from the scope of consolidation. But sales started to increase significantly in FY3/19 due to the expansion of the ERP and CRM businesses on the back of the Company's strong willingness to invest. So, the Company's results can be evaluated as steadily growing. In earnings, the Company set all-time highs (operating and ordinary incomes) in five straight years through FY3/19 and maintained profit margin at a level substantially exceeding the industry standard (while profits slipped in FY3/20 due to one-time special factors, as explained above, they recovered in FY3/21).

Trends in consolidated net sales and the ordinary income margin

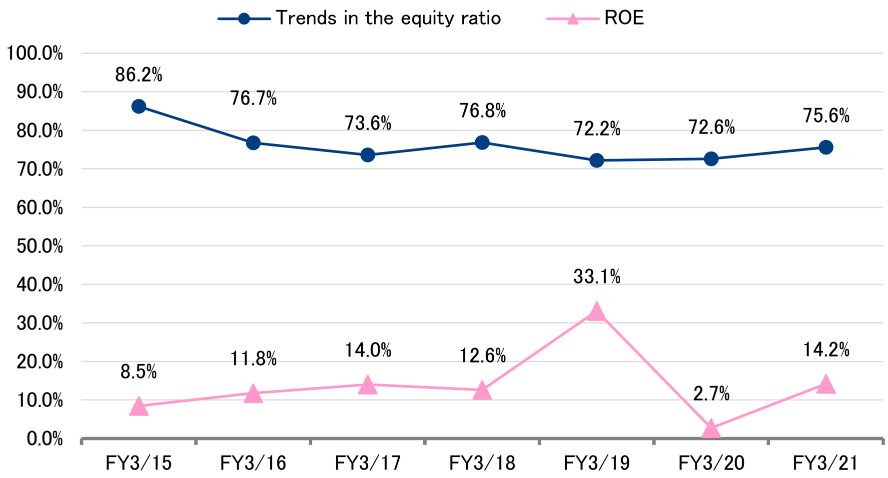


Source: Prepared by FISCO from the Company's financial results summary and financial results briefing materials

In financial conditions, the equity ratio, which reflects soundness of the financial base, remained at a high level and ROE, an indicator of capital efficiency, was above 10%. These levels demonstrate very healthy financial conditions. The large shift in ROE from 33.1% in FY3/19 to 2.7% in FY3/20, as already mentioned, reflected a variety of temporary special factors* and does not constitute a change in fundamental profitability (capital efficiency). ROE recovered to 14.2% in FY3/21.

* The Company booked profit from selling shares of an affiliate (TDSE) in FY3/19 and recognized project losses for a specific project in FY3/20.

Trends in the equity ratio and ROE



Source: Prepared by FISCO from the Company's financial results summary report

Main topics

Began provision of "ordering and payment service (SaaS)" on the DX proprietary platform (CBP) in May 2021

1. Started industrial-academic joint research with the Kyushu Institute of Technology

In April 2021, the Company started industrial-academic joint research with the Kyushu Institute of Technology with a theme of "research on systematizing operational knowledge for commercial flow and logistics and related application." This initiative involved opening a satellite office to perform lab functions at the New Industry Creation Assistance Center in Iizuka (Fukuoka Prefecture) (e-ZUKA Tri-Valley Center) as the Tecnos Japan e-ZUKA innovation lab. By combining the Company's knowledge on commercial flow and logistics business and knowhow related to systemization of human knowledge possessed by the Kyushu Institute of Technology School of Computer Science and Systems Engineering*, this project aims to support efficient use of limited resources and reduce waste through detection of problems that occur in commercial flow and logistics, mechanization of knowledge and experience related to solving these issues, and suitable application of the PDCA cycle.

* The Kyushu Institute of Technology School of Computer Science and Systems Engineering organizes advanced specialized knowledge of experts into a format that can be handled by computers and is implementing R&D aimed at putting this information into a knowledge-based system in various fields. Working through a venture launched by the Institute as part of industry-academic collaboration, these activities have led to commercialization of knowledge processing service built into mobile phone customer management systems, manufacturing process design assistance systems, and other systems.

2. Began provision of "ordering and payment service (SaaS)" on CBP

In May 2021, the Company began provision of "ordering and payment service (SaaS)" on its DX proprietary platform (CBP). This service targets "advanced transaction activities" and "advanced DCM (demand control management) and SCM (supply control management)" through shared data distribution and management covering the full range of transaction tasks (supply-demand adjustment, ordering, shipments and inspection, invoicing, and payment) with partners via SaaS*. Additionally, provision as SaaS (cloud service) offers an environment for utilization by smaller businesses too, not only large companies. The Company wants to contribute to realization of a sustainable society (reduction of disposal losses, lighter environmental load, alleviation of climate change, etc.), along with strengthening corporate competitiveness, through promotion of DX in society as a whole. It hopes to reach usage of 1mn cumulative transactions in three years by FY3/24.

