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■ Top Japanese maker of granulation and coating equipment, with a 70% share of Japanese market

Freund Corp. produces machinery for the formulation of medicines and foods. It claims a 70% share of the Japanese market for granulation equipment and coating equipment. In the fiscal year through February 2013, i.e., in FY2/13, the company increased its consolidated sales by 7.6% year-on-year (y-o-y), to ¥16,396mn, its consolidated operating profit by 38.0% to ¥1,470mn, its consolidated recurring profit by 44.1% to ¥1,618mn, and its consolidated net profit by 25.7% to ¥765mn.

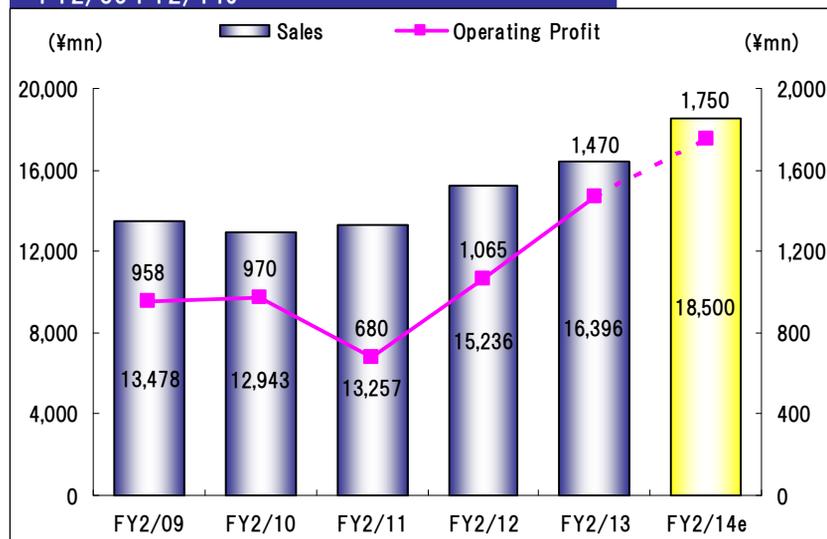
For FY2/14, the company projects a 12.8% y-o-y rise in consolidated sales to ¥18,500mn, a 19.0% increase in consolidated operating profit to ¥1,750mn, an 8.8% upturn in consolidated recurring profit to ¥1,760mn, and a 24.1% advance in consolidated net profit to ¥950mn. FY2/14 is the final year of the company's fifth medium-term plan, called Vision-50. This plan targets consolidated sales of ¥20bn and consolidated operating profit of ¥2bn for FY2/14. Given the current favorable operating environment for the company, its brisk order intake, and the weakening of the yen against other currencies, it seems likely that these targets will be achieved.

Freund Corp. has a healthy balance sheet, with an equity ratio of 61.4%, and management is positive about improving shareholder returns, aiming for a dividend payout ratio of 20% on a consolidated basis. If profits in FY2/14 exceed the company's current forecasts, the company may increase its dividend per share.

■ Check Points

- Growing as an R&D-based company
- Granulation and coating are indispensable processes for pharmaceutical production
- Company forecasts record-high profits for FY3/14, due in part to growth overseas

Consolidated Sales and Operating Profit (¥mn), FY2/09-FY2/14e



■ Company Outline

Growing as an R&D-based company

(1) History

The company name derives from the German word for friend, freund. The company's current chairman and chief executive officer, Mr. Yasutoyo Fusejima, was one of the company's founders, and the other founders were his friends. Therefore, they chose the name Freund Corp.

Freund Corp. was established in 1964, when it developed film-coating liquid and equipment. The company subsequently developed many kinds of mechanical devices and pharmaceutical additives. It bases its growth on research and development to produce goods that satisfy market demand.

