Nagaileben
7447 Tokyo Stock Exchange First Section

19-May-15

Important disclosures and disclaimers appear at the end of this document.

FISCO Ltd. Analyst
Noboru Terashima

Q2 Results Steady Overall, Remain within Forecast Range

Nagaileben Co., Ltd. <7447> (hereafter, "Nagaileben" or "the Company") is the leading manufacturer of medical gowns in Japan, with a domestic market share of over 60%. In the consolidated business results for Q2 FY8/15 (September 2014 – February 2015) announced by the Company, sales amounted to ¥6,840mn, a 1.0% increase year on year ("y-o-y"); operating profit amounted to ¥1,797mn, a 1.9% decrease y-o-y; recurring profit amounted to ¥2,033mn, a 5.6% increase y-o-y; and net profit amounted to ¥1,302mn, a 3.0% increase y-o-y. Production costs increased due to the yen's depreciation, driving operating profit lower y-o-y; however, profits increased from the recurring profit line downward owing to a U.S. dollar deposit foreign exchange hedge. Since the company usually experiences lower sales and profit through the first half of the fiscal year, the result is not a cause for concern.

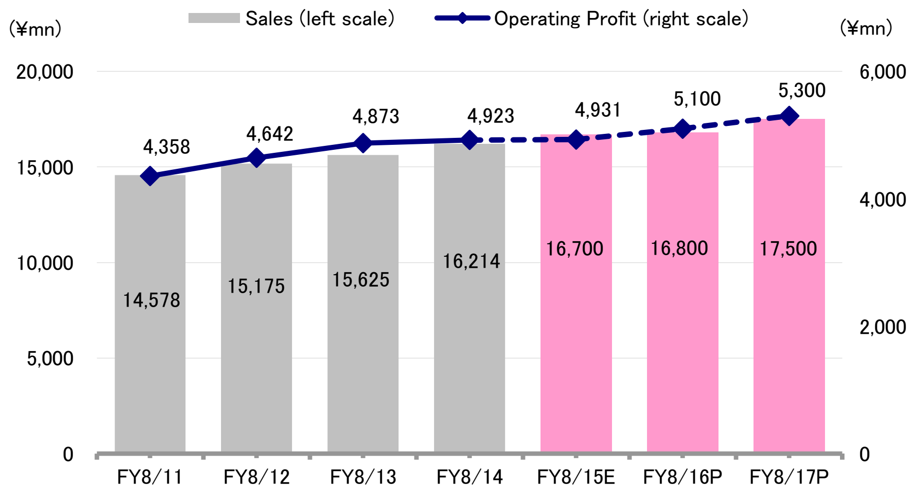
In its full-year business results for FY8/15, the current fiscal year, the Company expects to achieve: ¥16,700mn in sales, a 3% increase y-o-y; ¥4,931mn in operating profit, a 0.2% increase y-o-y; ¥5,058mn in recurring profit, a 1.1 decrease y-o-y; and ¥3,187mn in net profit, a 1.1% increase y-o-y. The forecasts for operating profit and net profit have been revised downward slightly from the initial forecast, while the forecast for recurring profit has been revised upward. However, in all cases the revisions are minor, and no cause for concern.

The company announced a new Mid-Term Management Plan, (numerical targets: sales of ¥17,500mn and operating profit of ¥5,300mn by FY8/17), and these targets have not changed. The Company plans to achieve these goals by expanding overseas production and strengthening its high-margin advanced functionality product range. Furthermore, the Company is taking a positive stance on shareholder returns, having already conducted a share buy-back of approximately 1.0mn shares (¥1,500mn) in FY8/15 through a takeover bid (TOB). As a result, combined with the forecast dividend (¥50 annual) the total return ratio for FY8/15 is expected to reach around 100%. This is certainly worthy of note.

Check Point

- System for integrated operations from planning through to raw material procurement, manufacture and sales is a key strength
- Consolidated business results for Q2 steady within forecast range overall
- Stable operating environment, aiming for record-high sales and operating profit

Sales and Operating Profit



Company Profile

Leading medical gown manufacturer with a share of over 60% of the domestic market for medical gowns for nurses

(1) Description of businesses

Nagaileben is a specialist manufacturer of medical gowns for nurses, doctors, patients and others. Established in 1915 as Nagai Shoten, the Company has a rich history. Since then, it has expanded its operations nationally to become a leading domestic manufacturer with a share of over 60% of the market for medical gowns for nurses.