* The Company confirmed the utilization effect through trial application and preparations within the group since 2020 that realized improvement of 15% in work processing steps and 20% in work processing man-hours.

3. Obtained recognition as a DX-certified operator as defined by METI

In June 2021, the Company obtained recognition as a DX-certified operator* as defined by Ministry of Economy, Trade and Industry (METI). The main reason appears to be positive assessment of the Company's initiative in stipulating the direction of its business vision and model with consideration of the impact of changes in society and the competitive environment driven by digital technology and disclosing these views to stakeholders. Certification is likely to give a major boost to the Company, which positions DX advances at companies and in overall society (supply chain) by combining ERP, CRM, and CBP as the core of its growth strategy.

* Based on the Act on Facilitation of Information Processing implemented on May 15, 2020, METI founded a program in which the national government certifies companies that promote initiatives in accordance with the "Digital Governance Code" defined by METI and are DX-Ready (companies ready to change their businesses through digitalization).

Results outlook

Expects continued increases in sales and profits in FY3/22 driven by IT investment demand accompanying DX initiatives

1. FY3/22 results forecasts

In FY3/22, the Company guides for sales and profit gains with ¥8,750mn in net sales (+6.7% YoY), ¥1,020mn in operating income (+10.4%), ¥1,055mn in ordinary income (+10.0%), and ¥710mn in net income attributable to owners of the parent (+7.4%).

Despite taking a cautious view of prolonged pandemic impact on investment activity, it forecast higher sales mainly driven by assisting deployments of ERP and CRM systems amid anticipated pick-up in IT investment demand related to corporate DX rollouts.

In earnings, it expects to increase profits, even with its current positioning in an upfront investment stage in platform (CBP) business, mainly on the positive effect of higher sales, and reach the ¥1bn level in operating (and ordinary) incomes for the first time. It also forecasts modest improvement in operating margin to 11.7% (vs. 11.3% in FY3/21).

FY3/22 forecast

(¥mn)

	FY3/21 Results		FY3/22 Forecast		Change	
	Amount	Ratio	Amount	Ratio	Amount	%
Net sales	8,197		8,750		553	6.7%
Operating income	924	11.3%	1,020	11.7%	96	10.4%
Ordinary income	958	11.7%	1,055	12.1%	97	10.0%
Net income attributable to owners of the parent	661	8.1%	710	8.1%	49	7.4%

Source: Prepared by FISCO from the Company's financial results summary report

2. FISCO view

Despite recognizing the need to continue focusing on the impact of corporate investment stances by the prolonged pandemic, FISCO expects the forecasts are sufficiently attainable considering external factors (such as stimulation of IT investment demand through DX advances) and internal factors (such as Company advantages in ERP and CRM and orders backlog situation *). Key points are ramp-up of "ordering and payment service" on its platform (CBP) as a future growth axis and deployment in proprietary DX business through collaboration with ERP and CRM, the Company's strengths. While it is necessary to wait over the medium term until full-fledged operation, the Company should present specific results and direction for this business.

* Orders backlog at end-FY3/21 was up 17.1% YoY to ¥1,697mn.

The industry environment

Mixed market environment of curtailing investments in the pandemic and investment demand to implement DX. Expecting full-fledged DX deployments over the medium term

1. ERP and CRM business trends

According to a market research company, the ERP market in Japan is expanding robustly on the back of steady investment in core systems, mainly by major companies. Investment in ERP continues to be stable. In particular, Cloud ERP, which entails provision on the Cloud (SaaS) or package operations (IaaS), is on a rapid growth trajectory. A focal point in the future, meanwhile, is the 2025 problem*. In other words, while the shortage in IT human resources in Japan will increase to approximately 430,000 people, full-scale development of DX is expected alongside the acceleration of digitalization, and ERP will also shift to comply with DX, including utilization of big data. ERP switching needs might occur later than initially expected (or proceed at a more moderate pace), alongside COVID-19 measures, following the decision by SAP, which is the largest ERP company, to delay its end of support for conventional ERP from 2025 to 2027. Nevertheless, interest in DX realization has risen and there is considerable focus on creating added value for the future.