Company History

1964	Founded with the development of film-coating liquid and automatic film-coating equipment.
1972	Moved the head office to Totsuka (now Takadanobaba), Shinjuku Ward, Tokyo.
1979	Licensed high-coater technology from Vector Corp., of the US.
1987	Licensed anti-mold food preservative technology from Seppic Co., of France.
1991	Developed the Spherex equipment for the production of seamless minicapsules.
1993	Licensed roller-compacter technology from Vector Corp., of the US, and dilactose technology from FrieslandCampina DMV, of the Netherlands.
1996	Registered shares on Japan's over-the-counter stock market.
1997	Acquired Vector Corp., of the US.
2004	In the company's 40th year, the head office moved to West Shinjuku, Tokyo. Shares listed on the JASDAQ exchange.
2009	Developed the Flow-coater Universal machine for coating liquid granule layers , and the Container-washing machine for washing containers used to convey granular substances.
2010	Established subsidiary Freund Pharmatec Ltd. in Ireland, acquired Turbo Kogyo Co., of Japan, and renamed it Freund-Turbo Corp., moved the head office to Okubo, Shinjuku Ward, Tokyo.
2012	Renamed Vector Corp., of the US, as Freund-Vector Corp.

Machinery division provides 60% of sales, making mainly machinery for formulating pharmaceuticals

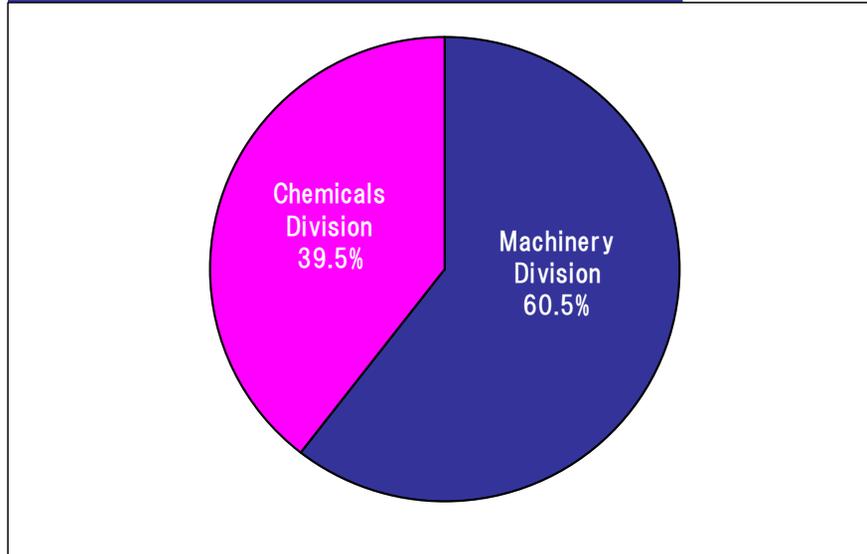
(2) Businesses

Freund Corp. has two main divisions, machinery and chemicals. The machinery division manufactures primarily machinery for formulating pharmaceuticals, while the chemicals division concentrates on making excipients for pharmaceuticals and preservatives for foods. Of the ¥16,396mn in sales generated by Freund Corp. in FY2/13, 60.5% came from the machinery division and 39.5% from the chemicals division. The machinery division supplied 67.5% of the company's operating profit, and the chemicals division provided 32.5%. Overseas sales accounted for 21.9% of total sales.

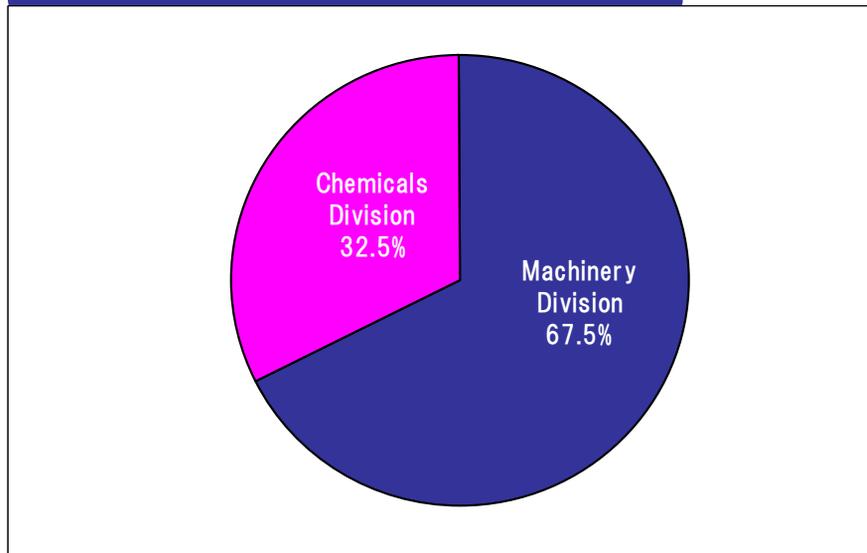


■ Company Outline

Breakdown of Consolidated Sales in FY2/13 by Division



Breakdown of Consolidated Operating Profit in FY2/13 by Division



Makes granulation and coating equipment

(a) Machinery Division

The machinery division produces and sells granulation and coating equipment for pharmaceuticals, foods and fine chemicals. A basic explanation of the structure of pharmaceuticals and their production process may facilitate an understanding of the company's equipment.

