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Company Research and Analysis Report

FISCO Ltd.

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■ New businesses to contribute substantially

In the first quarter of the fiscal year through August 2013, i.e., in September-November 2012 (Q1 FY8/13), Meiko Network Japan's consolidated sales rose 10.6% year-on-year (YOY) to ¥3,327mn, while its operating profit grew 35.2% YOY to ¥744mn. Both figures were record highs for the first quarter of a fiscal year. The sales growth was primarily attributable to the Meiko Gijuku school business and to the contribution of Youdec Co., which became a fully consolidated subsidiary at the end of July 2012. Profit growth was led by a 160.9% y-o-y jump in operating profit from Meiko Gijuku directly operated schools.

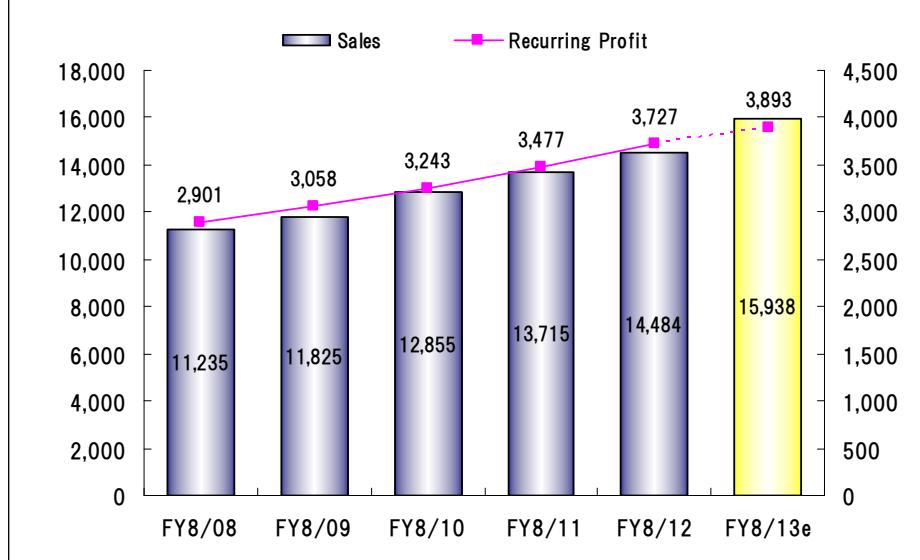
In Q2 FY8/13, the Meiko Gijuku directly operated schools have enrolled more students for winter-term instruction, so the company projects further YOY increases in sales and profits. There is a good chance that the company will slightly surpass its forecasts for H1 FY8/13 and raise its forecasts for the full fiscal year. The new businesses of Waseda Academy Kobetsu Schools and Meiko Soccer Schools are rapidly increasing the number of their students and forming a basis for greater growth in the future. We foresee steady growth from FY8/14 as new businesses supplement the growth from Meiko Gijuku schools.

For FY8/13, Meiko Network Japan plans to increase its dividend per share by ¥2, making it ¥27. Based on the company's net profit forecast, a dividend of ¥27 would equate to a dividend payout ratio of 32%. The company aims to maintain a dividend payout ratio of 35%, and given the likelihood of stronger profit growth this fiscal year than currently projected by the company, management may raise its dividend for the current fiscal year.

■ Check Points

- Q1 FY8/13 sales and profits hit record highs for a first quarter
- Earnings growth to be supplemented by an expanding market for supplementary education and possible tax reductions
- The company may well raise its dividend per share for FY8/13 more than currently planned

Sales and Recurring Profit (¥mn) in FY8/08 to FY8/12 and Company Forecasts for FY8/13e

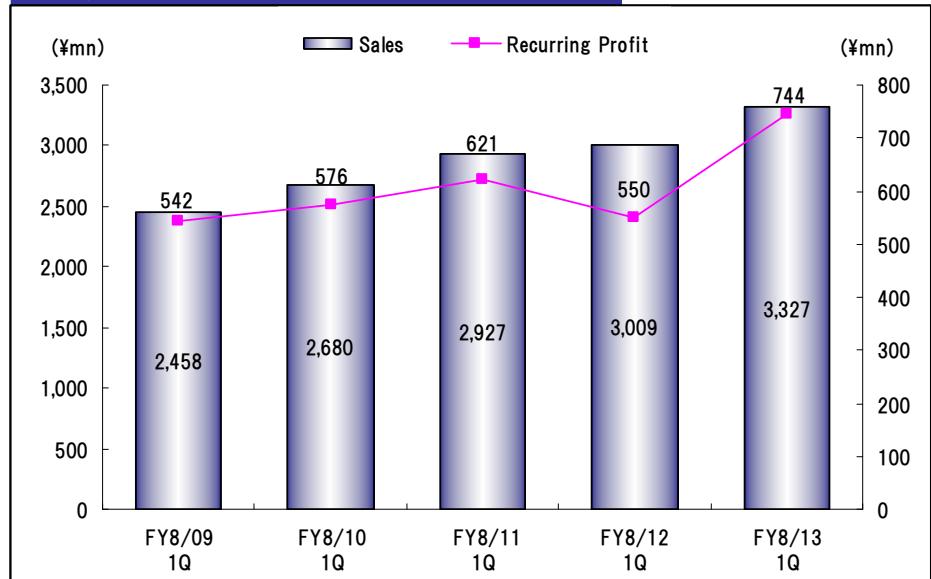


■ Results in Q1 FY8/13

Record-high Q1 sales and profits

As the company announced on January 10, 2013, in Q1 FY8/13, its sales grew by 10.6% YOY to ¥3,327mn, its operating profit increased by 35.2% YOY to ¥774mn, its recurring profit advanced by 30.8% YOY to ¥763mn, and its net profit rose by 36.9% YOY to ¥456mn. Thus, sales and profits reached record highs for a first quarter.