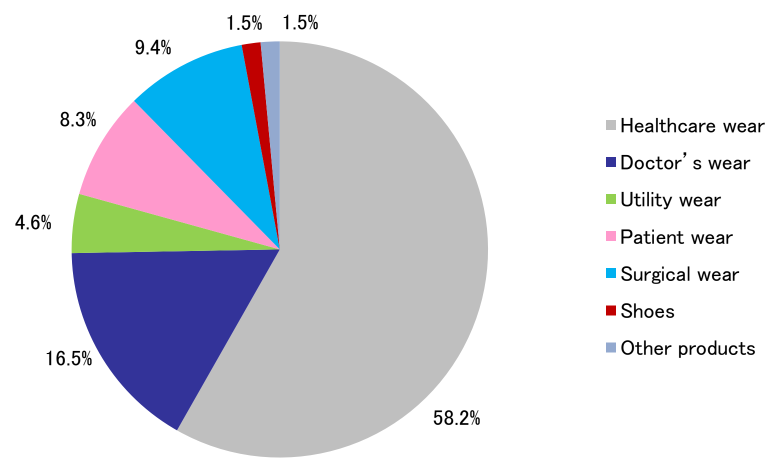
Company History

1915	Founded business specializing in medical gowns in Kanda-Jinbocho in Tokyo, Japan, as Nagai Shoten, privately owned by Koji Nagai.
1950	Liquidated Tokyo Eisei Hakui Co. Ltd. Koji Nagai and Tatsuro Sawanobori jointly established Nagai Shoten Co. Ltd.
1969	Established a subsidiary, Nagai Hakui Kogyo Co. Ltd., in Akita Prefecture to expand the medical gowns manufacturing division. Tatsuro Sawanobori was appointed President. Shifted focus of manufacturing and sales business specialization from multi-purpose white gowns to medical gowns.
1977	Built second product center in Kameido, Tokyo. Established partnership with a US company, G.D. Searle & company; and established Japan Surgical Apparel Co. Ltd. in Hiroshima to expand sales of new surgical apparel products for hospitals.
1978	Established technology partnerships with Angelica Corp (US) and Toray Industries, Inc. Developed and released medical gowns made with new fabric for leasing.
1980	Changed name to Nagai Co. Ltd. Opened sales office in Takamatsu, Kagawa. Concluded a license agreement with designer Kansai Yamamoto.
1982	Concluded a license agreement with designer Yukiko Hanai.
1988	Established Emit Co. Ltd. as a spin-off from Nagai Co. Ltd. Thereafter, the two companies exchanged their names, with Emit Co. Ltd. becoming a group management company, and Nagai Co. Ltd. becoming a group headquarters for sales.
1989	Newly built new Nagai Luminous, a manufacturing plant for high grade products, in Akita Prefecture. Started overseas production for global division of labor.
1994	Changed name from Nagai Co. Ltd. to Nagaileben Co. Ltd. Built a new logistics center in Akita Prefecture.
1995	Started over-the-counter trading of the company's stock. Started development and sales of a second pillar product to respond to the aging society. Vice President Ichiro Sawanobori appointed President.
1996	Concluded an agreement with French designer Andre Courreges.
1999	Opened sales office in Nagoya, Aichi Prefecture. Concluded a license agreement with designer Atsuro Tayama.
2001	Listed on the second section of Tokyo Stock Exchange.
2002	Established technology partnership with Standard Textile company, Inc. (US) and Toray Industries, Inc. for surgical textiles. Raised the status of Nagoya sales office to a branch.
2004	Acquired ISO 9001. Listed on the first section of Tokyo Stock Exchange. Absorbed Hokkaido Nagai Co. Ltd. and established Hokkaido branch.
2005	Acquired ISO 14001. Concluded a license agreement with designer Keita Maruyama.
2006	Concluded a brand agreement with designer Minako Yokomori.
2014	Relocated to new head office building in Kajicho, Chiyoda Ward, Tokyo.

●Sales Breakdown

All of the Company's products are medical gowns and related products. The sales contribution by item (FY8/14) is healthcare wear 58.2%, doctor's wear 16.5%, surgical wear 9.4%, patient wear 8.3%, utility wear 4.6%, shoes 1.5% and other products 1.5%. Healthcare wear consists of products mainly for nurses and carers, and utility wear consists of aprons, cardigans, and other items worn as outer garments. Profit margins for each item do not vary significantly; however, the profit margins of purchased products, such as shoes, are relatively lower.

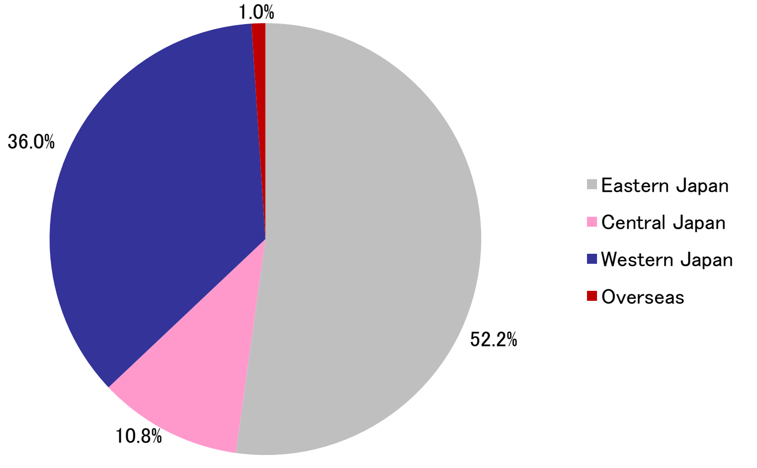
Sales Breakdown by Item (FY8/14)



We encourage readers to review our complete legal statement on "Disclaimer" page.

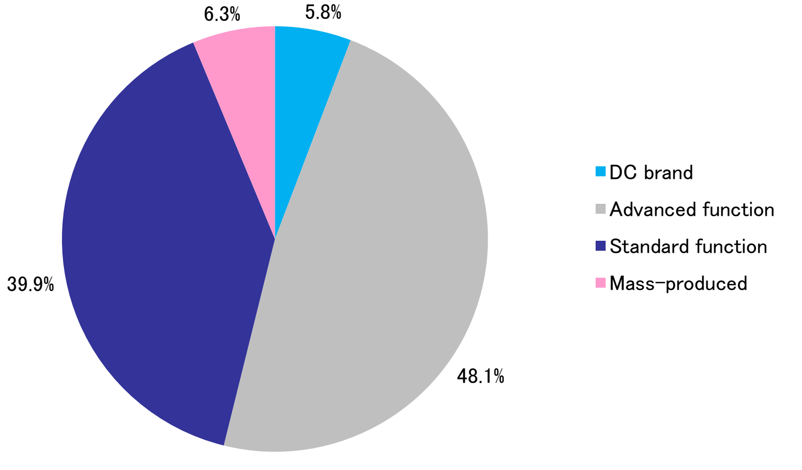
In terms of sales contribution by region, eastern Japan accounts for 52.2%, western Japan 36.0%, central Japan 10.8%, and overseas 1.0%. While coverage is nationwide, sales in central Japan and abroad remain low, indicating potential for future expansion.