Granulation and coating are indispensable processes for pharmaceutical production

In general, active ingredients account for only a small portion of pharmaceuticals; most of a drug is harmless excipients, such as starch, corn starch, and sugar. The raw materials for active ingredients and excipients are pulverized, aggregated and liquefied, but to be formulated into granules or tablets, they must be formed into uniform size and shape. Freund Corp.'s granulation equipment performs this function. Medicine in granule or tablet form is then coated several times to block its unpleasant smell or taste, to protect it from light, acid and/or water, and to ensure that it is absorbed in the intestines, where it can be most effective. Freund Corp.'s coating equipment performs this function.

Freund Corp. also manufactures a machine that produces seamless mini-capsules. The active ingredient of a medicine is injected into the center of these mini-capsules in liquid form. Currently, not many medicines are dispensed in seamless mini-capsules, so the company sells only a few of these machines each year. However, Freund Corp. holds a global monopoly on this type of machine, which generates high competitive market, so it should benefit from the gradual adoption of this method of drug delivery.

70% share of the Japanese market for coating equipment and granulation equipment, with growing business overseas

Freund Corp. claims a 70% share of the Japanese market for coating equipment and granulation equipment. It is the only company in the world that produces both chemicals and equipment using formulation technology. Recently, the company has expedited the growth of its business in Asian countries other than Japan, while its US subsidiary has done the same in the US, Europe and the Middle East. In Japan, Freund Corp. has only one competitor, Powrex Corporation (unlisted), which licenses technology from Glatt GmbH, based in Germany. The GEA Group, based in Denmark, is also a global competitor, this group is a conglomerate that produces for medical manufacture and food products. Glatt GmbH is the other company in the world that specializes in the same fields as Freund Corp.

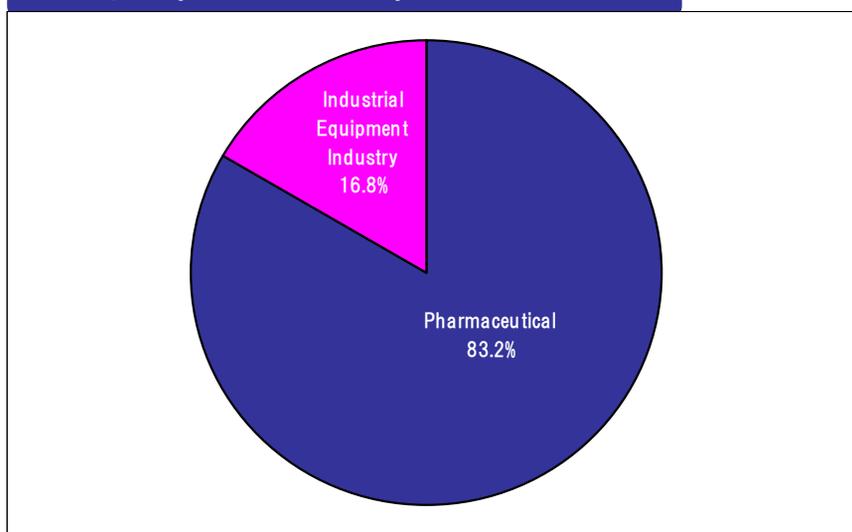
Machinery is custom-made and sold directly

All of Freund Corp.’ s products are custom made, so all sales in Japan are direct sales. These products range in price from ¥50mn to ¥100mn, and most products are sold with attachments costing 20-30% of the product price. The period between receiving an order and delivering a product is usually six months to one year. The main customers for Freund Corp.’ s machinery are pharmaceutical companies, and Freund Corp. supplies machinery to all of Japan ’ s leading pharmaceutical companies. It also supplies machinery to makers of new drugs, generic drugs, and over-the-counter drugs and to contract manufacturers.