Consolidated Sales (¥mn), Q1 FY8/09 - Q1 FY8/13

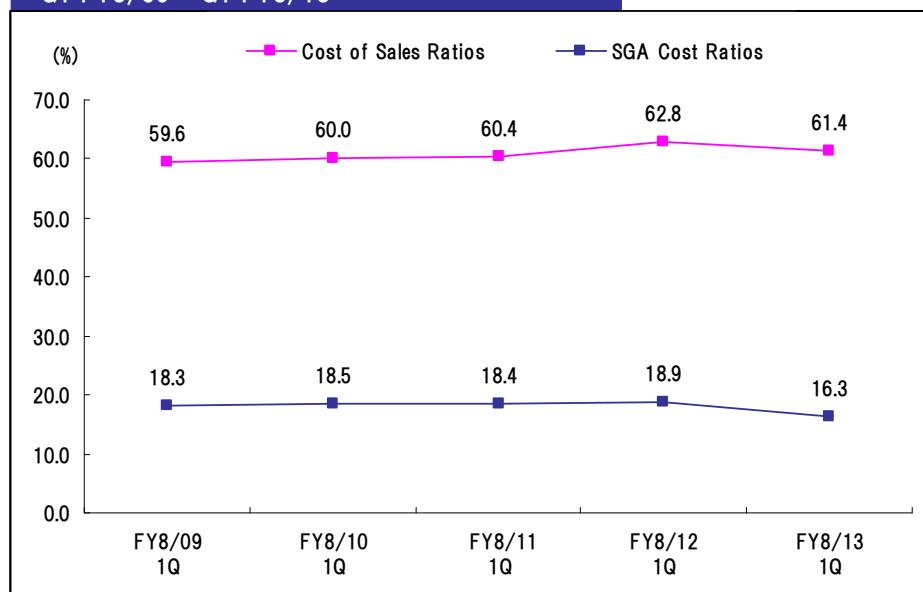


Performance (¥mn) by Business, Q1 FY8/09 - Q1 FY8/13

■ Results in Q1 FY8/13

	FY8/09 1Q	FY8/10 1Q	FY8/11 1Q	FY8/12 1Q	FY8/13 1Q	YOY
Sales						
Meiko Gijuku schools (directly)	1,203	1,206	1,340	1,372	1,393	1.5%
Meiko Gijuku schools (franchised)	1,236	1,318	1,422	1,464	1,560	6.6%
Supplemental education	-	135	142	123	126	2.7%
Other businesses	18	19	22	48	246	404.6%
Total sales	2,458	2,680	2,927	3,009	3,327	10.6%
Operating profit						
Meiko Gijuku schools (directly)	-	108	165	74	195	160.9%
Meiko Gijuku schools (franchised)	-	770	776	836	865	3.5%
Supplemental education	-	-15	5	-5	-8	-
Other businesses	-	1	-17	-30	-31	-
Company-wide operating costs	-	-289	-309	-325	-277	-
Total operating profit	-	576	621	550	744	35.2%
Operating profit margin (%)						
Meiko Gijuku schools (directly)	-	9.0%	12.3%	5.5%	14.0%	-
Meiko Gijuku schools (franchised)	-	58.5%	54.6%	57.1%	55.5%	-
Supplemental education	-	-	3.8%	-	-	-
Other businesses	-	9.7%	-	-	-	-
Total operating profit margin	-	21.5%	21.2%	18.3%	22.4%	-

Sales grew because business at Meiko Gijuku directly operated schools and Meiko Gijuku franchised schools expanded and because consolidated subsidiary Youdec Co. contributed about ¥180mn of sales. Youdec Co. publishes magazines about the content of entrance examinations for junior high schools and high schools and sells education materials. It was made a fully consolidated subsidiary at the end of July 2012. Most of the profit growth came from Meiko Gijuku directly operated schools. In Q1 FY8/12, these schools spent heavily on relocation and renovation. In Q1 FY8/13, they spent much less on relocation and renovation, so their profits increased. Furthermore, these schools enrolled more students per school in Q1 FY8/13 than they did in Q1 FY8/12, contributing to greater profitability. Youdec Co. just broke even, so it did not contribute much to profits.

