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■ Top-class profitability even among franchises

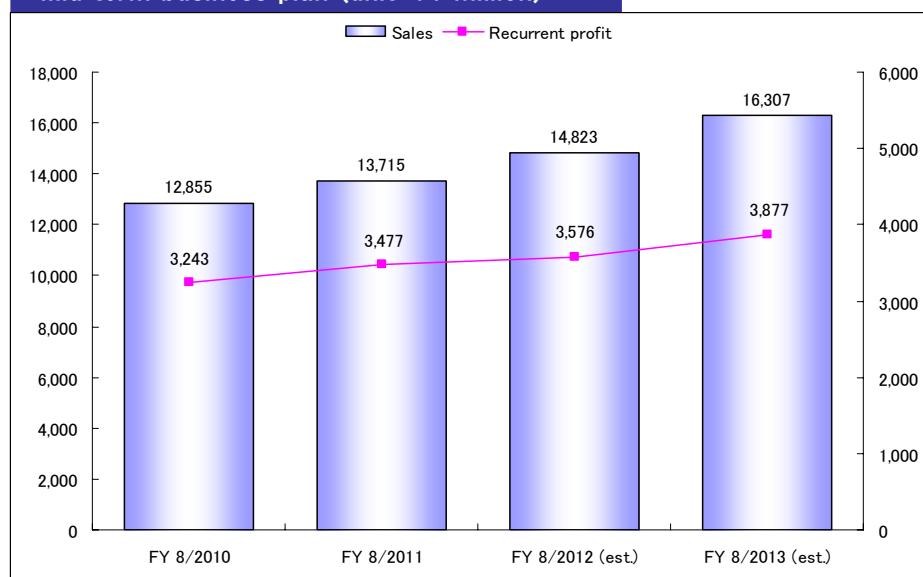
Focusing on developing individual tutoring schools (such as Meiko Gijuku), the firm is top class in profitability among franchise businesses. By franchise development, the number of schools exceeds 2,000, with basics to sustain expansion in the future. Further, 2011 saw the start of new businesses including *Kobetsu* (individual) School, positioned as a tutoring school for students seeking to enter higher-level schools, and Meiko Kids for after-school education and childcare. By employing the franchise system, the company plans to make rapid progress and expand profits further through a business alliance with ALC, which has extensive experience with English language schools, and plans to develop a transverse axis of franchises on the foundation of the tutoring schools.

In the three-year mid-term management plan announced in October 2010, targets were set for total sales of ¥16307 million and current profits of ¥3,877 million by August 2013, and by August 2011, the end of the first year of the plan, current profits advanced at a pace exceeding the three-year plan by 6.7%. If the new businesses succeed, one can anticipate further growth to come. The firm is attracting attention for actively pursuing return to shareholders. In concrete terms, it is aiming for a dividend payout ratio of approximately 35%, and to date, it has increased dividends for 13 consecutive terms. For the fiscal year ending August 2012, estimates are for a per-share dividend of ¥25, a ¥3 increase over the previous term.

■ Points

- Expansion at a pace of 100 schools per year despite declining birthrates
- Each franchise school maintains stable management by efficient operations
- Comparison with promising franchises is more valid than comparison with other private tutoring schools

Mid-term business plan (unit: ¥1 million)