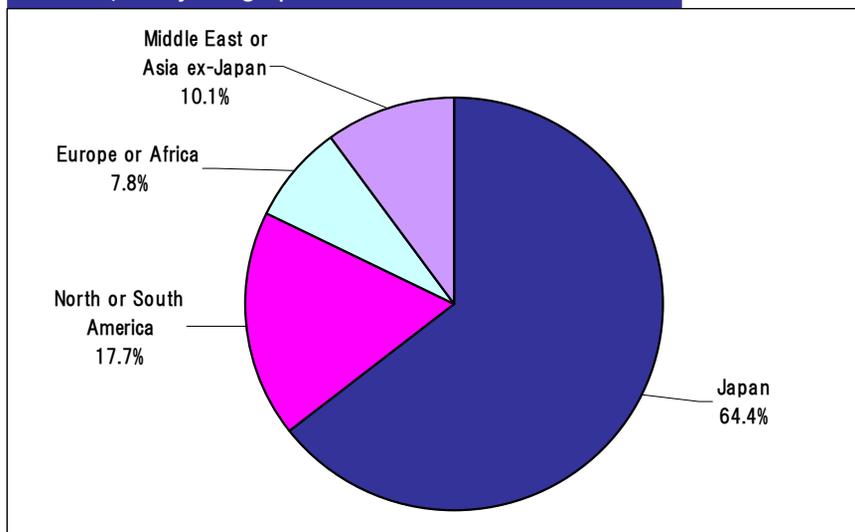
In recent years, Freund Corp. has fused pulverizing and micro-nano classifying technologies with its granulation and coating technologies to manufacture products for makers of general industrial products. In FY2/13, 83.2% of the sales generated by the machinery division were made to pharmaceutical companies and 16.8% were to makers of general industrial products.

In FY2/13, 64.4% of the sales generated by the machinery division were made in Japan, 17.7% were made in north or south America, 7.8% were made in Europe or Africa, and 10.1% were made in the Middle East or Asia ex-Japan. The parent company sells machinery mainly to pharmaceutical companies in Japan and other parts of East Asia, its US subsidiary Freund-Vector Corp. sells machinery to pharmaceutical companies in the Americas, Europe, and the Middle East, and Japanese subsidiary Freund-Turbo Corp. sells to makers of industrial products.

Breakdown of Consolidated Machinery Division Sales in FY2/13 by Customer Industry



Breakdown of Consolidated Machinery Division Sales in FY2/13 by Geographical Market



Produces primarily additives for pharmaceuticals

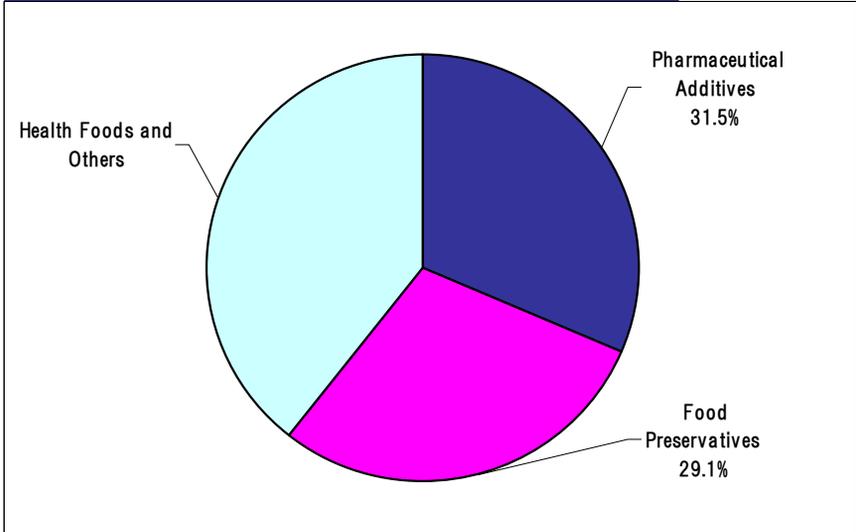
(b) Chemicals Division

The chemicals division produces primarily additives for pharmaceuticals, food preservatives, and enriched foods. It also manufactures food supplements on an original equipment manufacturer (OEM) basis. The OEM manufacture of food supplements accounts for about one-third of total sales by the chemicals division, and Freund Corp. has received many inquiries for further OEM manufacture, so these sales are likely to grow. The division applies good manufacturing practice* in the manufacture of pharmaceutical excipients, and its food preservatives sustain the quality of different kinds of foods, contributing to food safety.