Cost of Sales Ratios and SGA Cost Ratios (%)
Q1 FY8/09 - Q1 FY8/13

■ Business Trends by Devision

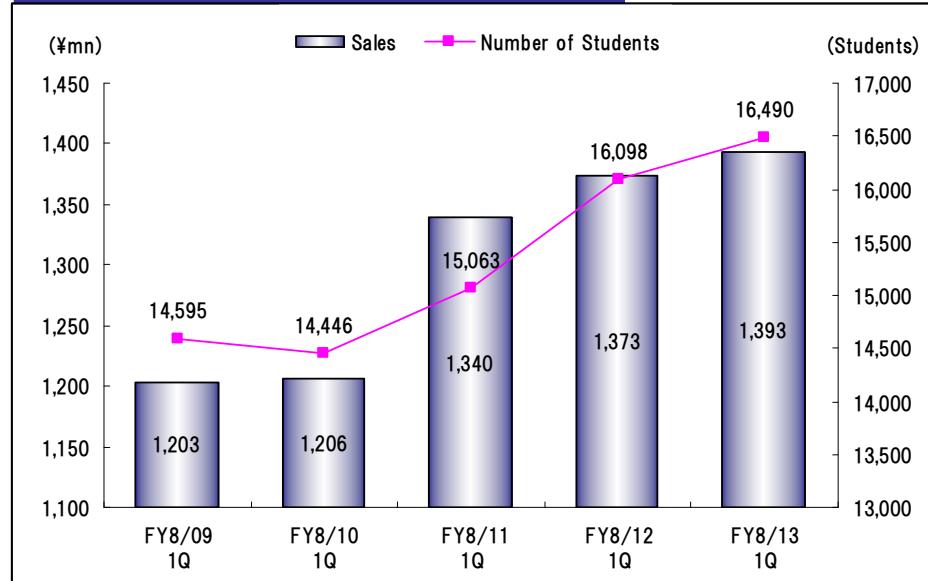
Increase in number of students supported sales growth

(1) Meiko Gijuku directly operated schools

In Q1 FY8/13, sales from Meiko Gijuku directly operated schools increased by 1.5% YOY to ¥1,393mn and operating profit rose by 160.9% to ¥195mn. The number of directly operated Meiko Gijuku schools declined by 13 YOY to 205, but 9 of these 13 were converted to franchised Meiko Gijuku schools. Despite the drop in the number of Meiko Gijuku directly operated schools, the number of students enrolled in these schools increased by 2.4% YOY to 16,490, reflecting the effect of renovating schools a year earlier and the effect of improving instruction through such measures as holding teachers' meetings and teachers' trainings at each area of instruction. This increase in the number of students contributed to sales growth.

As mentioned above, the Meiko Gijuku directly operated school business spent much less in Q1 FY8/13 on relocating and renovating schools than it did in Q1 FY8/12, which directly improved profits. Furthermore, the average number of students per Meiko Gijuku directly operated school increased by about 9% YOY, from 73.8 in Q1 FY8/12 to 80.4 in Q1 FY8/13. This rise improved profitability. Profitability also improved because some directly operated schools were converted to franchised schools.

Sales (¥mn) from and Number of Students at
Meiko Gijuku Directly Operated Schools, Q1
FY8/09 to Q1 FY8/13



■ Business Trends by Division

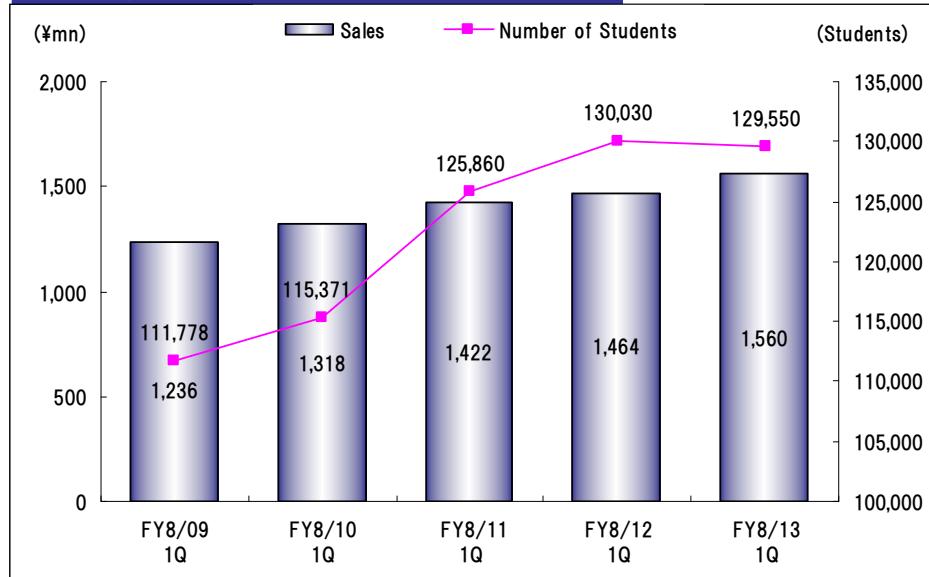
Number of schools increased but the average number of students per school declined slightly

(2) Meiko Gijuku franchised schools

In Q1 FY8/13, sales from Meiko Gijuku franchised schools grew by 6.6% YOY to ¥1,560mn and operating profit from these schools rose by 3.5% to ¥865mn. The number of Meiko Gijuku franchised schools increased by 3.7% YOY to 1,875, while the average number of students per school slightly decreased from 71.9 in Q1 FY8/12 to 69.0 in Q1 FY8/13, so the total number of students at these schools declined by 0.4% YOY to 129,550. Despite this slight decline in the total number of students, sales increased, largely because of greater sales of education materials. The operating profit ratio at Meiko Gijuku franchised schools declined YOY, indicating that System-wide sales at these schools was approximately unchanged YOY.

