

Meiko Network Japan

4668 Tokyo Stock Exchange First
Section

25-Aug.-15

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at the end of this document.FISCO Ltd. Analyst
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■ Meiko Gijuku returns to growth path as student numbers gain YOY

On July 10, 2015, Meiko Network Japan Co., Ltd. announced its consolidated results for the first three quarters (from September 2014 through May 2015) of the fiscal year through August 2015 (Q1-Q3 FY8/15). Consolidated Q1-Q3 net sales increased 19.0% year on year (YOY) to ¥13,102mn and operating income was up 2.1% YOY to ¥2,135mn, both almost according to plan. The consolidation of MAXIS Education, the largest Meiko Gijuku franchisee, as a wholly owned subsidiary, drove double-digit net sales growth. Sales were otherwise flat, however, reflecting the impact of forward investments in other businesses. Still, measures to revitalize growth for the Meiko Gijuku business gradually bore fruit, with the number of students increasing 0.4% YOY through the end of May, reversing seven consecutive quarters of declines.

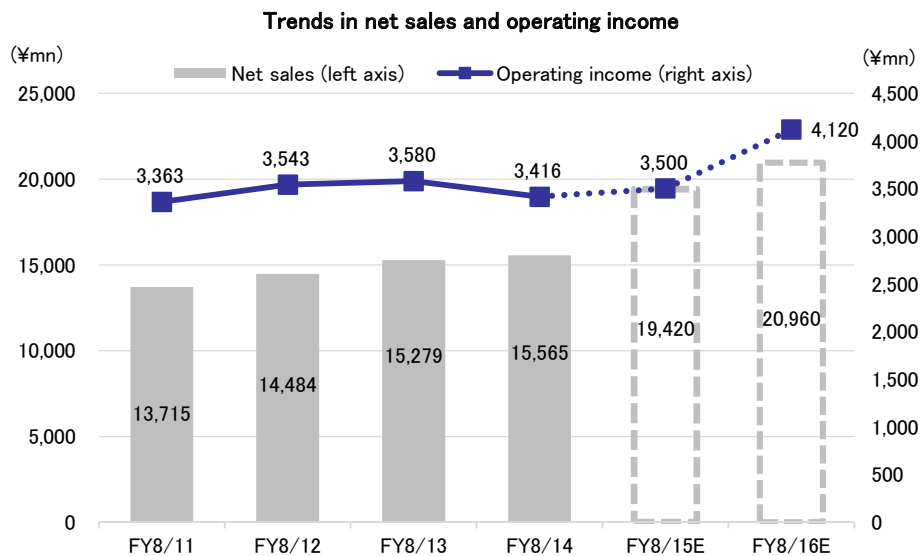
In other businesses, solid demand for childcare and after-school activities for elementary students contributed to steady growth for Meiko Kids Schools, which opened three facilities. All other operations expanded steadily, including Meiko Soccer Schools, Waseda Academy Kobetsu Schools, and Waseda EDU Japanese Language School, which became a subsidiary.

The company has retained its consolidated full-year forecasts for FY8/15 of net sales increasing 24.8% YOY to ¥19,420mn and operating income rising 2.5% to ¥3,500mn. Although the private tutorial school market continues to face intensified competition, the company is bolstering its infrastructure to rekindle growth for Meiko Gijuku operations. Efforts include deploying a unified area strategy with directly operated and franchised schools and reinforcing initiatives to enhance customer satisfaction at the Meiko Support Center. Internationally, the company announced a joint venture with a Taiwanese company in June to cultivate private tutorial schools locally. Other overseas efforts include running private tutorial schools in South Korea and kindergartens for Japanese children in Singapore. Taiwan is the third country outside Japan that the company has entered. It will be worth keeping tabs on progress down the track.

For FY8/15, the company plans to keep increasing dividends per share, raising them by ¥2.0 to ¥34.00 (for a dividend payout ratio of 41.5%). Management seeks to gradually increase the ratio to 50%. Based on a valuation of ¥1,400 per share at the close of trading on July 17, the gross investment yield per share unit, including shareholder special benefit plan (under which, each holder of 100 shares or more as of the end of August receives a ¥3,000 QUO card as a gift), was in the 4% level, significantly higher than the average dividend yield of around 1.5% for listed Japanese companies. This underscored the company's active stance on returning profits to shareholders.