> * The "2025 Cliff" DX report released by METI in September 2018 warned that companies would be unable to succeed in global business competition unless they revamped legacy systems and realized DX by 2025. In DX Report 2 (interim review) issued in December 2020, METI cited "formation of cooperative areas and development of a shared platform with industry peers," in addition to "platforms covering non-competitive areas," as a longer-term theme. This matches the Company's direction.

2. Impact by COVID-19

Regarding the impact by COVID-19, while decline in corporate capital investments and cautious stances accompanying weaker earnings are a concern, digital demand as a way of responding to the pandemic, such as IT investment demand for DX deployments and remote work support, has risen. Furthermore, some observers project acceleration of the digital trend thanks to a surge in social structure reforms (changes in workstyles and business models) for the post-pandemic environment (new normal). Companies need to make appropriate management decisions that address positive and negative aspects.

The growth strategy

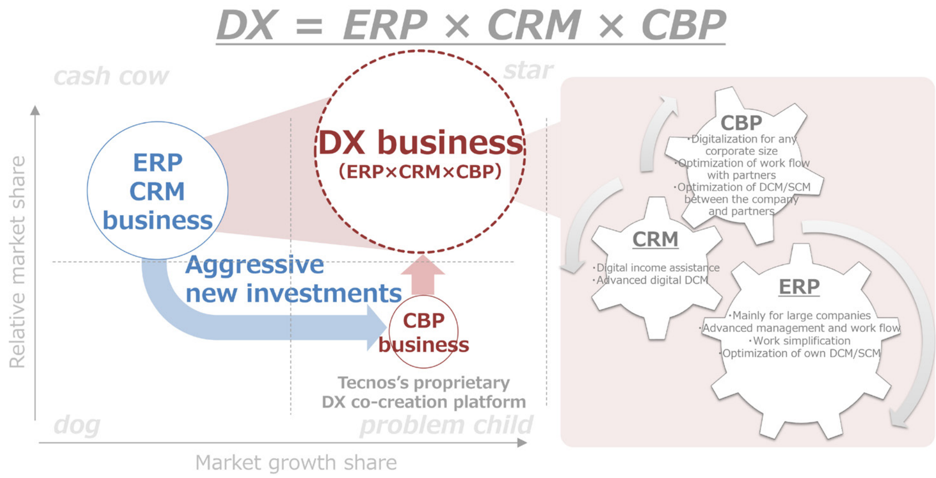
The Company aims to realize DX by building a proprietary platform. Promoting global business and investing in human resources

The Company's growth strategy has a direction (vision) of "LEAD THE CONNECTED SOCIETY TO THE FUTURE." Based on a mission of "Contributing to the development of society by connecting organizations, people, and data." In other words, in addition to deployment and switching of ERP (optimization at the individual-company level) using knowhow accumulated since its founding, it is strongly advocating the concept of an industry optimization-type platform business (optimization of the entire supply chain) that connects data among companies through collaborative creation with partner companies that have various cutting-edge technologies and deploying companies. It will combine ERP and CRM with its proprietary platform, and this will be the form of the digital transformation that the Company will progress. It has also set three points for the future investment areas towards growth, of "the platform business," "the global business," and "human resources and organizations."

1. Constructing a platform business

The Company is actively investing in constructing its proprietary platform (CBP), and also developing various services on this platform through collaborative creation, including with customer companies. Furthermore, it plans to promote business reforms at its customers by using AI and other technologies to utilize to the greatest possible extent the big data accumulated on this platform. The Company started provision of "ordering and payment service SaaS)" for its platform (CBP). Participating company benefits are simplification of workflow from orders to billing, improvement of supply chain efficiency, and flexible response to payment methods. Furthermore, the Company can steadily add new participants from a base of those who are connected and also benefits from acquisition of a recurring-type stable income source. While it is likely to continue in a phase of upfront costs for the time being, FISCO expects profitability in annual income within the next 2-3 years.

Policy for corporate management and work system business



Source: The Company's financial results briefing materials

2. Progressing the global business

The Company will accelerate business development for the North America market, based on the recently acquired business of Lirik. In particular, it intends to expand the commercial zone of this business from the current zone, which is focused on the West Coast of the United States. Its intention is to bring together the Company's and Lirik's strengths to expand the ERP x CRM x CBP business, while coordinating between Japan and North America. It will also acquire IT and AI human resources through strengthening Lirik's offshore base (India), while aiming to continue to discover and develop Silicon Valley's latest technologies.