The average number of students at Meiko Gijuku franchised schools slightly declined for two reasons: 1) the proportion of new franchised schools set up in regional cities, where there are fewer students than in large cities, has risen recently, and 2) the competition for students in large cities has intensified.

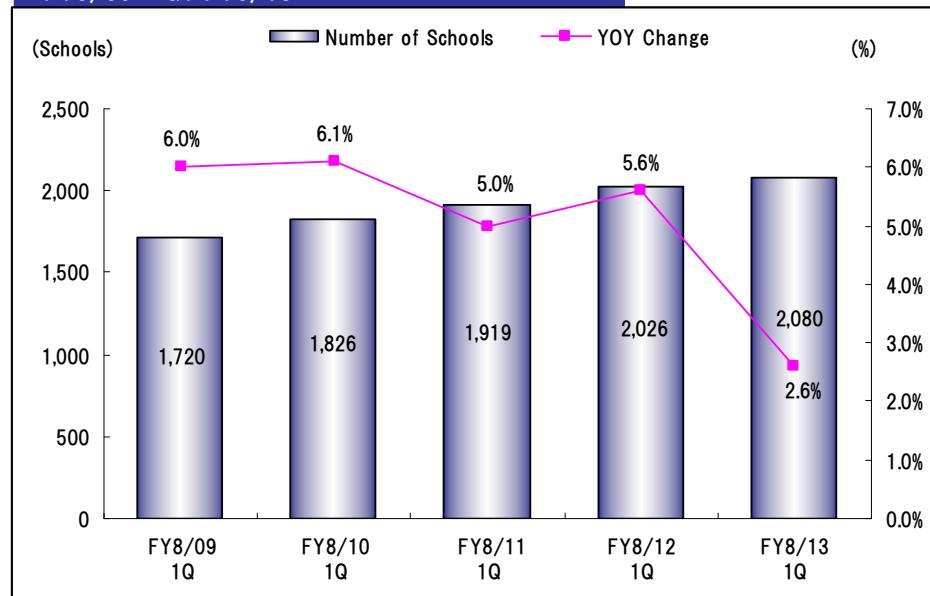
Sales (¥mn) from and Number of Students at Meiko Gijuku Franchised Schools, Q1 FY8/09 - Q1 FY8/13



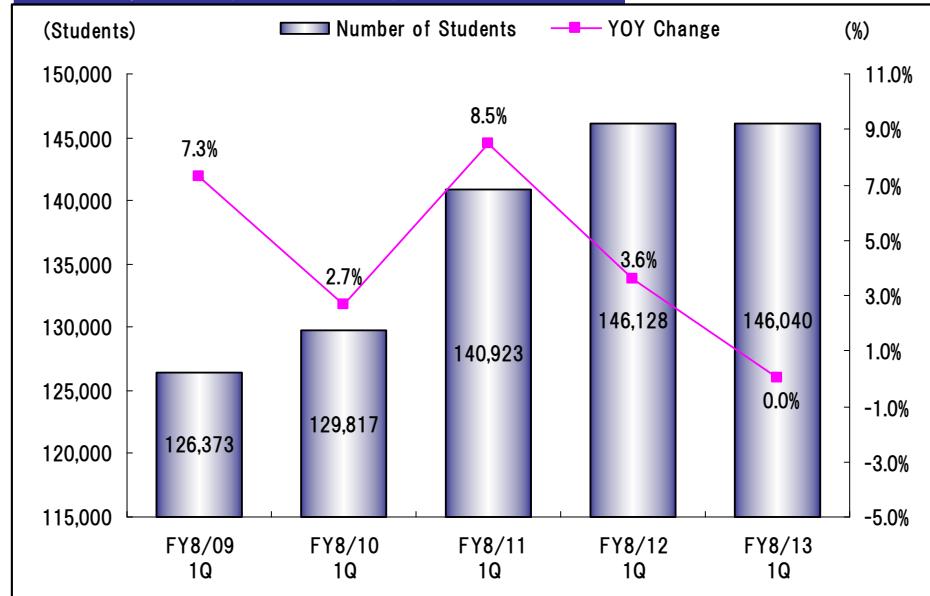
■ Business Trends by Division

The growth in the combined number of directly operated and franchised Meiko Gijuku schools and the growth in the total number of students at these schools slowed from Q4 FY8/12 to Q1 FY8/13. Management has addressed this problem with a number of actions. It has adjusted its student recruitment activity to reflect the distinctive characteristics of each school and area of operation. It has strengthened the instruction system at these schools by accumulating and sharing the best practices of each school and by conducting workshops to improve the skills of school supervisors. It has broadened the hospitality extended at these schools with the aim of improving the learning environment. Management expects these efforts to bear fruit in coming quarters.