Sales Breakdown by Region (FY8/14)



In terms of sales contribution by product (function), advanced-function products made up 48.1%, standard-function products 39.9%, mass-produced products 6.3%, and DC brand products 5.8%. As an example, in nursing wear products, when classified by price range, mass-produced products are under ¥5,000, standard-function products are ¥5,000-7,500, advanced-function products are ¥7,500-10,000, and DC brand products are over ¥10,000; the higher the price, the greater the profit margin.

Sales Breakdown by Product (FY8/14)



●Sales channels and production status

The company's end users include nurses, carers and doctors, with the purchasers of the products being mainly medical facilities such as hospitals, nursing care facilities and others. However, the company does not conduct direct sales, with 100% being agency sales via medical equipment wholesalers that trade with these medical and other facilities. As a result, direct sales expenses are contained; however, as sales staff is constantly in contact with large hospitals and other facilities, the company understands customers' needs.

In most cases, medical gowns are laundered within the hospitals by the hospitals themselves, but in recent years they have been switching to leasing. The lease term is typically four years. Because this generates lease switching demand every four years, it seems to provide stable support for the company's earnings.

Looking at the company's production structure, based on FY8/14 performance, 97.4% of its products are manufactured in-house (domestic production: 54.3%, overseas production: 43.1%) and 2.6% are purchased products. Overseas production is predominantly in Indonesia, but the company owns no factories and the goods are produced at factories of local partners, which mitigates investment risk and reduces costs.

System for integrated operations from planning through to raw material procurement, manufacture and sales is a key strength

(2) Distinctive characteristics and strength

The company is a specialized manufacturer of medical gowns, and one of its strengths is that it has in place systems to undertake everything from design to raw material procurement, manufacturing and sales. In its product planning, it can accurately understand customer needs and reflect them in its products. Specifically, the company works with major synthetic fiber manufacturers, such as Toray <3402> to develop functional textiles, including antibacterial, anti-static, industrial washable specification (reduced cost) textiles. It also supplies products of excellent design, which have earned a good reputation from its users. At the same time, it also incorporates overseas production, enabling it to sell its products at an appropriate margin.

Furthermore, in addition to its large number of affiliated factories, the company has the necessary financial resources to be able to constantly maintain product item inventories that extend into the thousands of varieties, while also being able to swiftly respond to a broad range of user needs, including for made-to-order products, through a rapid production and sales system (the Quick Response system) that delivers the desired product on a specified day. This has also helped it to earn strong trust from its customers. On the sales side, it has a network of close to 1,000 agents nationwide, and while its sales capabilities are robust, the company itself controls its sales expenses as much as possible.

As a result, the company's share of the domestic market for medical gowns for nurses exceeds 60%, and it maintains a firm position as the leading medical gown manufacturer in Japan. Additionally, it has maintained profitability with a gross margin of 46.8% (actual results for FY8/14). The fact that it is both highly profitable and has a high market share means that most of its customers are satisfied with its products and services, which is the company's greatest strength.

By concentrating its business resources in the niche market of medical gowns, the company can efficiently manage everything from design to manufacturing and sales. Moreover, although it is a niche market, room for further development remains, as it has relatively low market shares for patient wear, surgical wear and other items. The company has explicitly stated that the medical gown business could grow for some time and it will move aggressively to develop peripheral markets.

We encourage readers to review our complete legal statement on "Disclaimer" page.

Earnings Trends

Consolidated business results for Q2 steady within forecast range overall

(1) Summary for the Q2 of FY8/15

●Status of profit and loss

In the consolidated results for the Q2 FY8/15, the Company achieved: sales of ¥6,480mn, a 1.0% increase y-o-y; operating profit of ¥1,797mn, a 1.9% decrease y-o-y; recurring profit of ¥2,033mn, a 5.6% increase y-o-y; and quarterly net profit of ¥1,302mn, a 3.0% increase y-o-y. Sales and operating profit were both slightly lower than initially forecast, partly due to somewhat lackluster performance in Q1. However, recurring profit and net profit both surpasses the initial forecast, mainly due to gains on foreign exchange gains. The divergence from the initial forecast was small, however, and overall results were within the scope of the forecast.

Consolidated results

(¥mn)

	Q2 FY8/14		Q2 FY8/14			
	Amount	Sales %	Amount	Sales %	Change	y-o-y
Sales	6,775	100.0%	6,840	100.0%	64	1.0%
Gross profit	3,169	46.8%	3,187	46.6%	18	0.6%
SG&A costs	1,337	19.7%	1,390	20.3%	52	3.9%
Operating profit	1,831	27.0%	1,797	26.3%	-33	-1.9%
Recurring profit	1,925	28.4%	2,033	29.7%	107	5.6%
Net profit	1,264	18.7%	1,302	19.0%	37	3.0%

Sales were up 1.0% y-o-y, but still came in 1.6% below plan. There were no major changes in the market environment, and the lower-than-expected result was due to a delay in a contract renewal . Such factors are not a cause for concern. The gross profit margin declined to 46.6% from 46.8% in Q2 FY8/14, which reflects the gradually emerging effect of cost increases due to the yen's depreciation. Higher prices for raw materials and processing fees had a negative impact of -¥11mn on gross profit, while foreign exchange rate effects reduced profit by ¥35mn as the yen slid from ¥87.4 to ¥91.5 against the U.S. dollar y-o-y. On the other hand, there was a positive impact of around ¥43mn resulting from an increase in the ratio of overseas production, from 42.7% to 45.2%.