■ Check Point

- Consolidating MAXIS and other factors boosted Q3 revenues and earnings
- Anticipating double-digit growth for the full term, the key driver being the Meiko Gijuku directly operated business
- For FY8/15, set to continue record of consecutive dividend increases since listing, generating a gross investment yield per share in the 4% level



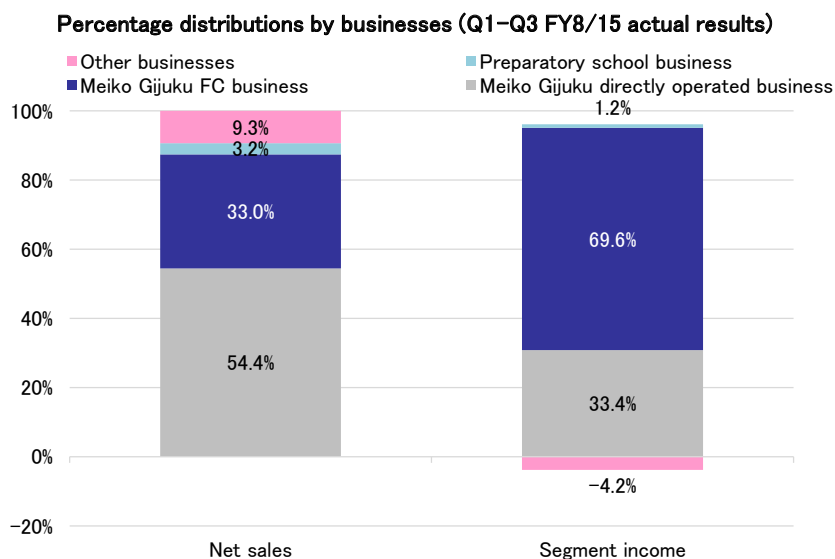
■ Description of Businesses

A leader among private tutorial schools, Meiko Gijuku Schools is the company's core business

Meiko Network Japan's main business is Meiko Gijuku Schools. Some of these schools are operated directly, but most are franchised. Meiko Gijuku is the leading brand of private tutorial schools in Japan. Through a subsidiary, Tokyo Ishin Gakuin (Tokyo Medical School Preparatory Institute), Meiko Network Japan also operates a preparatory school business specializing in preparation for medical university. In addition, the company engages in various other educational service businesses.

Among its other businesses outside tutorial and supplemental education are Meiko Soccer Schools for children. There is also Waseda Academy Kobetsu Schools, which provides tutorial instruction to junior high school and high school students seeking entry into prestigious high schools and universities. Meiko Kids Schools provides nursery care for preschool children and after-school care for elementary school children. Waseda EDU, which serves overseas students, is a subsidiary acquired in October 2014. The company's subsidiary YouDEC Co. publishes a magazine featuring information about the content of entrance examinations for junior high schools and high schools, produces model examination questions, sells educational materials to students of private schools, and offers private instruction to students at their schools. In addition, YouDEC's subsidiary, Koyo Shobo Co., is involved in the academic publishing business.

As detailed in the bar chart below, in Q1-Q3 FY8/15 the Meiko Gijuku business (directly operated and franchised operations) is the core source of the majority of Meiko Network Japan's total consolidated sales and profits. The company's policy described in its medium-term strategy calls for extending the growth of the Meiko Gijuku business while developing other educational businesses.



■ Business Trends

Consolidating MAXIS and other factors boosted Q3 revenues and earnings

(1) Overview of Q1-Q3 FY8/15

On July 10, 2015, the company announced its consolidated operating results for Q1-Q3 FY8/15 (September 2014 to May 2015). Consolidated net sales rose 19.0% YOY to ¥13,102mn, operating income increased by 2.1% to ¥2,135mn, ordinary income was up by 9.3% to ¥2,358mn, and net income rose by 8.4% to ¥1,486mn. The consolidation of MAXIS added ¥2,144mn to net sales, ¥218mn in operating income, and ¥107mn to the amortization of goodwill. Waseda EDU boosted ¥144mn to net sales and had a minor impact on operating income when including goodwill amortization. After excluding new consolidations, the company basically maintained the results of the previous corresponding term.