3. Investment in human resources and organizations

The problem of the shortage of human resources in its industry is become increasingly severe, and in this situation the Company intends to actively recruit overseas human resources. The Company aims to accumulate a track record of recruitment results, while utilizing the Group's networks and various cultures in India and the North America. On the other hand, it is also focusing on training employees. In particular, it is working to develop global human resources, including sending its Japanese employees to the overseas bases it has acquired (in the US and India). In April 2019, it newly established the Innovation Center in Tokyo (Nihonbashi). In addition to securing excellent human resources, its aims include developing human resources, establishing an environment to promote innovation, and making advances in telework. It is also recruiting partners that include venture companies with the latest technologies.

Despite lingering uncertainty about the impact by the prolonging of COVID-19, FISCO sees latent growth potential exceeding 10%, even just in ERP and CRM business, including DX responses, excluding this factor. A longer-term point hence is how much the Company is capable of adding to this growth through platform business, a strategic area. In particular, platform business faces less constraint (human resources, etc.) on expansion than ERP and CRM businesses up to now and offers potential for a positive cycle in which rising recruitment of participants further enhances platform value (network externality). It is necessary to evaluate growth curve and income structure changes in a few years considering sudden increase in profitability when sales exceed the breakeven point and collaboration upside in ERP and CRM business (joint deployments). Even with the need to continue monitoring positive and negative aspects of pandemic impact, structural reforms for realizing DX have become an issue that needs to be addressed by not only companies but also society. Finding solutions to social issues hence should be seen as a major opportunity for the Company to drive its own growth. FISCO intends to focus on progress in full-fledged operation of platform business and also creation of new value, including collaboration with partner companies and others. Furthermore, the Company's promotion of global business is sufficiently attainable given its track record with global standard systems (SAP and salesforce) and utilization of human resources obtained through the Lirik acquisition (including the development site in India) and sales channels (in North America). The extent to which the Company can horizontally apply knowhow and human resources accumulated in domestic platform business to global activities is likely to dictate future potential. The largest bottleneck, meanwhile, is securing personnel, a common issue for the industry. From this perspective too, development of platform business with few personnel constraints, related creation of knowledge-intensive business, and recruitment of overseas human resources are important strategies for the Company.

Shareholder returns policy

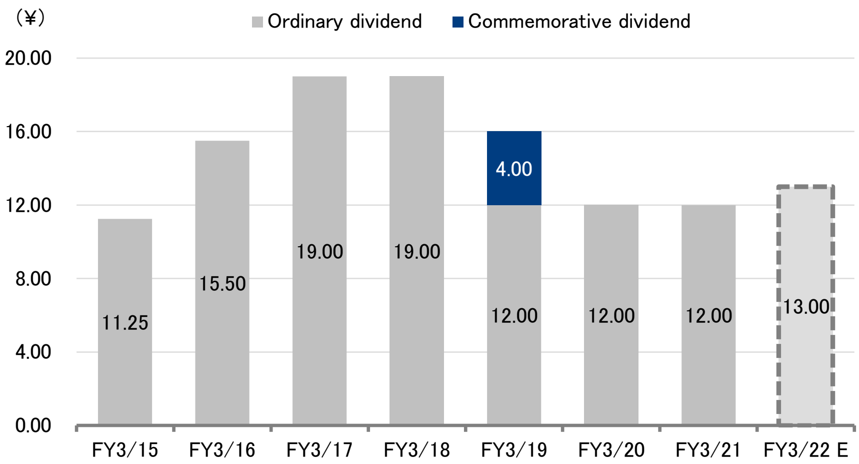
Paid a ¥12 dividend per share in FY3/21
Plans to raise the dividend by ¥1 YoY to ¥13 in FY3/22

The environment surrounding the Company's industry is changing greatly. In such a situation, its policy for the future is to increase the allocation of funds to growth investment while also returning profits to shareholders by considering profits-linked factors. Specifically, as the dividend to return profits to shareholders, it has set a target of 35% or above of "the deemed dividend resource (deemed net income*)" of consolidated ordinary income adjusted by the effective tax rate. In addition, it has positioned the acquisition of treasury shares as a measure to supplement the dividend to return profits to shareholders, and it is flexibly acquiring them according to cash flow conditions and other factors.

* The deemed dividend resource (deemed net income) = consolidated ordinary income x (1–effective tax rate).

For the FY3/21 dividend per share, the Company paid a ¥12 ordinary dividend. The Company plans to raise the dividend per share by ¥1 YoY to ¥13 in FY3/22.

Trend in the dividend per share



Note: Dividend values for FY3/16 and earlier retroactively apply stock splits of 1-to-2 shares for ordinary shares implemented by the Company on May 1, 2016 and December 17, 2016.
Source: Prepared by FISCO from the Company's financial results summary report

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