Total Number of Meiko Gijuku Schools and YOY Change in this Number by Quarter, Q1 FY8/09 - Q1 FY8/13



Total Number of Students at Meiko Gijuku Schools and YOY Change in this Number by Quarter, Q1 FY8/09 - Q1 FY8/13



Cutting fixed costs to turn profitable

(3) Supplemental education

This division is operated by consolidated subsidiary Tokyo Ishin Gakuin (Tokyo Medical School Preparatory Institute), which prepares students for entry into medical school. In Q1 FY8/13, sales at this unit rose by 2.7% YOY to ¥126mn and the unit suffered an operating loss of ¥8mn, compared with an operating loss of ¥5mn in Q1 FY8/12. The performance of this business depends mainly on the number of new students enrolled every spring. In spring 2012, this number declined, leading to a deterioration of business. However, the subsidiary has been reducing its scale and fixed costs. For example, at the end of FY8/12, it amortized all remaining goodwill and other fixed costs as an asset impairment loss. Now, it is strengthening its student recruitment efforts.

Franchises of new businesses expected to contribute to profits eventually

(4) Other businesses

In its other business division, Meiko Network Japan operates several new businesses and consolidated subsidiary Youdec Co., described previously. In Q1 FY8/13, these other businesses recorded sales of ¥246mn, which was about five times their sales in Q1 FY8/12. However, they suffered an operating loss of ¥31mn, compared with an operating loss of ¥30mn in Q1 FY8/12.

Youdec Co. made an initial contribution to Q1 sales of ¥180mn. Excluding this contribution, sales from other businesses rose by about 40% YOY, demonstrating brisk growth by new businesses. As the new businesses are still in their early stages of investment, they remain unprofitable, but if the company applies its expertise in franchising to develop franchises of its new businesses, they will probably contribute significantly to profits in the future.

In Q1 FY8/13, the Meiko Soccer School business generated sales of ¥26mn, up from ¥22mn in Q1 FY8/12. The business suffered an operating loss of ¥800,000. During Q1 FY8/13, this business opened two new directly operated schools, bringing the total to eight. It also has one franchised school. In Q1 FY8/13, this business enrolled 763 students, 55 more than in Q4 FY8/12.

■ Business Trends by Division

The new Waseda Academy Kobetsu School business is operated jointly by Meiko Network Japan and Waseda Academy. During Q1 FY8/13, each school opened two new directly operated schools, bringing the total number of directly operated schools to two. They also opened one new franchised school, bringing the total number of franchised schools to eight. The directly operated schools enrolled 215 students in Q1 FY8/13, 18 more than in Q1 FY8/12. Hereafter, this business intends to open more franchised schools.

Abrakadoodle Art Studios offer emotional enrichment programs for children from preschool to elementary school ages. This business is building a foundation for expansion. While raising the level of the services it offers, it aims to set up a basic operation to follow students from recruitment through enrollment. In April 2012, this business opened a multipurpose facility, Mirai Kids Club(Future Kids Club), in a shopping center in Tsuzuki Ward, Yokohama City. This club offers English language conversation classes, as well as art classes. By broadening the range of its services, this facility aims to attract more students.

■ Company Forecasts for FY8/13

Market growth and tax-reduction measures to support profit growth

For H1 FY8/13 and FY8/13, the company maintained its original forecasts, shown in the table below. The company's implied forecasts for Q2 FY8/13 are sales growth of 9.4% YOY and an operating profit decline of 10.6% YOY.

In Q1 FY8/13, sales were in line with the company's original forecast, but operating profit was slightly above its original forecast. So far in Q2 FY8/13, there have been no major changes in the Japanese market for supplementary education, nor any reasons for large increases in company costs. Thus, it appears that operating profit in H1 FY8/13 could exceed the company's forecast by ¥150-200mn. Full-term profits will depend primarily on the success of each business in attracting new students, but they will probably surpass the company's forecasts slightly.

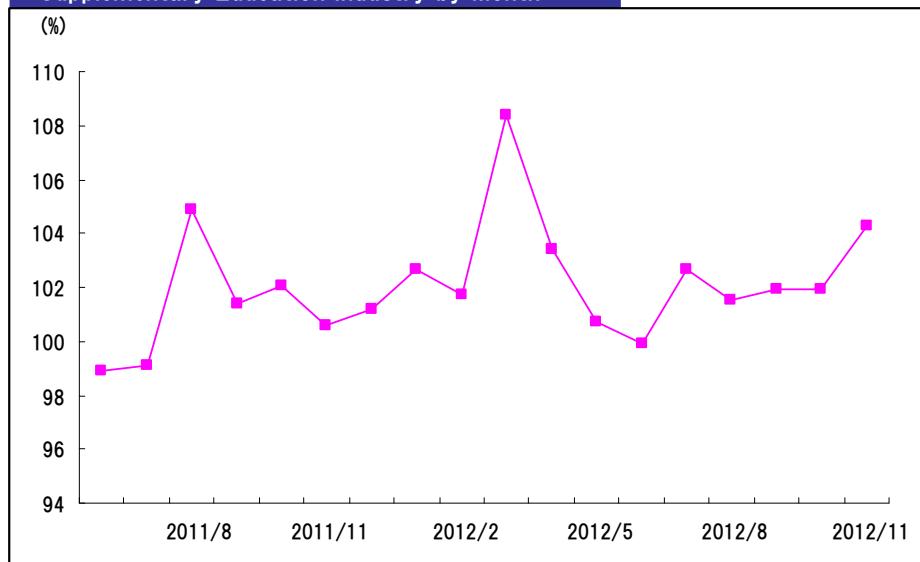
Company Forecasts (¥mn) for H1 FY8/13 and FY8/13