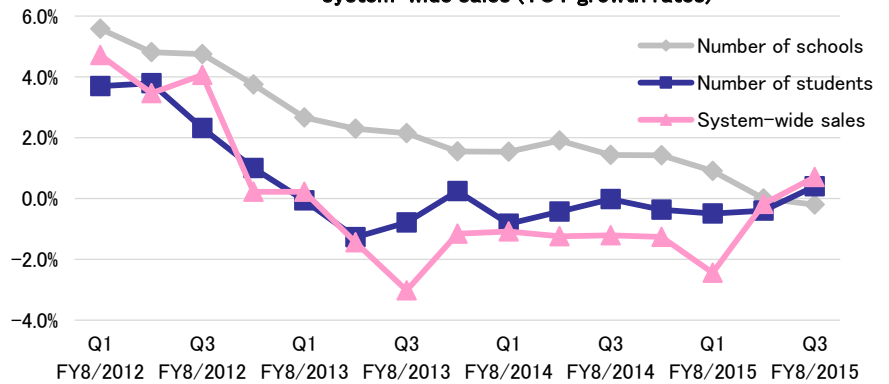
Q1-Q3 FY8/15 results (consolidated)

(unit: ¥mn)

| | Q1-Q3 FY8/14 | | Q1-Q3 FY8/15 | | |
|------------------|--------------|-----------|--------------|-----------|-------|
| | Actual | vs. Sales | Actual | vs. Sales | YOY |
| Net sales | 11,009 | - | 13,102 | - | 19.0% |
| Cost of sales | 6,916 | 62.8% | 8,516 | 65.0% | 23.1% |
| SGA expenses | 2,002 | 18.2% | 2,451 | 18.7% | 22.4% |
| Operating income | 2,090 | 19.0% | 2,135 | 16.3% | 2.1% |
| Ordinary income | 2,158 | 19.6% | 2,358 | 18.0% | 9.3% |
| Net income | 1,371 | 12.5% | 1,486 | 11.3% | 8.4% |

In the third quarter (March to May 2015), while the number of students at the core Meiko Gijuku business rose 0.4%, the first gain in seven quarters, it is also worth noting that school system-wide sales were up 0.7% YOY, the first gain in 10 quarters. With competition in the private tutorial school market continuing to intensify, the company's revenues had stagnated since FY8/13. Several initiatives to regenerate growth, however, have gradually proven fruitful. They have included such internal and organizational reforms as integrating directly operated and franchise schools and qualitatively and quantitatively enhancing communication with students and guardians through the new Meiko Support Center. Despite a slight decline in school numbers, the company will likely regain growth once earnings per school improve.

Meiko Gijuku business school and student numbers and system-wide sales (YOY growth rates)



Note: Including franchise schools. School and student numbers are as of term-ends. System-wide sales are aggregates for all of the sales of directly managed schools and administration fees, instruction charges and other sales (excluding educational materials charges and examination fees) for franchise schools.

The ratio of the cost of sales to sales was 65.0%, up 2.2 percentage points YOY, the principal cause being a higher personnel expense ratio from the acquisition of MAXIS. The SGA expenses ratio was 18.7% up 0.5 of a percentage point, but this was due mainly to an increase in amortization of goodwill for the consolidation of subsidiaries MAXIS and Waseda EDU (up ¥130mn YOY to ¥145mn). With that factor excluded, the ratio would have been negative 0.5 of a percentage point. The share of profit of entities accounted for using the equity method was up ¥68mn, while the gain on sales of investment securities and reversal of loss on valuation of investment securities rose ¥53mn, increasing non-operating income ¥156mn.

Even after factoring out the consolidation of subsidiaries, the Meiko Gijuku directly operated business achieved higher revenues and earnings

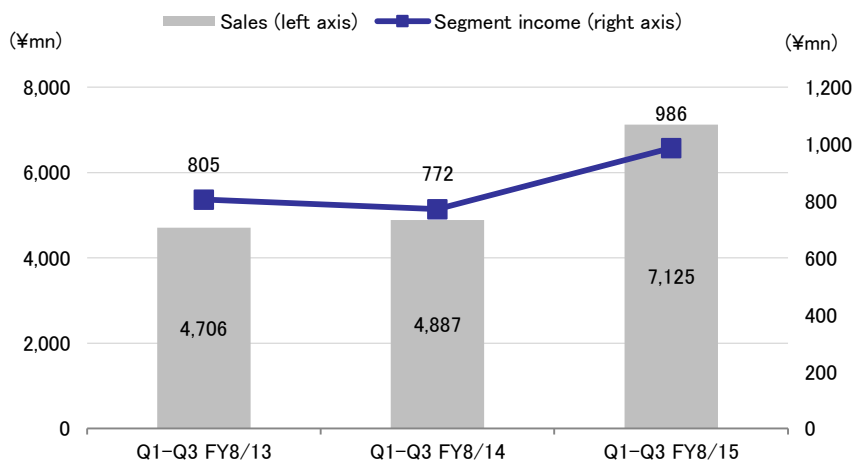
(2) Business segment trends

○Meiko Gijuku directly operated business

Sales in the Meiko Gijuku directly operated business segment increased by 45.8% YOY to ¥7,125mn, and segment income increased by 27.8% YOY to ¥986mn. The MAXIS contributions were ¥2,144mn in sales, ¥218mn in operating income, and ¥107mn in amortization of goodwill. Even without these contributions, net sales would have risen 1.9% YOY to ¥4,981mn, with segment income gaining 13.4% YOY to ¥875mn.