The chemicals division sells mainly to pharmaceutical companies, health food (supplements) makers, and makers of general foods. A large portion of its OEM production of supplements is for a leading Japanese manufacturer of health care products. This manufacturer bought ¥2,248mn of machinery and chemical products from Freund Corp. in FY2/13, which was 13.7% of Freund Corp.'s total sales.

*Note: good manufacturing practice is a set of standards set by Japan's Ministry of Health, Labor and Welfare which must be met for machinery used in the production of pharmaceuticals and foods. All advanced countries have similar standards.

Breakdown of Consolidated Chemicals Division Sales in FY2/13 by Product Type



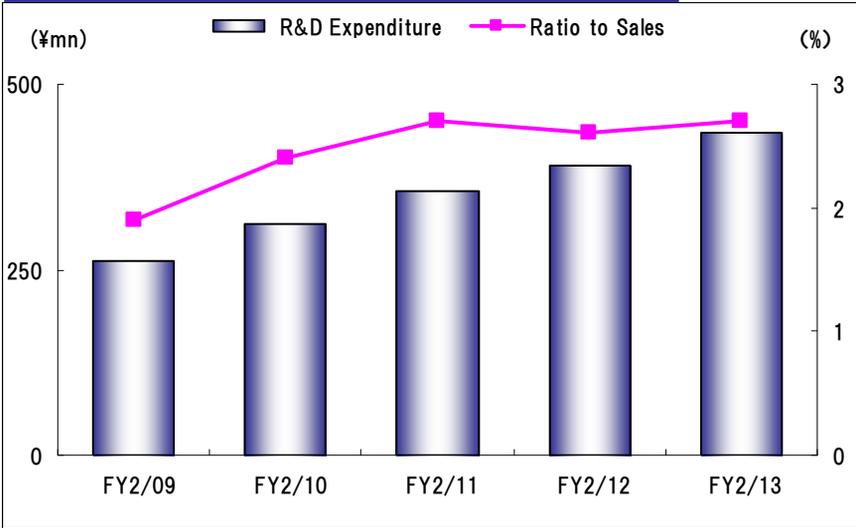
Company motto is independent technological development

(3) Distinctive Features and Strength

A distinctive feature and strength of Freund Corp. is its fusing of technology for product formulation, machinery production, and chemical production. It is the only company in the world that joins these three technologies, and through this combination, it develops many new products and earns the trust of customers.

The company’s motto is independent technological development, and its R&D center is staffed by experts in many fields, including mechanical engineering, pharmacology, electronic engineering, applied chemistry, and biochemistry. Thus, the company can offer system solutions for all of its machinery and chemicals and test their applications for many users. Freund Corp.’s R&D expenditure has grown from ¥261mn (1.9% of sales) in FY2/09 to ¥435mn (2.7% of sales) in FY2/13.

R&D Expenditure (¥mn) and Ratio to Sales, FY2/09-FY2/13



Increases in pharmaceutical production and new drug development affect company positively

(4) Impact of Pharmaceutical Production on Freund Corp.' s Sales

Because Freund Corp.' s machinery division sells most of its products to pharmaceutical companies, its sales are positively affected by an increase in the overall output of pharmaceuticals, since pharmaceutical companies eventually have to expand their production capacity to increase their output.

In general, pharmaceutical companies do not use the same machinery to produce drugs with different active ingredients. To manufacture new drugs, these companies usually purchase new equipment. Consequently, an increase in the production of new drugs also positively affects sales by Freund Corp.' s machinery division. Similarly, an increase in the production of generic drugs supports sales by this division.

Yen depreciation lifts profits modestly

(5) Impact of Exchange Rate Fluctuations on Freund Corp.' s Sales

Freund Corp.' s exports from Japan are denominated in yen, so they are affected little by changes in yen exchange rates. However, its consolidated US subsidiary, Freund-Vector Corp., records its sales and profits in US dollars, so depreciation of the yen against the US dollar increases the yen sales and profits from this subsidiary and Freund Corp.' s consolidated sales and profits.