	Sales	YOY	Operating Profit	YOY	Recurring Profit	YOY	Net Profit	YOY	EPS (¥)	DPS (¥)
H1 FY8/13	7,898	9.9	1,967	2.5	2,004	0.1	1,191	6.1	43.17	13.0
FY8/13	15,938	10.0	3,846	8.6	3,893	4.5	2,323	18.0	84.23	27.0

■ Company Forecasts for
FY8/13

According to the Survey of Designated Service Industries by the Ministry of Economy, Trade and Industry, the number of students in Japan's supplementary education industry continues to grow by single digits YOY. In addition, Japan's Liberal Democratic Party recently gained control of the lower house of the Diet, the House of Representatives, giving it executive control of the government. To stimulate economic growth, the LDP proposes several measures. One such measure is to allow elderly citizens to deduct from taxable income their contributions to the education of their grandchildren, up to a certain amount. If this proposal becomes law, it should stimulate further growth of the market for supplementary education.

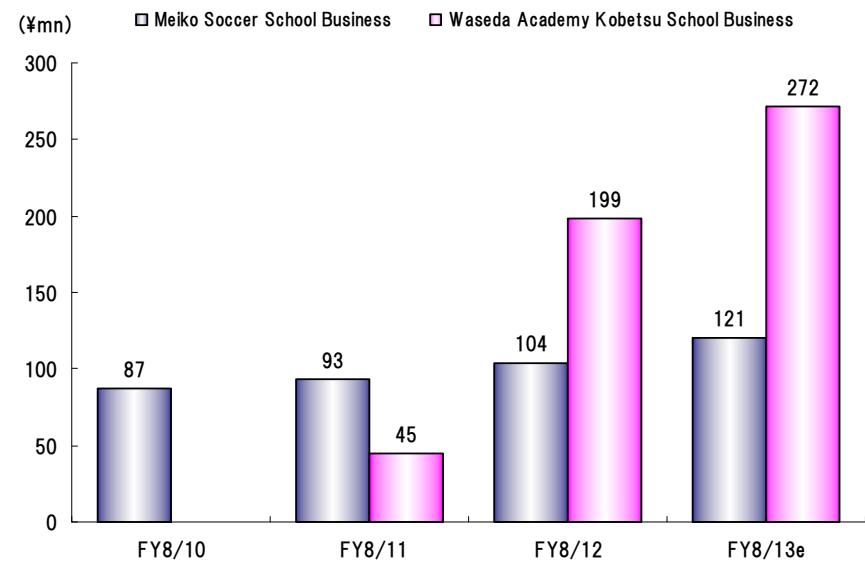
YOY Rate of Change in Japan's Supplementary Education Industry by Month



For FY8/13, the company projects YOY sales and operating profit growth of about 5% from its Meiko Gijuku school businesses (directly operated and franchised combined), reflecting an increase in the number of franchised schools and students from Q2. The company expects its supplemental education business to return to profitability in FY8/13, reflecting more aggressive recruitment of students in spring 2013 and throughout the year. The company forecasts a 244% YOY jump in sales from other businesses, mainly due to a roughly ¥700mn contribution by Youdec Co. The company projects a continued small operating loss for these businesses, reflecting early investment costs. However, as described previously, both the Meiko Soccer School business and the Waseda Academy Kobetsu School business are rapidly increasing their sales, and both should contribute to profits soon. At the end of 8/12, there were two directly operated and eight franchised Waseda Academy Kobetsu Schools. By the end of FY8/13, the company plans to have in operation 19 franchised Waseda Academy Kobetsu Schools, and five years from now, it aims for 100 franchised schools.

■ Company Forecasts for
FY8/13

YOY Rate of Change in Japan's
Supplementary Education Industry by Month



Performance (¥mn) by Business, FY8/10 - FY8/13e

Sales	FY8/10	FY8/11	FY8/12	FY8/13e	YOY
Meiko Gijuku schools (directly)	6,287	6,574	6,864	14,244	4.7%
Meiko Gijuku schools (franchised)	5,846	6,402	6,736		
Supplemental education	633	594	559	578	3.3%
Other businesses	87	143	324	1,115	244.1%
Total sales	12,855	13,715	14,484	15,938	10.0%
Operating profit					
Meiko Gijuku schools (directly)	1,128	1,315	1,443	4,996	5.0%
Meiko Gijuku schools (franchised)	3,055	3,256	3,313		
Supplemental education	40	7	-7	5	-
Other businesses	7	-174	-120	-50	-
Company-wide operating costs	-1,123	-1,041	-1,086	-1,100	-
Total operating profit	3,108	3,363	3,543	3,846	8.6%
Operating profit margin (%)					
Meiko Gijuku schools (directly)	17.9%	20.0%	21.0%	35.0%	-
Meiko Gijuku schools (franchised)	52.3%	50.9%	49.2%		-
Supplemental education	6.5%	1.3%	-	0.8%	-
Other businesses	8.0%	-	-	-	-
Total operating profit margin	24.2%	24.5%	24.5%	24.1%	-