After excluding MAXIS, the number of directly operated schools increased by 3 YOY to 221 reflecting transfers from franchisees. The number of students as of the end of May advanced 3.6% YOY to 15,660. The average number of students per school was up by 1.5 YOY to 70.8, while sales per student also improved slightly, underscoring greater profitability per school. Measures to increase student numbers are gradually delivering results, including efforts to share information on successes in new student admission counseling, communicate better with students and guardians, and deploy an integrated area strategy with franchised schools. Progress in cost reductions has augmented efforts to boost revenues and boost earnings. MAXIS has 90 directly operated schools, each with an average 70.5 students at the end of May, for a total of 6,350.

Meiko Gijuku directly operated business



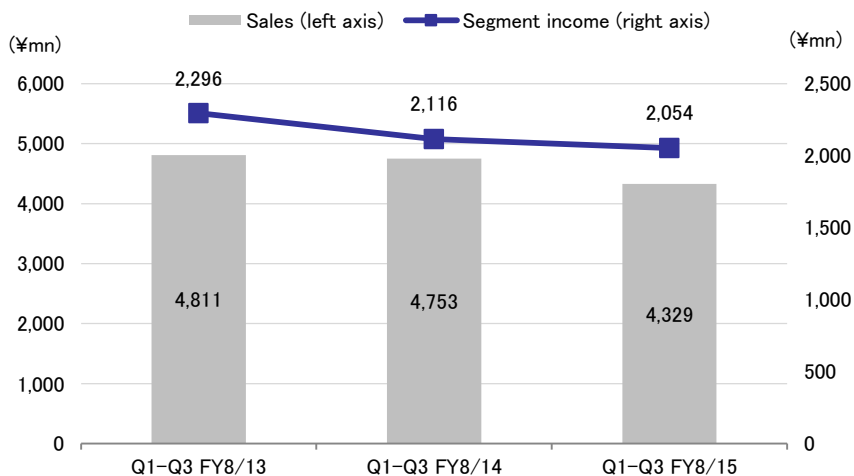
○ **Meiko Gijuku FC business**

Sales in the Meiko Gijuku FC business segment decreased 8.9% YOY to ¥4,329mn. Segment income declined 2.9% to ¥2,054mn.

Including the 90 of MAXIS, the number of franchised schools as of the end of May declined 8 YOY to 1,901, and the number of students was down 0.1% YOY to 102,853. The main factor in stagnant student numbers was a downturn in the Kyushu area, where competitions has continued to intensify. The number of students dropped by 477 YOY in Kyushu, while the number rose by 533 in other areas. Still, compared with the decline of 1,604 as of the end of February, the pace of the decline in the Kyushu area has slowed greatly, and there are signs that the downturn is beginning to bottom out. On top of that, the average number of students per school increased by 0.2 YOY, to 54.1, the first rise in four years. This indicates that measures to increase student numbers at franchised schools have begun bearing fruit, albeit belatedly compared with directly operated ones.

From FY8/15, the company restructured organizations by area. This made it easier to deploy area campaigns jointly with directly operated schools, notably producing leaflets to solicit students. While stepping up activities to attract students, the company has been able to reduce costs for franchised schools.