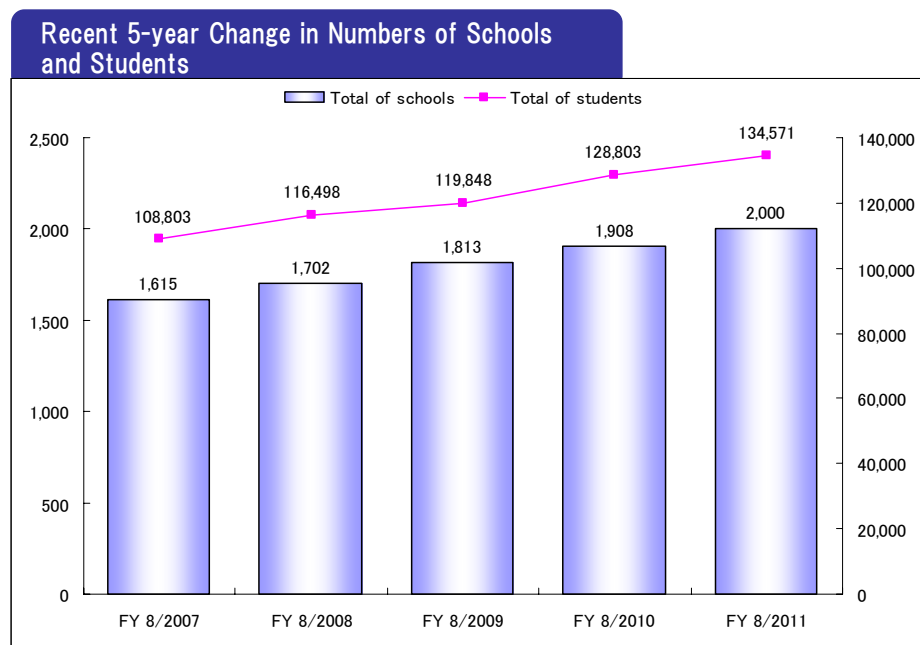


Business information

Despite declining birthrates, expansion at a pace of 100 schools per year

In 1984, current president and representative director Hirotake Watanabe founded Meiko in Tokyo with the goal of developing a nationwide franchise chain of individual-tutoring cram schools for all grade levels. Under the brand name Meiko Gijuku, it started with 17 schools, including both franchised schools and directly-operated schools.

By 2002 the company exceeded the benchmark of 1,000 schools, reaching 1,500 in 2006, and 2,000 in 2011 (with 215 directly-operated schools and 1,785 franchised schools, as of August 2011). With more than 130,000 students, the business stands at the top of the industry in number of schools and number of students (excluding home schools such as KUMON and Gakken schools).

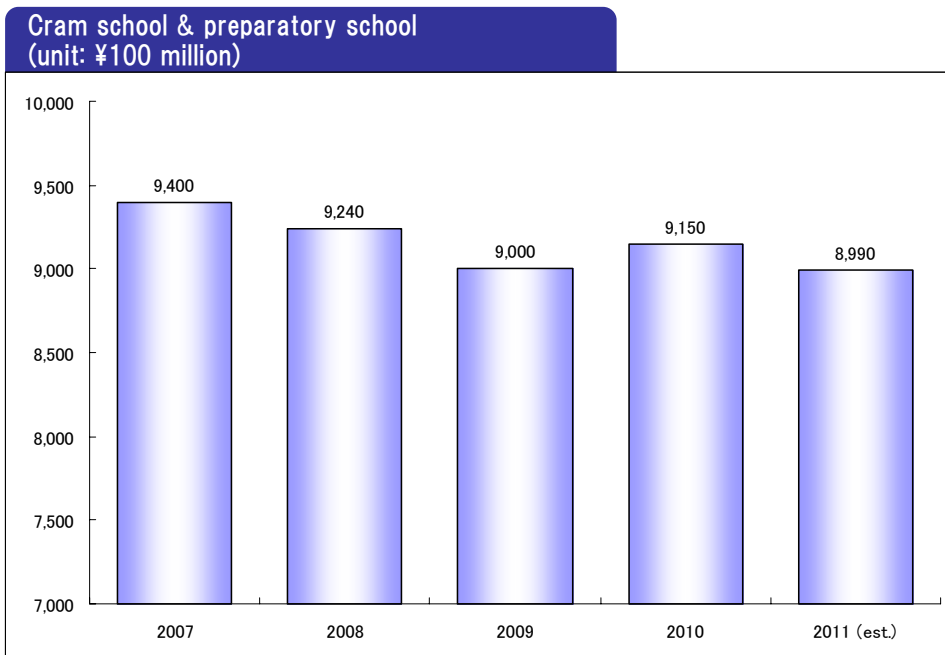


The distinctive feature of Meiko Gijuku is that it targets every level of schooling from elementary school through high school. In addition, its fundamental concept is to have one instructor provide guidance for learning to three students at the same time. Based on the educational philosophy of “self-motivated learning,” its most basic concept is to enable students to acquire study habits through which they can learn on their own. For this reason, the majority of target students come from the middle ranks in terms of learning and school performance, making it distinct from cram schools aimed at advancement to difficult-to-enter schools.