Selling, general and administrative (SG&A) costs climbed 3.9% y-o-y to ¥1,309mn. The main factor driving this increase was an increase in depreciation cost (¥35mn) due to the relocation to a new head office. However, the increase had been factored in initially, and SG&A costs were actually 2.6% lower than planned.

Meanwhile, the greater-than-expected increase in recurring profit was mainly due to increases in non-operating profit, particularly foreign exchange gains. To hedge against the effects of the yen's depreciation on the cost of sales, the company held deposits in U.S. dollars. The foreign exchange gain arising from these deposits increased dramatically from ¥56mn in Q2 FY8/14 to ¥220mn. Meanwhile, in extraordinary profit/loss, a gain on sale of fixed assets of ¥114mn recorded in Q2 FY8/14 (in association with the relocation to the new head office) was not recorded this year. As a result, the rate of increase in net profit was lower than that of recurring profit.

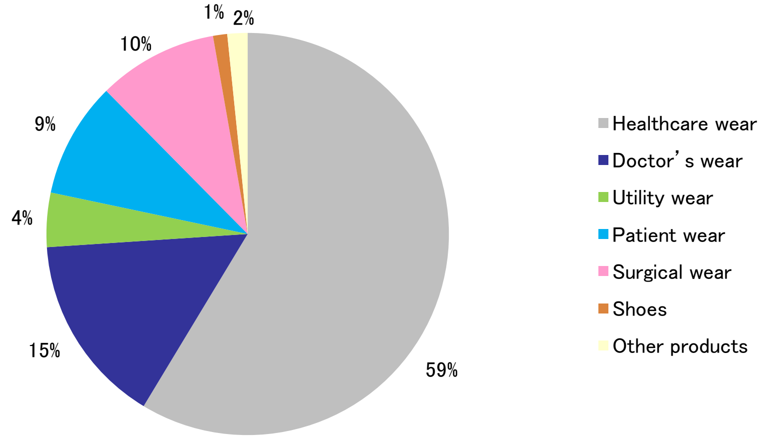
●Sales Breakdown by item

Sales Breakdown by Item

(¥mn)

	Q2 FY8/14		Q2 FY8/14	
	Amount	y-o-y	Amount	y-o-y
Healthcare wear	3,914	+5.1%	4,011	+2.5%
Doctor's wear	1,064	+8.4%	1,046	-1.7%
Utility wear	334	-4.9%	298	-10.9%
Patient wear	617	+6.3%	635	+2.9%
Surgical wear	641	+3.3%	659	+2.7%
Shoes	87	-13.5%	77	-10.6%
Other products	114	+14.6%	110	-3.5%
Total	6,775	+4.8%	6,840	+1.0%

Sales Breakdown by Item (Q2 FY8/15)



In sales by item; healthcare wear amounted to ¥4,011mn, a 2.5% increase y-o-y; doctor's wear amounted to ¥1,046mn, a 1.7% decrease y-o-y; utility wear amounted to 298mn, a 10.9% decrease y-o-y; patient wear amounted to ¥635mn, a 2.9% increase y-o-y; surgical wear amounted to ¥659mn, a 2.7% increase y-o-y; shoes amounted to ¥77mn, a 10.6% decrease y-o-y; and other products amounted to ¥110mn, a 3.5% decrease y-o-y.

In the core healthcare wear segment, results came in somewhat lower than the company's plan, mainly reflecting changes in renewal demand for some products and delayed recording of sales. However, the product segment still managed to record its highest ever Q2 sales. In doctor's wear sales declined y-o-y because of a high rate of growth (8.4%) in Q2 8/14, and there were no particular changes in market trends. Utility wear recorded a significant decline in sales as the shift away from individual supply toward shared use of items continued. Patient wear performed strongly against growing market demand. Surgical wear also market a steady increase in sales driven by market penetration of scrub wear and compel packs.

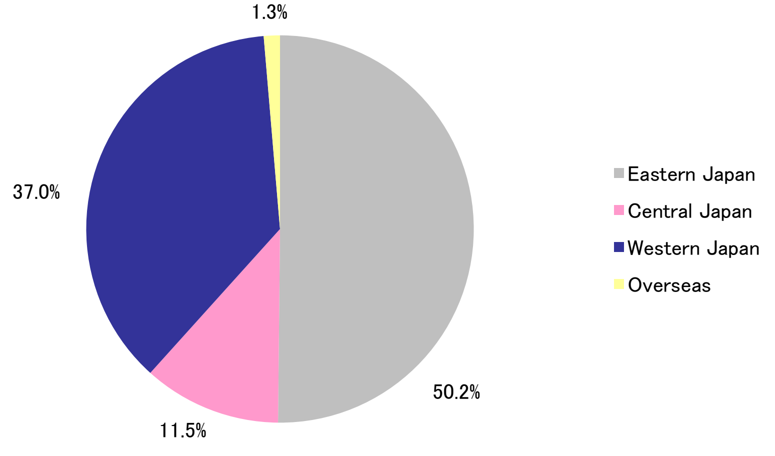
Sales Breakdown by Region

(¥mn)

	Q2 FY8/14		Q2 FY8/15	
	Amount	y-o-y	Amount	y-o-y
Eastern Japan	3,422	+0.0%	3,430	+0.3%
Central Japan	779	+25.1%	787	+1.0%
Western Japan	2,503	+6.1%	2,529	+1.0%
Overseas	70	+21.6%	92	+31.5%
Total	6,775	+4.8%	6,840	+1.0%

We encourage readers to review our complete legal statement on "Disclaimer" page.