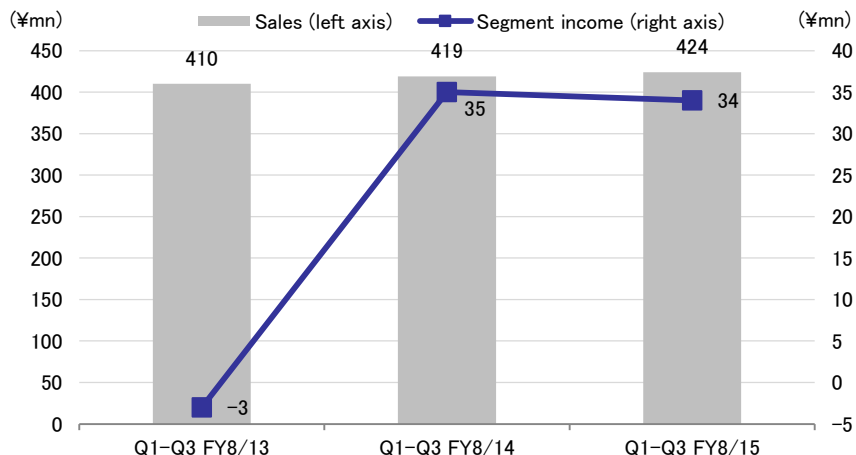
Meiko Gijuku FC business



○Preparatory school business

Sales in the preparatory school business that Tokyo Ishin Gakuin (Tokyo Medical School□Preparatory Institute) operates increased by 1.2% YOY to ¥424mn. Segment income dropped 3.3% to ¥34mn. Though revenues continued declining through Q2 FY8/15, there was a payoff from focusing on consultations with students and guardians for medical university entries and from advertising on websites for medical professionals and in specialist magazines, with new admissions surging for spring 2015. Q3 FY8/15 alone, segment sales rose 20.2% YOY and segment income was ¥7mn (from a ¥14mn loss in Q3 FY8/14). The number of students at the end of May was up 26 YOY to 151, the highest number of students at that time of the year since Tokyo Ishin Gakuin became a subsidiary.

Preparatory school business



○Other businesses

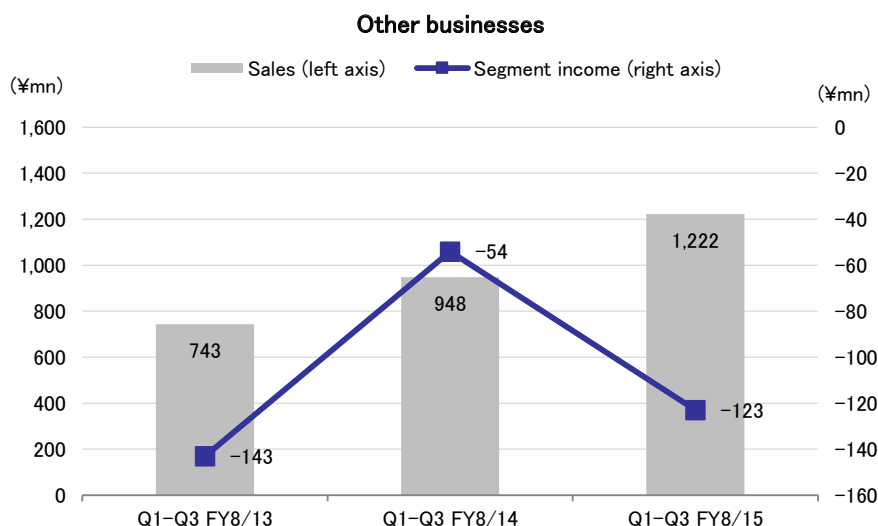
Sales for other businesses increased 36.1% YOY to ¥1,222mn. The segment loss was ¥123mn, up from ¥54mn a year earlier.

By operation, Meiko Soccer Schools posted sales of ¥102mn (¥96mn in Q1-Q3 FY8/14) and an operating loss of ¥11mn (¥18mn in Q1-Q3 FY8/14). The number of directly operated schools decreased by 1 YOY to 14, for a total of 16 schools, including two franchised ones. However, the total number of students for directly operated and franchised schools combined expanded to 1,003, at the end of May, up 134 YOY. The issue in increasing school numbers continued to be finding futsal courts for practice.

Sales from Waseda Academy Kobetsu Schools were ¥256mn (¥190mn in Q1-Q3 FY8/14), and the operating loss edged up to ¥29mn. This was despite an increase in sales, and was due to operating system expenses, which had been recorded as corporate expenses, being allocated to business segment expenses from FY8/15. Excluding this factor, the segment saw a slight increase in income. The number of directly operated schools was 6 (up 3 YOY). The number of franchised schools was 10 (down 4 YOY), and the number of Waseda Academy directly managed schools was 9 (up 3 YOY). The number of students at the end of May climbed to 1,525 (up 422 YOY). A key factor in the student number growth was the track record the schools have built as many students have passed entrance exams for highly selective junior high and high schools. There was a reduction of four franchised schools; two of the four are directly operated by MAXIS and now count as directly operated.

Sales from Meiko Kids Schools expanded from ¥44mn a year earlier to ¥78mn, a 1.7-fold increase. Losses increased, however, reflecting increased initial outlays on opening three new schools in spring 2015. Amid strong demand for elementary student childcare and after-school activities, student admissions at two of the new schools have increased significantly, and numbers at the other school have risen steadily.