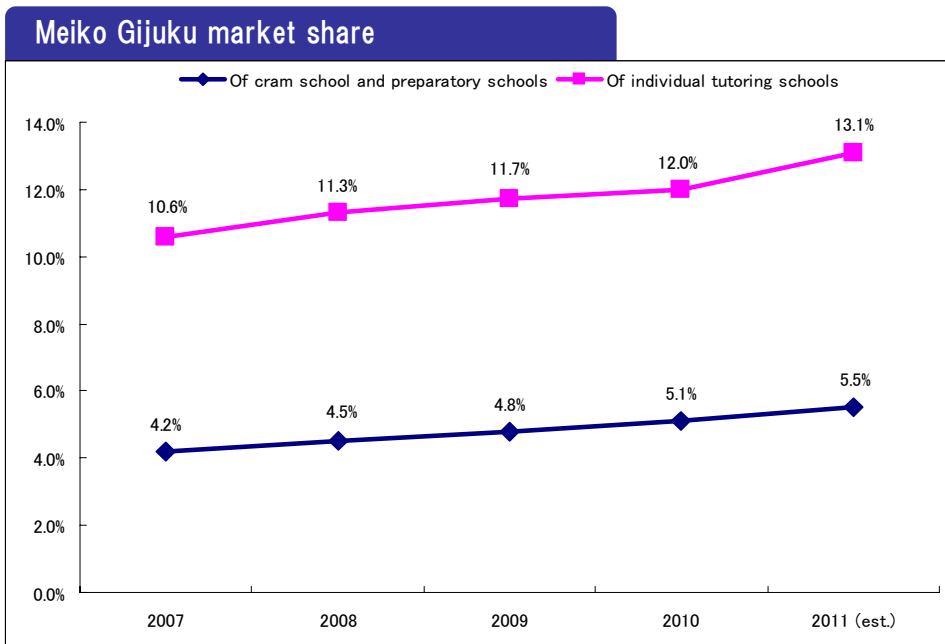
During the past few years, as shown in the graphs, the tutoring school market has shown a small decrease along with the declining birthrate, and yet the company, while expanding the scale of its business at the rate of 100 schools per year, continues to increase sales by an average of 6%, thereby steadily increasing market share.



Business information



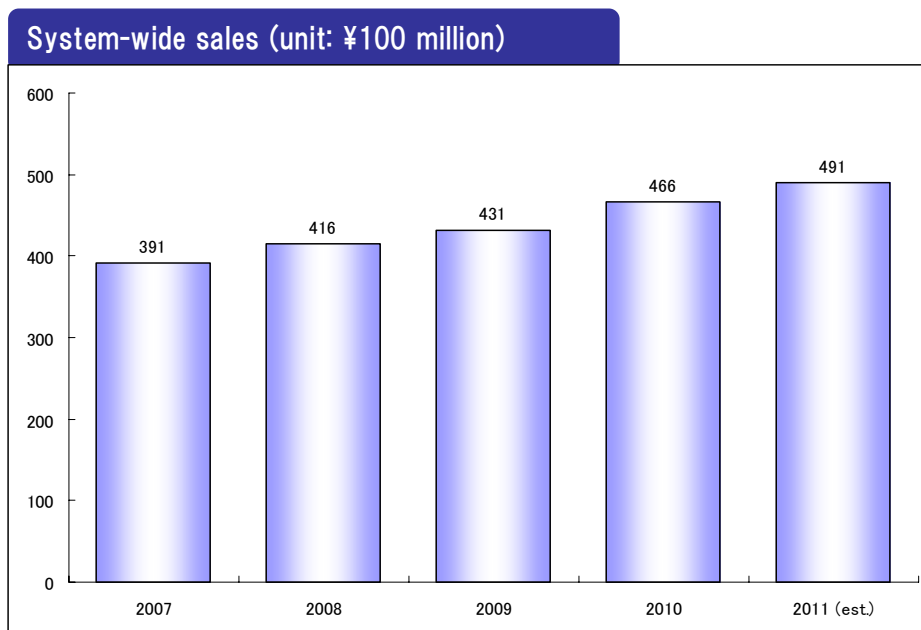
Source: Yano Research Institute Ltd., *Kyoiku Sangyo Hakusho 2011 nendo*, Revenue base of industries