Sales Breakdown by Region (Q2 FY8/15)



By region, eastern Japan sales were ¥3,430mn, up 0.3% y-o-y; central Japan sales were ¥787mn, up 1.0%; western Japan sales were ¥2,529mn, up 1.0%, and overseas sales were ¥92mn, up 31.5%. All regions achieved new record high net sales.

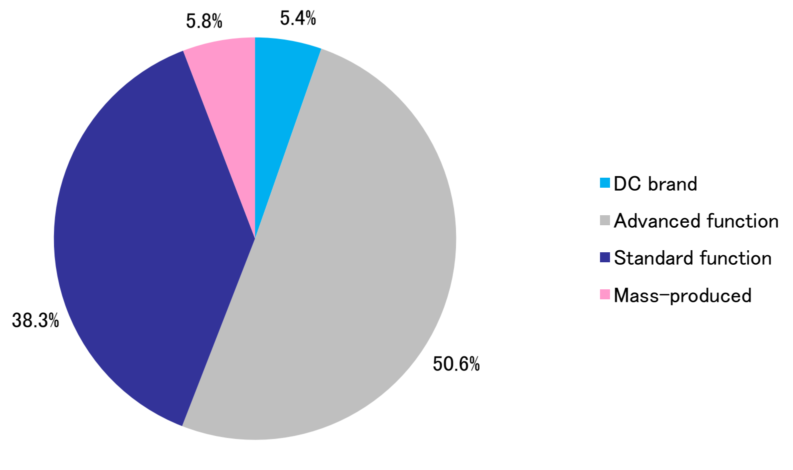
In eastern Japan, the company recovered from a delayed contract renewal in Q1 to secure sales that were almost flat y-o-y. In central Japan, where the overall regional scale is small, the size of each transaction has a significant effect; however, thanks to concentrated efforts in sales promotion, the company's sales outperformed even the dramatic increase recorded in Q2 FY8/14. In western Japan, the company made steady progress in acquiring new projects; however, the overall increase was muted by the effects of delays in renewals. Nevertheless, there are still expectations for a recovery in the second half of the year. Overseas sales expanded steadily, partly because of the yen's depreciation, however the scale is still small.

Sales Breakdown by Product

(¥mn)

	Q2 FY8/14		Q2 FY8/15	
DC brand	394	-2.9%	366	-7.2%
Advanced function	3,267	+8.6%	3,457	+5.8%
Standard function	2,712	+3.4%	2,617	-3.5%
Mass-produced	400	-5.5%	398	-0.6%
Total	6,775	+4.8%	6,840	+1.0%

Sales Breakdown by Product (Q2 FY8/15)



Looking at sales by product, DC brand product sales were ¥366mn, down 7.2% y-o-y; advanced function product sales were ¥3,457mn, up 5.8%; standard function product sales were ¥2,617mn, down 3.5%; and mass-produced product sales were ¥398mn, down 0.6%. Sales of advanced function products, which have a comparatively high profit margin, are expanding steadily.

●**Financial position**

The company's financial status has remained stable. Total assets at the end of Q2 FY8/15 amounted to ¥36,715mn, a decrease of ¥2,435mn compared to the previous year-end. Total current assets amounted to ¥27,177mn, a decrease of ¥2,412mn, primarily reflecting a decrease of ¥3,544mn in cash and deposits and an increase of ¥1,025mn in inventories. Fixed assets amounted to ¥9,537mn, a decrease of ¥23mn.

Total liabilities amounted to ¥3,800mn, a decrease of ¥668mn compared to the previous year. Its primary causes include a decrease of ¥639mn in corporate tax payable. Net assets amounted to ¥32,915mn, a decrease of ¥1,766mn compared to the previous fiscal year-end. This was mainly caused by a decrease of ¥ 452mn in retained earnings due to dividend payouts and ¥1,500mn decreased due to acquisition of treasury stock. As a result of these, the shareholders' equity ratio was 89.6%, an increasing from 88.6% at the previous year-end.

Balance Sheet

(¥mn)

	End FY8/14	End Q2 FY8/15	Change
Cash and deposits	19,054	15,510	-3,544
Notes and accounts receivable	4,696	4,710	+14
Securities	1,516	1,517	0
Inventories	3,835	4,860	+1,025
Current assets	29,589	27,177	-2,411
Buildings and other structures	2,570	2,502	-67
Land	4,480	4,480	0
Investment and other assets	1,651	1,757	+106
Fixed assets	9,560	9,537	-22
Total assets	39,150	36,715	-2,434
Bills and accounts payable	1,517	1,658	+140
Corporate tax payable	1,333	694	-639
Total liabilities	4,468	3,800	-668
Retained earnings	33,569	33,117	-451
Treasury stock	-3,402	-4,902	-1,499
Net assets	34,681	32,915	-1,766
Total liabilities and net assets	39,150	36,715	-2,434

New records for sales and operating profit projected for FY8/15

(2) FY8/15 business results forecast

FY8/15 business results forecast

(¥mn)

	FY8/14		FY8/15E			
	Amount	Sales %	Amount	Sales %	Change	y-o-y
Sales	16,214	100.0%	16,700	100.0%	+486	3.0%
Gross profit	7,585	46.8%	7,682	46.0%	+97	1.3%
SG&A costs	2,662	16.4%	2,751	16.5%	+89	3.3%
Operating profit	4,923	30.4%	4,931	29.5%	+8	0.2%
Recurring profit	5,142	31.7%	5,088	30.5%	-54	-1.1%
Net profit	3,224	19.9%	3,187	19.1%	-37	-1.1%

For the full-year business results for FY8/15, the company expects to achieve ¥16,700mn in sales, a 3% increase y-o-y; ¥4,931mn in operating profit, a 0.2% increase y-o-y; ¥5,088mn in recurring profit, a 1.1 % decrease y-o-y; and ¥3,187mn in net profit, a 1.1% decrease y-o-y. The sales forecast has not been revised from the forecast at the start of the fiscal year; however, the forecasts for operating profit and net profit have been revised downward by ¥75mn and ¥57mn, respectively, and the forecast for recurring profit has been revised upward by ¥30mn.