There were ¥144mn in sales from the Japanese language school of Waseda EDU, which became a consolidated subsidiary in Q2. The number of students remained high, at 393, as of the end of May. Although the school posted some operating profits, it is unlikely to contribute to the company's operating income after ¥22mn in goodwill amortization. To accommodate solid demand, in July the company raised student capacity by 100, to 520. Admissions to the Japanese language school are in April, July, October and January. As of July, the number of students increased to around 440 with new admissions. By October, we expect the school to be at full student capacity.



Maintaining a high equity ratio despite M&As lowering current ratio

(3) Financial status and management indicators

In the Company's financial status as of the end of May 2015, total assets were ¥17,095mn, up ¥526mn from the end of FY8/14. The main factors were a ¥1,266mn decrease in cash and deposits, mainly from acquisitions of MAXIS and Waseda EDU shares, and a ¥1,889mn rise in goodwill.

Total liabilities stood at ¥3,338mn, down ¥39mn from the end of FY8/14, reflecting lower income taxes payable despite an increase of advances received as a result of the consolidations of two subsidiaries. Net assets increased ¥565mn YOY to ¥13,756mn, reflecting a rise in retained earnings.

Although the current ratio was down following a decrease in cash and deposits, the equity ratio remained above 80% owing to earnings gains, and since the company continued to manage virtually without debt, we consider that it has continued to maintain a good financial status.

Consolidated balance sheet and management indicators

| | FY8/14 | Q3 FY8/15 | Changes | Factors for change |
|------------------------------------|---------------|---------------|------------|---|
| Current assets (cash and deposits) | 9,707 | 8,334 | -1,373 | Acquisition of shares of MAXIS, Waseda EDU (¥1,513mn) Goodwill increased by ¥1,889mn |
| | 7,363 | 6,096 | -1,266 | |
| Fixed assets | 6,860 | 8,760 | 1,899 | |
| Total assets | 16,568 | 17,095 | 526 | |
| Current liabilities | 2,774 | 2,643 | -131 | Advances received (+¥484mn) and income taxes payable (-¥626mn) |
| Fixed liabilities | 602 | 695 | 92 | |
| Interest-bearing debt | 70 | 99 | 29 | |
| Total liabilities | 3,377 | 3,338 | -39 | |
| Net assets | 13,191 | 13,756 | 565 | Retained earnings increased by ¥575mn |
| Measures of financial stability | | | | |
| Shareholders' equity ratio | 79.4% | 80.2% | | |
| Current ratio | 349.8% | 315.3% | | |
| Interest-bearing debt ratio | 0.4% | 0.6% | | |

■ Outlook

Anticipating double-digit growth for the full term, the key driver being the Meiko Gijuku directly operated business

(1) Financial outlook for FY8/15

Meiko Network Japan has left its outlook for consolidated financial results for FY8/15 unchanged, planning net sales of ¥19,420mn, up 24.8% YOY, operating income of ¥3,500mn, up 2.5% YOY, ordinary income of ¥3,620mn, up 2.5% YOY, and net income of ¥2,260mn, up 2.7% YOY.

Through Q3 FY 8/15, the company attained 67.5% of its full-year net sales forecast and 61.0% of its operating income forecast. Compared with the average Q3 achievement levels of the last three years (70.4% of net sales and 60.6% of operating income), sales lagged forecasts slightly, as the Meiko Gijuku franchise business was slightly weaker than anticipated. Earnings grew in line with previous averages, however, and we think that the company can reach its targets if there are no major changes in the market climate.

In sales forecasts for each business, the Meiko Gijuku directly operated business should boost its revenues 48.7%, owing partly to the contribution of MAXIS, but franchised school sales should rise only 0.3%. As well as expanding market share through such efforts as opening satellite schools in areas with solid demand, the company plans to boost the profitability of franchised schools.

The company plans a 1.2% YOY increase for the preparatory school business. We think that it will slightly exceed its targets, however, as the number of admissions for spring 2015 was more than expected, as mentioned earlier.

With regard to other businesses, the company's policy is still to increase school numbers at Meiko Soccer School, Waseda Academy Kobetsu Schools, and Meiko Kids Schools, and management is forecasting an increase in sales due to an increase in student numbers. The company anticipates more sales gains for Waseda EDU owing to higher student numbers. That said, the company expects Meiko Kids Schools to incur a slightly higher operating loss because of greater upfront investments.