System-wide sales volume divided by market scale (calculated from Yano Research)



Business information



Note: "System-wide sales" includes the entire sum of enrollment fees, teaching material fees, and testing fees of directly-operated schools; total sum of enrollment fees, tuition fees, etc. from franchise schools; but does not include sales of educational and test materials from franchise schools.

The firm is developing businesses other than Meiko Gijuku, including the following: Waseda Academy Kobetsu School, which started with the 2010 tie-up with Waseda Academy in order to incorporate the latter's operational skills in the development of individual tutoring schools; Meiko Kids, which combines the functions of childcare after school hours with that of a tutoring school; Abrakadoodle art studio, an art education program aiming at enhancing the creativity and powers of expression of children ages 20 months to 12 years; and Meiko Soccer School, whose schools nurture children's soccer skills. In addition, Tokyo Ishin Gakuin, a preparatory school for those seeking entrance to medical-related universities, was purchased in 2009 and now operates as a subsidiary.

Performance trends by business (unit: ¥1 million)

Sales by business	FY 8/2007	FY 8/2008	FY 8/2009	FY 8/2010	FY 8/2011	YOY
Meiko Gijuku directly-operated schools	5,334	5,711	6,004	6,288	6,575	4.6%
Meiko Gijuku franchise schools	4,971	5,442	5,740	5,846	6,403	9.5%
Preparatory school	-	-	-	634	594	-6.2%
Other businesses	79	81	80	87	144	64.5%

Operating profits by business	FY 8/2007	FY 8/2008	FY 8/2009	FY 8/2010	FY 8/2011	YOY
Meiko Gijuku directly-operated schools	-	-	-	1,128	1,315	16.6%
Meiko Gijuku franchise schools	-	-	-	3,056	3,256	6.6%
Preparatory school	-	-	-	41	8	-81.4%
Other businesses	-	-	-	7	-174	-
All businesses expenditures	-	-	-	-1,123	-1,042	-



■ Strength of franchise development

Each franchise school maintains stable management by efficient operations

The growth of the domestic tutoring school market is reaching an upper limit, and one of the reasons why this firm has continued to grow—during a period of restructuring and weeding out—is the successful functioning of its franchise system. The franchise system itself widely permeates a wide range of business sectors—including retail sales, restaurants, and the service industry—and the cram school business is no exception.

To franchise head offices such as this company, the benefit of the franchise system is that it enables rapid expansion of business operations at low cost. Further, because one can rely on stable royalty income from franchise contracts, one can keep business risk at an absolute minimum. On the other hand, for the franchisee (member), it is possible to absorb the necessary know-how through the company's service training system, which the head office implements in order to convey the essential management skills required to take a school from start-up to going concern. Therefore, it has the merit of improving the ability to attract students because of the strength of the Meiko Gijuku brand and the marketing power of the head office, thereby putting operations on the right track within a comparatively short period of time.

Within the Meiko Gijuku franchise system, although the company introduced a fee system that is inexpensive in comparison with other companies, by means of efficient operations, each franchised school is able to carry out stable operations. In-service training is facilitated by various training programs for new owners, including owners' club training sessions, regularly scheduled block training sessions, and training sessions for head teachers and new instructors. Further, there is vigorous exchange of information between member owners. As of August 2011, there were 481 owners, of which 53.2%, more than half, operate more than one school.