The increase in sales is projected based on the launch of new high-value-added products in the mainstay healthcare wear and doctor's wear sectors, and steady growth of patient wear and surgical wear. Further, the company continues to focus on raising its market share in central Japan and western Japan, and plans once again to achieve record sales and profits.

Factors affecting gross profit are expected to be increases of ¥226mn from higher sales and ¥53mn from the further expansion in the percentage of production conducted overseas (forecast to increased from 43.1% in FY8/14 to 44.4% by FY8/15 year-end) and decreases of ¥58mn due to increased material and processing costs and ¥89mn due to exchange rate effects (with the yen depreciating from an actual average rate of ¥88.1 to the US dollar in FY8/14 to a projected average rate of ¥93.3 for FY8/15). As a result, gross profit for FY8/15 is forecast to be ¥7,682mn (an increase of ¥96mn, or 1.3%, y-o-y), ¥75mn lower than the forecast at the start of the fiscal year, mainly because of the foreign exchange rate trending towards a weaker yen. As a result, the gross profit margin to forecast to be 46.0% (compared to 46.8% in FY8/14).

While there is a concern over cost increases due to the weak yen, it is unlikely that negative effect will emerge all at once since the company has entered into foreign exchange forward contracts and so forth. Even though the impact of the weak yen will gradually surface, the company plans to partially offset the cost increase by continuing to relocate production to a new plant as stated below. A number of general uniform manufacturers have already raised the prices of their products, but the company has not; therefore there is still room to improve the sales cost ratio by raising prices in the worst case scenario.

SG&A costs are forecast to be ¥2,751mn (a 3.3% increase y-o-y), reflecting an expected increase in depreciation costs of ¥35mn associated with the new company headquarters and ¥30mn for costs related to the company's 100th anniversary. The y-o-y decrease in recurring profit assumes that the foreign exchange gains (¥87mn) and the gain on securities sold (¥67mn) recorded in non-operating profit in FY8/14 will decline; however, the forecast has been revised upward by ¥30mn from the start of the fiscal year. The revision reflects the gains realized on the conversion of some of the company's U.S. dollar deposits into yen, where foreign exchange gains had not been factored into the initial forecast at all. If the yen weakens further by the end of FY8/15 compared to FY8/14, it is possible that the decline in profits will be less than anticipated. Furthermore, since the extraordinary profit that was recorded in FY8/14 (the ¥115mn profit on the sale of the old headquarters) will not occur in FY8/15, and revisions to the tax system are expected to increase the amount of corporate tax payable, the forecast for net income has been revised downward by ¥57mn from the forecast at start of the fiscal year, and is expected to decline y-o-y.

Breaking down the company's net sales forecasts by item, region, and product, in net sales forecasts by item, strong net sales are forecast for all items except for utility wear. By region, sales are expected to increase in all regions. By product, sales are expected to expand steadily mainly in advanced function products.

We encourage readers to review our complete legal statement on "Disclaimer" page.

Mid-term Management Plan and Outlook

Targets for FY8/15 to be met ahead of schedule, management announces a new Mid-Term Management Plan

(1) Mid-term Management Plan

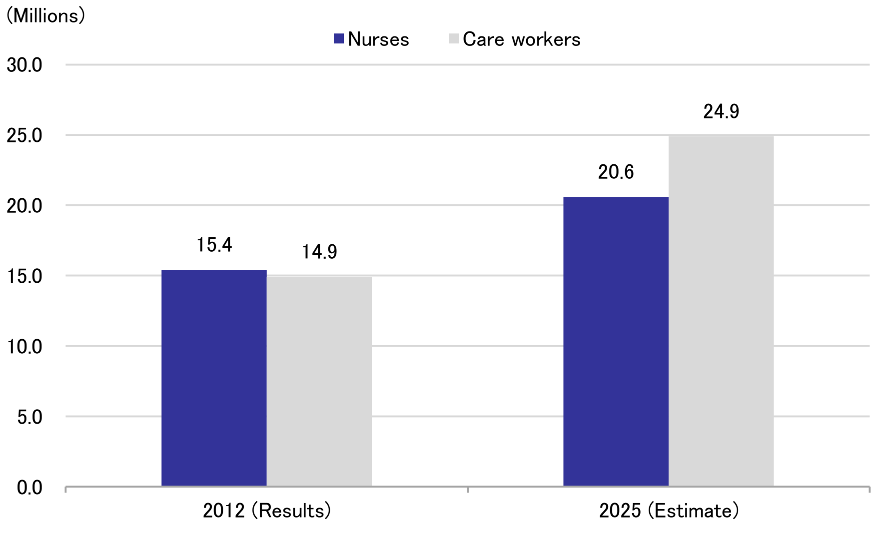
The company had set sales of ¥16,800mn and operating profit of ¥5,100mn as the targets for FY8/16 in its Mid-Term Management Plan. But given the strong possibility of it meeting these targets in FY8/15, it has released new targets for the Mid-Term Management Plan for FY8/17, with sales of ¥17,500mn and operating profit of ¥5,300mn. It plans to develop its business by implementing the policies described below, but considering its business environment, these targets can be considered fairly conservative and are very achievable.