Sales by segment

| | (¥mn) | | | | |
|---|--------|--------|--------|---------|--------|
| | FY8/12 | FY8/13 | FY8/14 | FY8/15E | Growth |
| Meiko Gijuku directly operated business | 6,864 | 6,814 | 7,062 | 10,503 | 48.7% |
| Meiko Gijuku FC business | 6,736 | 6,613 | 6,565 | 6,582 | 0.3% |
| Preparatory school business | 559 | 597 | 593 | 600 | 1.2% |
| Other businesses | 324 | 1,319 | 1,434 | 1,733 | 20.8% |
| Eliminations | - | -66 | -88 | - | - |
| Total | 14,484 | 15,279 | 15,565 | 19,420 | 24.8% |

Income by segment

| | (¥mn) | | |
|--|--------|--------|--------|
| | FY8/12 | FY8/13 | FY8/14 |
| Meiko Gijuku directly operated business | 1,443 | 1,461 | 1,455 |
| Meiko Gijuku FC business | 3,313 | 3,276 | 3,072 |
| Preparatory school business | -7 | 37 | 58 |
| Other businesses | -120 | -126 | -44 |
| Corporate expenses, amortization of goodwill, etc. | -1,086 | -1,068 | -1,126 |
| Total | 3,543 | 3,580 | 3,416 |

Targeting record operating income for the first time in three years in FY8/16, the final year of three-year medium-term business plan

(2) Three-year medium-term business plan

For FY8/16, when its three-year medium-term business plan ends, the company targets net sales of ¥20,960mn and ¥4,120mn in operating income. Management seeks to post record operating income in this term for the first time in three years.

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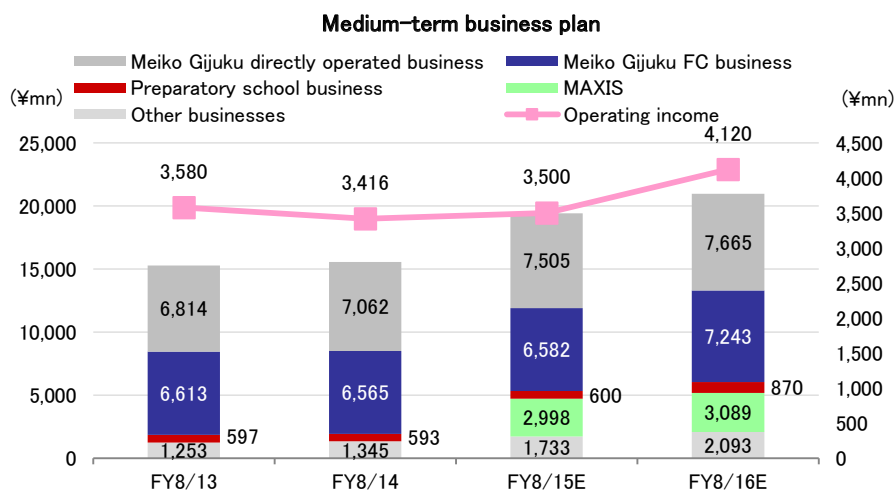
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* An instructional technique for boosting academic results by teaching self-learning techniques so students can find answers through independent thought and inquiry rather than being taught the answers.

Looking at the sales plan by business, the company looks for expansion in the Meiko Gijuku directly operated and franchised school businesses, with the preparatory school business and other businesses also delivering gains. Management aims to retain the Meiko Gijuku business as central to earnings while pushing ahead strategically to expand school and student numbers in other educational service businesses, thereby bolstering revenue and earnings underpinnings.

The Meiko Gijuku franchise business, which accounts around 70% of operating income, is the key to achieving the three-year medium-term business plan. The key factor in a 10% sales rise for the franchise business in FY8/11 was that both the number of schools and students advanced 5% YOY, while sales per student also increased. The situation is admittedly harder, as competition has intensified among private tutorial schools because the pie has shrunk as the number of children has declined. That said, the company plans to achieve its three-year plan by continuing to focus on measures to regenerate growth.

Specifically, we expect the number of students and new school openings to increase more efficiently owing to the integration of the Meiko Gijuku Directly Operated Business Division and Meiko Gijuku Franchised Business Division and the reorganization of businesses by area. In addition, the company will bolster the support center established to enhance customer satisfaction and thereby endeavor to retain students. Also, the company has started boosting instructor training (stratified training) at directly managed and franchised schools alike through systematized initiatives to enhance operational capabilities. Augmenting these initiatives, the company plans to expand student numbers by highlighting “Meiko-style! Self-supported learning” to differentiate itself competitively.