■ Strategy for the medium-to-long term

Aiming to expand its top sales ranking in the industry

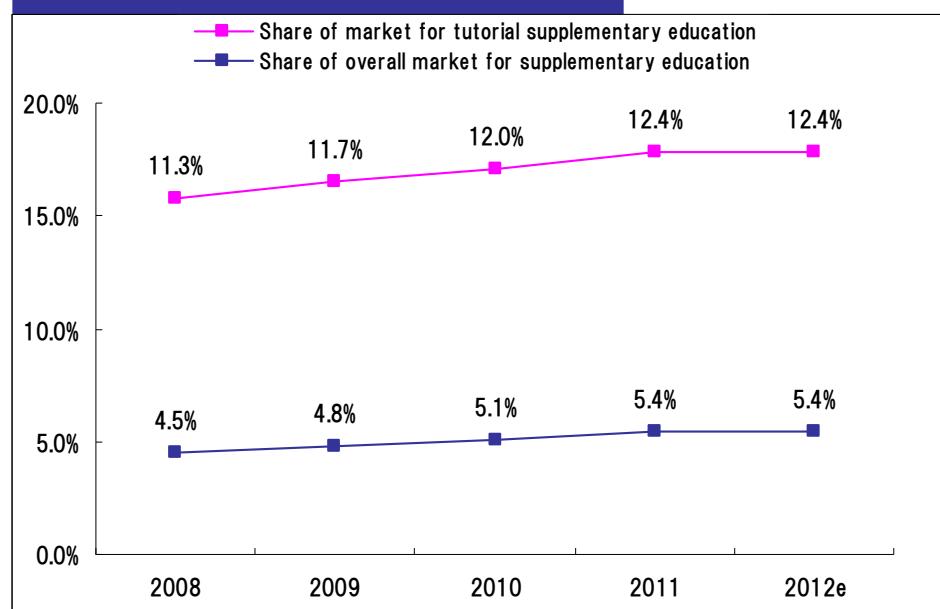
As detailed in the table below, Meiko Network Japan holds the top share of Japan's market for supplementary education in terms of sales. As shown in the graph below, the company has steadily increased its market share in recent years. Yet, with just 5.4% of the market, the company can clearly expand its share further. Over the medium-to-long term, the company plans to apply its knowledge of franchising to increase the numbers of its schools, students and classes. As part of its class menu, the company is considering distributing attractive video content.

Ranking of Listed Japanese Providers of Supplementary Education

Company	Sales (¥mn)
Meiko Network Japan (Meiko Gijuku schools System-wide sales)	49,287
Eikoh (Eikoh Seminar, Navio, Vis-a-vis)	34,067
Nagase Brothers (Toshin High School, Toshin Satellite Preparatory School, etc.)	27,493
Gakken Holdings (Gakken Classrooms, Saishin, Asunaro Gakuin, etc.)	20,725
Riso Kyoiku (Tomas Schools)	20,146
Sanaru (Sanaru Cramming Schools, Sanaru Individual Partner, Keimeisha)	18,751
Ichishin Holdings (Ichishin Gakuin, Ichishin Preparatory School, Kotaro Juku)	17,964
Waseda Academy	17,225
Wao Corporation (Ability Development Center, Individual Instruction Axis)	16,673

Note: Sales are for fiscal years ending between September 2011 and August 2012, except for Sanaru, for which the fiscal year ended in June 2011

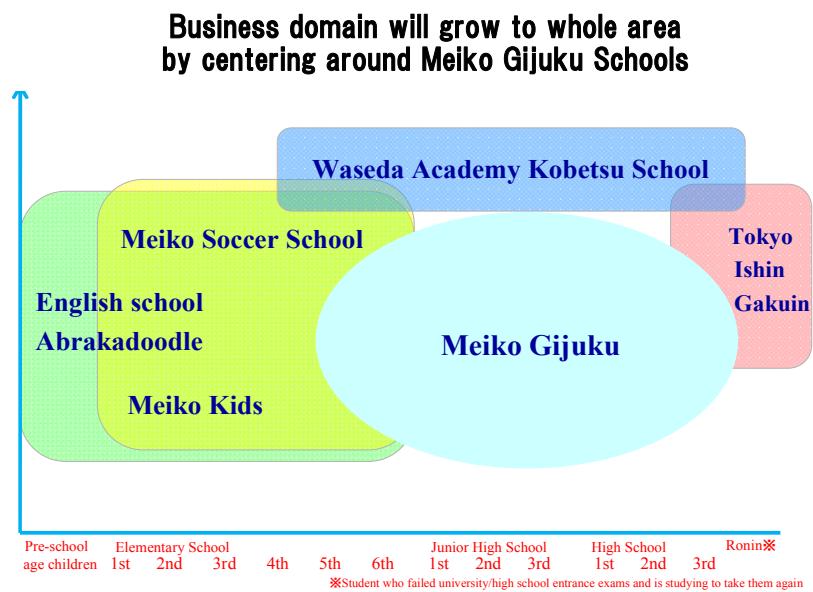
Meiko Gijuku Market Shares, FY08 to FY12e