The break-even point for a single school is 40 students, and that number drops to 28 students when the owner also functions as head of the school. In the fiscal year ended August 2011, the average number of students for franchise schools nationwide was 67 students, with average royalty sales of over ¥2.35 million per school remaining stable over the past several years, which means that, in general, operating conditions are favorable. Consequently, with the number of schools increasing at the rate of 100 per year—of which 80% are operated by successful prior owners who are reinvesting in the business—a favorable cycle has formed in which newly created schools get on track early on in their operations.

Figures for franchise schools

Franchise schools index	FY	FY	FY	FY	FY
	8/2007	8/2008	8/2009	8/2010	8/2011
Average of students per school	66.4	67.6	65.7	67.3	67.0
Royalty income (¥1 million)	3,078	3,344	3,542	3,747	4,089
Average royalties sales per school (¥1000)	2,216	2,285	2,266	2,267	2,352

*Royalties are 10% of each franchise school's revenues



■ Growth strategies

Commitment to expanding student strata by increasing quality and number of schools and advancing into new business areas

The company has announced new strategies for the 3-year mid-term management plan issued in October 2010. As the framework for its growth strategy, in addition to the expansion of profits through the increase in the number of schools using the existing Meiko Gijuku franchise system, the plan calls for increasing the number of students per school and the number of classes offered at each school, yielding an increase in the profits of each school. Moreover, in order to build the foundations of the second and third enterprises, the firm is addressing the issues of launching into new business areas in order to expand customer strata.

The new enterprises include the previously mentioned Waseda Academy Kobetsu School, Meiko Kids, Abrakadoodle, and Tokyo Ishin Gakuin, and in addition to these, attention should be given to the business and capital alliance with ALC in the development of English schools. The customer strata of Meiko Gijuku has mainly been the group from the 4th year of elementary school through the 3rd year of high school, with the volume zone being students whose performance at school is in the middle of their respective classes. In addition, the firm is broadening its target age range at a single stroke from the lower age levels, which begins with Meiko Kids and Abrakadoodle, to the high-school level, including students attending preparatory schools aiming for medical-related universities and, through the alliance with ALC, plans for expanding into English language schools. A basic description of these ventures is as follows.

(1) Waseda Academy Kobetsu School

As to the Waseda Academy Kobetsu School, in January 2011, two directly-operated schools were established in Saitama Prefecture (while Waseda Academy established one directly-operated school), and preparations are underway for the development of franchises. The key issue here will be how successful the educational affairs know-how of Waseda Academy, which has a proven record of achievements in the operation of group-style instruction preparatory schools, can be integrated with the know-how of the firm's individual-tutoring style of instruction.

(2) Meiko Kids

Meiko Kids opened one school in Tokyo in February 2011. In December the firm announced a business alliance with Tokyu group's Kids Base Camp, which has a track record of achievements within the same business category. The content of this alliance is to fuse the operations skills and ability to develop program contents of the Kids Base Camp with the skills of the firm in operating individual-tutoring schools and in franchise development, in advancing a new business category which strengthens and combines the functions of tutoring school, after-school childcare, and other types of lessons, while cultivating a new customer base. These developments warrant attention during the years to come, as the number of households in which both parents work increases and the needs for such new types of business become even more apparent.

■ Growth strategies

(3) Abrakadoodle art studio

Abrakadoodle is an art education program, founded in 2002 in the U.S., which seeks to enhance children's creativity, expressive ability, and sense of independence by means of having children create pictures and paintings and having presentation about the art work. The target age is 1-12 years old. At present, two studios are under development, each with approximately 20 students. Because the degree of interest in art education is low in Japan, not much attention is paid to this business, but it is a popular educational program in the U.S., and currently consideration is being given to the possibility of developing the business together with ALC English schools with which the firm has business ties.

(4) Tokyo Ishin Gakuin

Acquired in 2009, Tokyo Ishin Gakuin has a 34-year tradition as a preparatory school specializing in preparing applicants for entrance exams to medical-related universities. At present, it directly operates 4 schools in the Tokyo metropolitan area and 1 in Yokohama, and 2 of these are wholly dormitory-residence system schools. The core student stratum is children of physicians in private practice.