Note: The most recent company forecasts used for FY8/15 segment sales

Developing private tutorial school business in Taiwan as the third country outside Japan that the company has entered

(3) Cultivating private tutorial schools in Taiwan

One of the company's growth strategies is to expand the scope of its educational services. As a part of its efforts, it announced in June that it would develop a private tutorial school business in Taiwan.

The stated goal is to establish a joint venture by the end of October 2015 with local educational firms Han Lin Publishing Co., Ltd., and Baida Culture and Education Company Limited to develop this business. The approach will be to conclude a master franchise agreement with the joint venture. The company would have a 25% stake in that entity, receiving fees for franchise rights. A specific schedule to roll out operations will be determined in future discussions.

Han Lin Publishing is a diversified firm, engaging in group tutorial schools and publishing textbooks and other educational materials. Baida Culture and Education strategically oversees three tutorial school businesses in Taiwan. Baida Culture and Education currently operates 17 such schools. With demand for private tutorial schools expected to grow in Taiwan, the company aims to take advantage of market growth, thereby supplying its expertise to the joint venture.

Taiwan is the third country outside Japan that the company has entered. In South Korea, it launched a private tutorial school business through NEXCUBE Corporation (an equity method affiliate in which it has a 24.4% stake), formed in 2011 through a capital partnership. In 2014, the company opened a kindergarten for Japanese children in Singapore. While the impacts of these operations on the company are still minor, it is worth keeping tabs on overseas businesses, which could become important in the years ahead.

■ Shareholder Return Policy and Social Contribution Initiatives

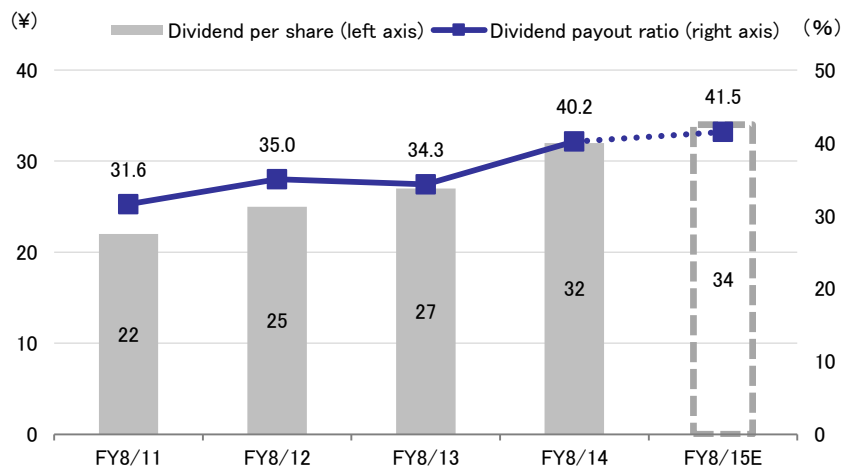
For FY8/15, set to continue record of consecutive dividend increases since listing, generating a gross investment yield per share in the 4% level

For FY8/15, management intends to raise dividends by ¥2 per share, to ¥34.00 (for a dividend payout ratio of 41.5%), retaining its record of continued dividend growth since listing. The company ultimately targets a ratio of 50%. The Company maintains a shareholder special benefit plan of giving shareholders as of August 31 a QUO card worth ¥3,000 per share unit (100 shares). On the basis of the closing share price of ¥1,400 on July 17, 2015, the gross investment yield per share unit is in the 4% level, which far exceeds the average gross investment yield for listed companies of about 1.5%.

Also, with regard to ROE (Return On Equity), which is gaining importance as an investment indicator, the company's actual figure was 17.6% for the previous fiscal year, which far exceeds the average 8.5% for the companies listed on the first section of the Tokyo Stock Exchange, and thus will gain continued attention as an attractive company to invest in.

The company constantly engages in social contribution initiatives. The latest example is Meiko Kyoiku Kenkyujo, a foundation that Hirotake Watanabe, president, and Yoshiko Okui, vice president, established in May 2014. That entity gained authorization in April this year as a public foundation. The foundation accepted its first applications for a scholarship program in December 2014, deciding to offer scholarships without repayment obligations to 45 underprivileged students. Also, the company made donations to a school feeding initiative of the United Nations World Food Programme in February this year and for earthquake relief efforts in Nepal in April.

Dividend per share and dividend payout ratio



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