■ Business Trends

Double-digit profit growth

FY2/13 Results

In FY2/13, the company increased its consolidated sales by 7.6% y-o-y, to ¥16,396mn, its consolidated operating profit by 38.0% to ¥1,470mn, and its consolidated recurring profit by 44.1% to ¥1,618mn. Because Freund-Vector Corp. declared ¥301mn of legal fees as an extraordinary loss, Freund Corp.' s consolidated net profit rose by only 25.7% to ¥765mn. When the company announced its results for the third quarter of FY2/13, it raised its sales forecast for the full fiscal year to ¥16.6bn. Sales did not reach this target, mainly because the company changed its sales agent in India, sacrificing some sales in that country. However, the company expects its sales in India to be higher in FY2/14 as a result of its change.

■ Business Trends

Consolidated Results (¥mn), FY2/12-FY2/13

	FY2/12		FY2/13		YOY
	Amount	Ratio	Amount	Ratio	
Sales	15,236	100.0	16,396	100.0	7.6
Cost of goods sold	10,624	69.7	11,313	69.0	6.5
Gross profit	4,612	30.3	5,083	31.0	10.2
SGA cost	3,546	23.3	3,612	22.0	1.9
Operating Profit	1,065	7.0	1,470	9.0	38.0
Recurring Profit	1,123	7.4	1,618	9.9	44.1
Net Profit	608	4.0	765	4.7	25.7

The machinery division increased its sales by 3.4% y-o-y to ¥9,914mn and its operating profit before the allocation of corporate costs by 29.2% to ¥1,172mn, and the chemicals division raised its sales by 14.7% to ¥6,482mn and its operating profit before the allocation of corporate costs by 20.2% to ¥565mn.

Consolidated Sales and Operating Profit (¥mn) by Division, FY2/12-FY2/13

	FY2/12		FY2/13		Change	YOY
	Amount	Ratio	Amount	Ratio		
Sales	15,236	100.0	16,396	100.0	1,160	7.6
Machinery	9,582	62.9	9,914	60.5	332	3.5
Chemicals	5,653	37.1	6,482	39.5	829	14.7
Operating profit	1,065	7.0	1,470	9.0	405	38.0
Machinery	907	-	1,172	-	265	29.2
Chemicals	470	-	565	-	95	20.2
Corporate costs	▲ 312	-	▲ 267	-	-	-
Exchange rate(Yen-US dollar)	79.8	-	79.8	-	-	-

■ Results by Division

Increased sales to pharmaceutical companies

(1) Machinery Division

As detailed in the table below, the machinery division expanded its sales to pharmaceutical and food companies by 4.2% y-o-y to ¥8,248mn, but its sales to makers of industrial products fell by 0.4% to ¥1,666mn. The parent company increased its sales of machinery by 6.5% to ¥7,024mn, subsidiary Freund-Vector Corp. raised its sales of machinery by 6.1% to ¥2,983mn, and subsidiary Freund-Turbo boosted its sales by 9.9% to ¥1,022mn.



■ Results by Division

**Consolidated Machinery Division Sales (¥mn)
in FY2/12-FY2/13 by Customer Industry**

	FY2/12		FY2/13		YOY
	Amount	Ratio	Amount	Ratio	
Machinery Division Sales	9,582	100.0%	9,914	100.0%	3.4
Pharmaceutical & Food Industries	7,909	82.5%	8,248	83.2%	4.2
Industrial Equipment Industry	1,673	17.5%	1,666	16.8%	▲ 0.4

**Consolidated Machinery Division Sales (¥mn)
in FY2/12-FY2/13 by Company**

	FY2/12		FY2/13		
	Amount	YOY	Amount	Ratio	YOY
Machinery Division Sales	9,582	18.4%	9,914	100.0%	3.4
Freund Corp.	6,595	38.1%	7,024	70.8%	6.5
Freund-Vector Corp.	2,812	1.5%	2,983	30.1%	6.1
Freund-Turbo Corp.	930	-	1,022	10.3%	9.9

OEM production of supplements for a leading Japanese maker of health care products grew notably

(2) Chemicals Division

The chemicals division lifted its sales of pharmaceutical additives by 4.8% y-o-y to ¥2,041mn (see table below), but its sales of food preservatives fell by 0.2% to ¥1,889mn, while its sales of health foods jumped by 40.8% to ¥2,552mn, mainly because of a large increase in OEM production of supplements for the leading Japanese maker of health care products referred to earlier.