The firm remains fully committed to developing these businesses and, by the end of the original mid-term plan in August 2103, is aiming at raising the level of sales in enterprises other than Meiko Gijuku enterprises to a level that is 10% or more than the total overall sales of the firm.

Mid-term Business Plan (unit: ¥1 million)

	FY 8/2010	FY 8/2011	FY 8/2011	FY 8/2012	FY 8/2013
	Results	Projection	Results	Projection	Projection
Sales volume	12,855	13,711	13,715	14,823	16,307
Meiko Gijuku	12,134	12,838	12,977	13,624	14,496
Tokyo Ishin Gakuin	633	700	594	850	1,000
Soccer School	87	90	93	95	99
Waseda Academy Kobetsu School	-	66	45	146	496
Meiko Kids etc.	-	15	4	107	214
Recurring profit	3,243	3,258	3,477	3,576	3,877
Term net profit	1,897	1,768	1,922	2,030	2,206

■ Overview of first quarter of FY 8/2012

Prior investment for relocation and renewal virtually as projected

According to the settlement of accounts for the first quarter (September to November) of FY 8/2012 announced on January 10, sales revenues amounted to ¥3,009 million (an increase of 2.8% YOY), operating income amounted to ¥550 million (a decline of 11.4% YOY), current profits amounted to ¥583 million (a decline of 11.2% YOY), and net quarterly earnings amounted to ¥333 million (an increase of 1.3% YOY).

Against a background of continuing decline in birthrates and decreasing market scale within the private tutoring school industry as a whole, the expansion of the number of schools and the number of registered students resulting from franchise development enabled sales to continue to serve as the base of increased revenue. However, due to the burden of prior investment in new businesses and the increased investment resulting from relocation and remodeling of schools directly operated by Meiko Gijuku, both operating profits and recurring profits declined. In regard to net quarterly profits, the special loss calculated in the same quarter of the previous year resulting from the impact of the expenditures arising from the application of asset exclusion liability accounting standards were eliminated, therefore increased profit was shown. In terms of the performance outlined in the company's plan, performance is virtually on track and consequently projected results for the first half (September 2011 to February 2012) and full year to August 2012 remain as initially planned. Trends for respective sectors are outlined in the following.

(1) Directly-operated Meiko Gijuku business

For the directly-operated businesses, total sales increased 2.4% over the same period of the previous year to ¥1,372 million, while operating profits declined 54.6% to ¥74 million. Over the same period of the previous year, the number of schools increased by 3.8% (218 schools) and the number of students increased by 6.9% (16,098 students), yet average sales per student declined 4.2%, as a result of which, sales revenues were somewhat sluggish. In terms of profitability, in addition to this sluggishness, as a result of maintaining school facilities so that students can comfortably attend and actively relocating and remodeling facilities, a temporary increase in expenditures resulted in a double-digit decline in profits.

(2) Meiko Gijuku franchise business

For the franchise business, sales increased 2.9% over the same period of the previous year to ¥1,464 million, while operating profits rose 7.7% to ¥836 million. As a result of securing at an early stage facilities for potential development of schools and picking out possible operators from among current owners, the number of franchise schools grew 5.8% over the same period of the previous year to 1,808 schools, while the number of students continued to expand by 3.3% to 130,030 students.



(3) Preparatory school business

The sales revenues of the firm's consolidated subsidiary Tokyo Ishin Gakuin declined by 13.4% over the same period of the previous year to ¥123 million, while experiencing an operating loss of ¥5 million (whereas the previous year was a ¥5 million gain). The reason for this was that as a result of the Great East Japan Earthquake Disaster and the nuclear power station accident, those in the provinces who had planned to enroll in 2011 cancelled in rapid succession. Student recruitment for spring 2012 is being promoted via school guidance fairs, website portals for those aiming at employment in medical fields, and advertisement campaigns in specialty magazines – all aimed at increasing the number of enrollments.