Stable operating environment, aiming for record-high sales and operating profit

(2) Future Business Strategies

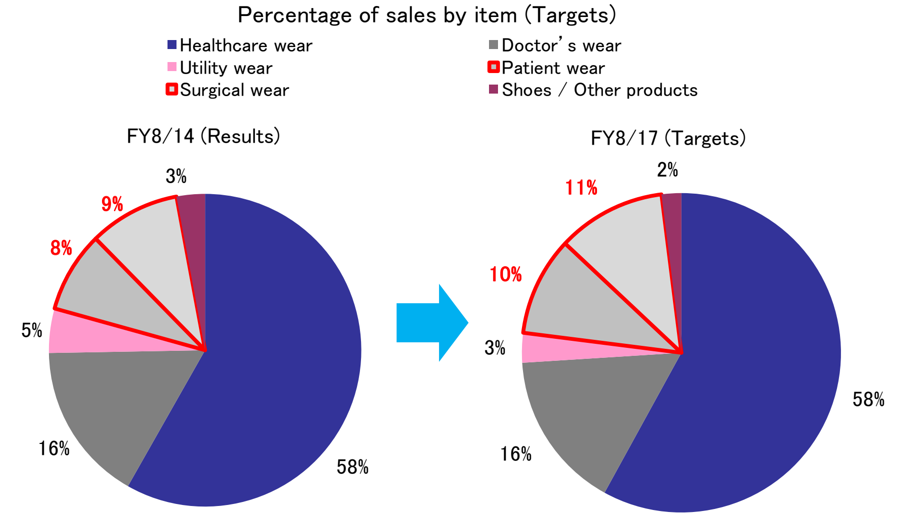
The operating environment surrounding the company should be favorable for some time. According to the material released by the Ministry of Health, Labour and Welfare, the number of nurses in Japan is projected to increase from 15.4 million in 2012 to 20.6 million in 2025. Moreover, the number of care workers is projected to increase from 14.9 million in 2012 to as many as 24.9 million in 2025. In this operating environment, the company plans to achieve its Mid-Term Management Plan based on the following strategies.

Projected demand for nurses and care workers



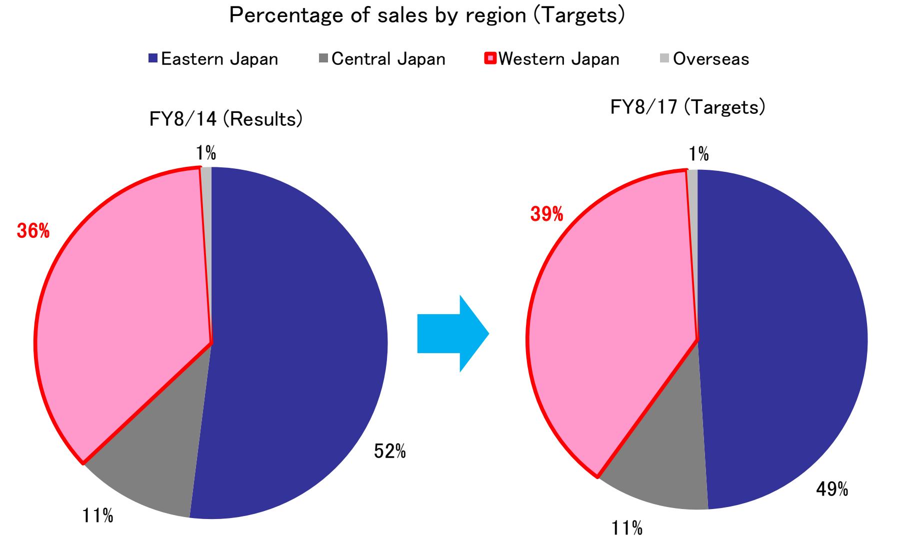
●**Expansion in patient, surgical & other peripheral market**

In its mainstay healthcare wear, the company already maintains a high market share and can expect stable renewal demand. On the other hand, the peripheral market for patient wear and surgical wear and others still has development potential. The company plans to focus on expanding the peripheral market by launching new products.



●**Increase market share in western Japan**

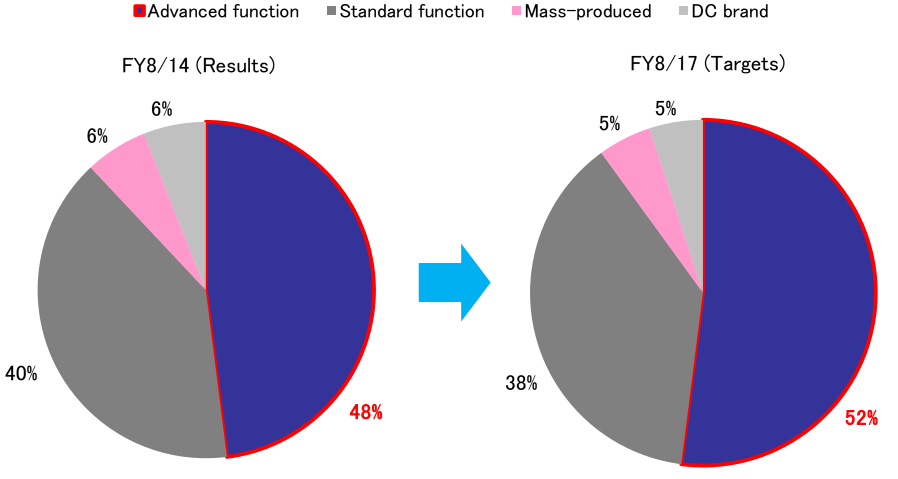
By region, the company maintains a high market share in eastern Japan, but in central Japan and western Japan, it has relatively low market shares. In other words, these regions have potential for further market share growth. To expand its market share, the company will not only conduct an aggressive sales campaign, but will actively launch advanced function products and new products.