**Consolidated Chemicals Division Sales (¥mn)
in FY2/12-FY2/13 by Product Type**

	FY2/12		FY2/13		YOY
	Amount	Ratio	Amount	Ratio	
Chemicals Division	5,653	100.0%	6,482	100.0%	14.7
Pharmaceutical Additives	1,948	34.5%	2,041	31.5%	4.8
Food Preservatives	1,892	33.5%	1,889	29.1%	▲ 0.2
Health Foods and Others	1,812	32.1%	2,552	39.4%	40.8



Financial Condition

Company holds ample net cash, as it is debt-free

At the end of FY2/13, Freund Corp.'s cash and deposits were ¥582mn larger than they had been a year earlier, mainly because of an increase in cash from operations and a recovery of sales receivables. Inventories grew by ¥227mn in FY2/13, mainly because inventories of finished goods increased by ¥278mn to accommodate sales growth. Total equity increased in FY2/13, primarily due to the ¥765mn of net profit earned during the fiscal year.

Summary Balance Sheet (¥mn), FY2/12-FY2/13

	FY2/12	FY2/13	Change
Cash and cash equivalents	3,035	3,617	+582
Notes and sales receivable	4,954	4,764	▲ 189
Inventories	1,874	2,102	+227
Current assets	10,554	11,084	+530
Tangible fixed assets	2,861	2,910	+48
Intangible fixed assets	26	29	+3
Investments, other assets	898	946	+47
Total fixed assets	3,787	3,886	+98
Total assets	14,342	14,971	+628
Accounts payable	2,810	2,478	▲ 331
Advances received	1,223	1,279	+56
Current liabilities	5,204	5,015	▲ 189
Long-term accounts payable	322	326	+4
Reserve for retirement allowances	165	168	+3
Negative goodwill	42	34	▲ 7
Fixed liabilities	647	640	▲ 7
Total liabilities	5,852	5,655	▲ 196
Total liabilities and equity	8,489	9,315	+825

In FY2/13, Freund Corp.'s operations generated ¥740mn of cash, while its investments used ¥322mn and its financing used ¥164mn. The company's cash and cash equivalents increased by ¥352mn in FY2/13, and the balance of these assets came to ¥3,387mn at the end of the fiscal year. As the company has no debt, it has substantial net cash.

Summary Cash Flow Statement (¥mn), FY2/12-FY2/13

	FY2/12	FY2/13
Cash flow from operations	1,219	740
Income before taxes and adjustments	1,102	1,337
Depreciation expense	264	232
Change in sales receivables	▲ 813	217
Change in inventories	▲ 494	▲ 158
Change in other assets	141	203
Change in accounts payable	745	▲ 350
Change in advances received	673	2
Cash flow from investments	▲ 154	▲ 332
Purchases of tangible fixed assets	▲ 120	▲ 172
Cash flow from financing	▲ 134	▲ 164
Dividend payment	▲ 129	▲ 129
Change in cash and cash equivalents	902	352
Balance of cash and cash equivalents at term-en	3,035	3,387



■ Company Forecasts for FY2/14

Record-high profits, due in part to growth overseas

For FY2/14, the company projects a 12.8% y-o-y rise in consolidated sales to ¥18,500mn, a 19.0% increase in consolidated operating profit to ¥1,750mn, an 8.8% upturn in consolidated recurring profit to ¥1,760mn, and a 24.1% advance in consolidated net profit to ¥950mn. The company foresees a decline in demand for machinery from some east Asian countries due to the political situations in these countries, but it projects strong demand in the Americas and the Middle East. Therefore, it forecasts record-high profits for FY2/14, although smaller than targeted in its current medium-term plan.