(4) Others

The new business operations—including Meiko Soccer School, Waseda Academy Kobetsu School, Meiko Kids, and Abrakadoodle—had a 118.2% increase in revenues, expanding favorably to ¥48 million. However, due to the increase in initial investment, operating losses rose slightly to ¥32 million (compared with ¥17 million in the previous year). Further, in regard to initial launching of English education business, the firm signed a business and capital tie-up agreement with ALC last July, and currently negotiations are underway to establish an operations alliance advancement committee to establish a new type of English school and construct a business model for such operations.

Quarterly trends by business (unit: ¥1 million)

Sales by business	1Q11	2Q11	3Q11	4Q11	1Q12	YOY
Meiko Gijuku directly-operated schools	1,340	2,115	1,107	2,013	1,372	2.4%
Meiko Gijuku franchise schools	1,422	1,819	1,298	1,864	1,464	3.0%
Preparatory school	142	170	111	171	123	-13.4%
Other businesses	22	27	36	59	48	118.2%
Total sales revenue	2,928	4,128	2,552	4,108	3,009	2.8%

Operating profits by business	1Q11	2Q11	3Q11	4Q11	1Q12	YOY
Meiko Gijuku directly-operated schools	165	766	-119	504	75	-54.6%
Meiko Gijuku franchise schools	777	918	555	1,007	837	7.7%
Preparatory school	5	-3	-18	23	-5	-
Other businesses	-17	-63	-49	-45	-31	-
All businesses' expenses, amortization expense of goodwill	-309	-235	-239	-258	-325	-
Operating profit total	621	1,383	130	1,230	551	-11.4%

■ Performance outlook and Comparison with franchise-based business

Comparison with promising franchises is more valid than comparison with other private tutoring schools

The company's forecast for consolidated results for August 2012 are for ¥14,823 million net sales (an increase over the previous year of 8.1%), operating profits of ¥3,576 million (an increase of 6.3%), ordinary profits of ¥3,567 million (an increase of 2.9%), and current net profits of ¥2,030 million (an increase of 5.6%). These figures, however, are brought over unchanged from the values announced in the mid-term plan a year ago. The actual results for the first year, ending August 2011, when compared with the original plan, showed sales at approximately the same level and current profit at 6.7% with net profit at 8.8%, exceeding expectations. As a result, current fiscal year net sales advanced according to plan, and it is anticipated that in regard to profit, there may be a slight rise over expectations.

As to the valuation of the stock, when compared with the average estimated price-earnings ratio (PER) for this year of 11 for the 19 tutoring school businesses listed on the Tokyo Stock Exchange (based on each company's EPS projections), this company's PER is comparatively low at around 9. Compared with the valuation figures of key enterprises in other industries which are expanding through franchise development, such as convenience stores and restaurants, in addition to the projected PER in the graph, the dividend yield is attractive and in terms of profitability it appears top class.

As stated earlier, the development of Meiko Gijuku franchises, accompanied by an increase in the sales per school, supports a projection of expansion of profits. If franchise development in the new businesses also contributes to profits, then considerable performance and growth can be anticipated.

Further, the average current year PER (EPS based on company projections) for the 19 tutoring schools listed on stock exchanges stands at 11, while this firm's PER of 9 is below that average. Given the firm's distinctive franchise composition, comparisons of its performance transcend the framework of private tutoring schools alone. The declining birthrate has not just started, and from the viewpoint that the firm's results have expanded despite that fact, it would be more appropriate to compare its performance and projections with those of expanding franchise-based business such as convenience stores, restaurants and other service industries. In terms of anticipated PER and dividend yield, the firm is very appealing and belongs among the top class of such franchises in profitability.

Index comparison with each convenience store

Company name	Code	PER	ROE	Dividend yield
Lawson	2651	19.8	12.2%	3.87%
Circle K Sunkus	3337	20.0	5.2%	3.13%
Seven & i Holdings	3382	15.0	6.3%	2.86%
Meiko Network	4668	9.6	22.0%	3.55%
Family Mart	8028	20.4	8.3%	2.55%
Mini Stop	9946	13.6	6.3%	3.16%

as of January 13



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