Source: Yano Research Institute, *Educational Industry White Paper 2012*

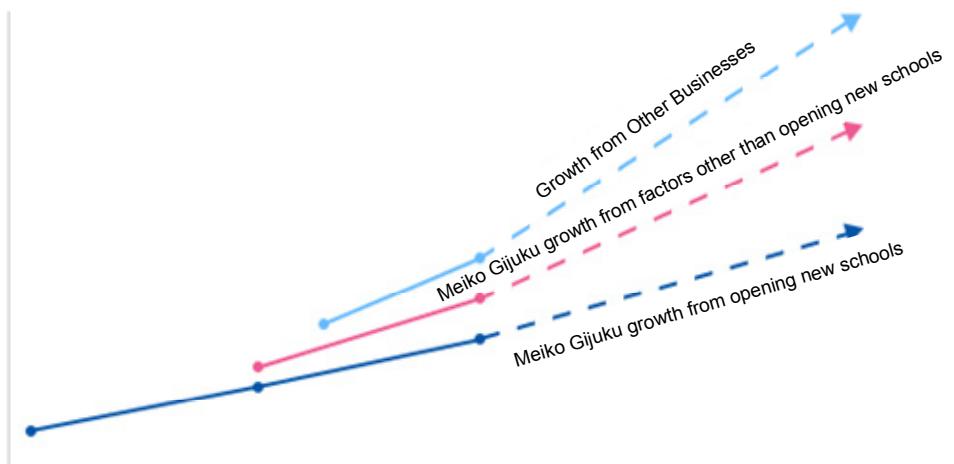
■ Strategy for the medium-to-long term

Over the medium-to-long term, the company plans to continue to develop businesses based on its basic principles of nurturing human resources by contributing to educational and cultural programs and achieving goals by developing and diffusing franchising knowhow. While expanding its core Meiko Gijuku school business, the company will develop its new businesses, thereby increasing the age range of its students and achieving sales and profit growth toward 2020.



Source: Company

Growth Path Image



Source: Company

■ Shareholder Return Policy

The company offers attractive shareholder returns

Because of its concern for shareholder returns, Meiko Network Japan remains popular among equity investors. For FY8/13, the company plans to raise its dividend payment per share by ¥2 to ¥27. Based on the company's current forecast of net profit, this dividend payment would result in a dividend payout ratio of only 32%, lower than the company's target, of 35%. Thus, if company profits grow throughout FY8/13 at the pace they increased in Q1, there is a good chance that the company will increase its dividend per share by more than ¥2.

The company also plans to continue a shareholder award program begun in FY8/12 through which each shareholder of a minimum lot receives a ¥3,000 QUO card. Based on the company's closing share price on February 6, 2013, of ¥1,068, the proposed dividend per share payment of ¥27 and the shareholder award, the total yield to holders of a minimum unit of shares (100 shares) exceeded 5%. Among listed Japanese cram schools, this total yield was surpassed only by the total yields offered by Ichishin Holdings and Tokyo Kobetsu Shido Gakuin, but these companies impose restrictions on the use of their awards, making them of little value to general shareholders. In practical terms, therefore, Meiko Network Japan is among the top cram schools or companies in other industries growing through franchising, measured by total yield to shareholders.

Prospective PERs and Shareholder Yields of Leading Japanese Cram Schools and of Other Listed Companies Growing through Franchising

	Company	Share price (6th FEB)	Projected EPS	Planned DPS	Prospective PER	Dividends yield	Total yield	Shareholder award program
4668	Meiko Network Japan	1,068	84.2	27.0	12.6	2.5%	5.3%	¥3,000 QUO cards for holders of 100 shares or more
4714	Riso Kyoiku	7,620	478.7	260.0	15.9	3.4%	-	
4645	Ichishin Holdings	316	34.9	10.0	9.0	3.2%	9.5%	¥10,000 discount coupons for holders of 500 shares or more
4745	Tokyo Kobetsu Shido Gakuin	236	6.2	6.0	38.0	2.5%	4.3%	¥1,000 tuition discount coupons
6053	Eiko Holdings	707	67.7	24.0	10.4	3.4%	-	
2651	Lawson	6,940	334.3	190.0	20.7	2.7%	-	
2702	McDonald's Japan	2,382	120.3	30.0	19.7	1.3%	2.5%	¥3,000 food purchase coupons
7611	Hiday Hidakaya	2,093	141.6	32.0	14.7	1.5%	2.5%	¥2,000 coupons for cash or rice
2674	Hardoff Corporation	646	66.7	25.0	9.6	3.9%	-	

Note: The shareholder awards are for holders of minimum share units for all companies except Ichishin Holdings

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