The company expects sales at its machinery division to grow by 16.0% y-o-y in FY2/14 to ¥11.5bn. It believes new products will contribute to a 17.6% rise in sales of machinery to pharmaceutical and food companies to ¥9.7bn, while it foresees an 8.0% rise in sales of machinery to manufacturers of industrial products to ¥1.8bn. The company projects an 8.0% y-o-y increase in sales of chemicals to ¥7.0bn, with sales of pharmaceutical additives growing by 2.9% to ¥2.1bn, sales of food preservatives rising by 5.9% to ¥2.0bn, and sales of health foods advancing by 13.6% to ¥2.9bn. OEM sales of supplements to the leading Japanese maker of healthcare products are expected to remain brisk, and sales of a new health food, launched in Q1 FY2/12, are seen growing to a leading food company.

Consolidated Results in FY2/13 and Company Forecasts (¥mn) for FY2/14

	FY2/13		FY2/14		YOY
	Amount	Ratio	P/E Est.	Ratio	
Sales	16,396	100.0	18,500	100.0	12.8
Machinery	9,914	60.5	11,500	62.2	16.0
Pharmaceutical & Food Industries	8,248	-	9,700	-	17.6
Industrial Equipment Industry	1,666	-	1,800	-	8.0
Chemicals	6,482	39.5	7,000	37.8	8.0
Pharmaceutical Additives	2,041	-	2,100	-	2.9
Food Preservatives	1,889	-	2,000	-	5.9
Health Foods and Others	2,552	-	2,900	-	13.6
Operating profit	1,470	9.0	1,750	10.7	19.0
Recurring profit	1,618	9.9	1,760	10.7	8.8
Net profit	765	4.7	950	5.8	24.1

■ Medium-term Plan and Further Development

FY2/14 is the final year of the company' s current medium-term plan

(1) The final year of Vision-50

The company' s current medium-term plan, called Vision-50, targets consolidated sales of ¥20bn and consolidated operating profit of ¥2.0bn for FY2/14, both higher than the company' s current forecasts, of ¥18.5bn and ¥1.75bn, respectively. The company currently does not plan to revise its targets for FY2/14, indicating that it could exceed its forecasts for the year.

Aging of society and increased use of generic drugs benefit the company

(2) Expansion of existing markets

As Freund Corp. already holds high market shares for many kinds of machinery, particularly, granulation machinery, it may not be able to increase these shares significantly. However, the company would benefit from an expansion of existing markets for its customer industries. For example, the consumption of pharmaceuticals in Japan is likely to grow as Japanese society ages. In an effort to stem the rise in medical costs in Japan, the public and private sectors may promote the consumption of generic drugs, rather than brand drugs. Leading pharmaceutical companies will no doubt continue to develop new drugs to boost their shares of the global market. All these developments would support increased sales of Freund Corp.' s machinery and chemicals. Furthermore, sales of pharmaceuticals in 17 developing countries, led by the BRICS countries, are projected to grow by 6% per year. As these countries replace imported drugs with drugs made locally, they will need the machinery and chemicals made by Freund Corp.

Horizontal and vertical development possible

(3) Development of new markets

Freund Corp. should be able to apply its technology in machinery and chemicals to develop new markets. For example, if it could demonstrate that its seamless minicapsules enhanced the effectiveness of a drug, it could sell more of its machines to manufacture such capsules to pharmaceutical companies. Hard capsules are now used to deliver bifidobacteria to the large intestine. If Freund Corp. could show that the use of such hard capsules optimizes the effect of supplements, it could increase its sales of coating machinery to make hard capsules and its OEM production of supplements.

The company will probably apply its technology in granulation, powdering, sorting and pulverizing to produce new products that drive growth. It has already used technology acquired from subsidiary Freund-Turbo Corp. to enter the business of producing industrial machinery for the manufacture of fine chemicals. Hereafter, Freund Corp. intends to produce industrial machinery for the manufacture of toner materials, cosmetics, agro-chemicals, battery materials, and foods. The growth potential for such machinery is significant.



■ Shareholder Return Policy

Company aims to please shareholders

At the end of FY2/13, the company had no debt and an equity ratio of 61.4%. At the same time, management aims to maintain a dividend payout ratio of 20% on a consolidated basis. Thus, for FY2/13, the company paid a dividend of ¥20 per share, which was ¥5 higher than its dividend for FY2/12. For FY2/14, the company has announced that it will pay a dividend of ¥25 per share. Management obviously places a premium on capital efficiency and shareholder returns.

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