● **Development and sales of advanced function product**

The company is actively developing products with even greater functionality and added value to deliver added value to markets where it is already strong, and to serve as tools for its marketing strategy in markets where it seeks to increase its market share. To that end, its strategy is to collaborate more closely with material manufacturers and trading companies while further refining its Quick Response (QR) production system to raise customer satisfaction.

Percentage of sales by product (Targets)



● **Improving gross profit margin**

In the last 20 years, the company's gross profit margin has improved approximately 12 percentage points (from around 35% to 47%). In the future, although improving profitability at the same pace as before will not be easy, the company aims to make further improvements mainly through the following measures.

The first is increased overseas production. Currently, the company's ratio of overseas production is still around 45.2%, which is low when compared to other apparel manufacturers. In other words, there is considerable room to further increase the overseas production ratio with potential for improving profitability from expansion of overseas production. However, the company's policy is to not shift domestic production at once to overseas, but rather to produce the portion of the increased sales at overseas while maintaining domestic production volumes. In February 2014, a new factory, which had been under construction in Java in central Indonesia, began operation, and it is expected that by the end of 2015, the transfer of existing production from Jakarta will have been completed.

The second measure to improve profitability is the development of high value-added products. If the percentage of sales of products with high profit margins increases, the overall gross profit margin will also improve. Furthermore, while there have been no official announcements, the company continues to develop new markets, and its plans for new markets (new products) should also contribute to improving gross profit margins in the future.

The yen's depreciation is also a major factor weighing down profitability. As a countermeasures to this, the company's policy is to make active use of futures contracts to level out the effects of exchange rate fluctuations, while using U.S. dollar deposits to hedge against the fluctuations as much as possible.

Shareholder Return Policy

Plan to provide steady dividends, aiming for payout ratio of 50%

The company's shareholders' equity ratio has reached 89.6% (Q2 FY8/15) and it is financially stable. Additionally, considering the company's business conditions, it seems highly unlikely that those profits will rapidly deteriorate, so continued stable earnings are expected. As a result, as its distribution of earnings outside the company (particularly dividend payments) is low and profits will accumulate in shareholders' equity each year, return on equity (ROE) will decline, which is to say, capital efficiency will decline. However, the company also actively returns profits to shareholders as detailed below, and in this way it maintains a high ROE (9.5%, FY8/14 result).

The company has demonstrated a policy of stable dividend payments and has targeted a dividend payout ratio of 50% (nonconsolidated basis), a high level compared to the majority of listed companies. Meanwhile the company has flexibly made share buy-backs. Recently it conducted a share buy-back (¥1,500 per share, purchased amount: ¥1,500mn) through a TOB. As a result, if the annual dividend of ¥50 per share is conducted as expected, together with the share buyback, distribution outside the company will total ¥3,100mn, for a total return ratio of 97.2% against the expected net profit. Looking at the company's total dividend, share buybacks, dividend payout ratio, and total return ratio from FY8/01 to FY8/14, the total dividend and dividend payout ratio have improved enormously from ¥475mn and 27.4% in FY8/01 to ¥1,712mn and 54.4% in FY8/14. This shows that the company is highly conscious of its shareholder returns and maintaining capital efficiency; and thus this should be also highly regarded.

Dividend payout ratio and total return ratio

(¥mn)

	Total dividend	Share buyback	Dividend ratio*	Total return ratio*
FY8/01	475	0	27.4%	27.4%
FY8/02	475	0	29.3%	29.3%
FY8/03	530	1,697	29.7%	124.6%
FY8/04	744	0	36.5%	36.5%
FY8/05	1,117	0	56.9%	56.9%
FY8/06	1,117	0	53.4%	53.4%
FY8/07	1,117	0	53.1%	53.1%
FY8/08	1,083	1,077	56.6%	111.2%
FY8/09	1,040	1,220	57.3%	122.2%
FY8/10	1,127	0	51.4%	51.4%
FY8/11	1,205	226	52.0%	61.7%
FY8/12	1,205	0	55.1%	55.1%
FY8/13	1,541	229	51.3%	58.7%
FY8/14	1,712	0	54.4%	54.4%

* Nonconsolidated basis

We encourage readers to review our complete legal statement on "Disclaimer" page.

FISCO

Disclaimer

FISCO Ltd. (the terms "FISCO", "we", mean FISCO Ltd.) has legal agreements with the Tokyo Stock Exchange, the Osaka Exchange,and Nikkei Inc. as to the usage of stock price and index information. The trademark and value of the "JASDAQ INDEX" are the intellectual properties of the TokyoStock Exchange, and therefore all rights to them belong to the Tokyo StockExchange.

This report is based on information that we believe to be reliable, but we do not confirm or guarantee its accuracy, timeliness,or completeness, or the value of the securities issued by companies cited in this report. Regardless of purpose,investors should decide how to use this report and take full responsibility for such use. We shall not be liable for any result of its use. We provide this report solely for the purpose of information, not to induce investment or any other action.

This report was prepared at the request of its subject company using information provided by the company in interviews, but the entire content of there port, including suppositions and conclusions, is the result of our analysis. The content of this report is based on information that was current at the time the report was produced, but this information and the content of this report are subject to change without prior notice.

All intellectual property rights to this report, including copyrights to its text and data, are held exclusively by FISCO. Any alteration or processing of the report or duplications of the report, without the express written consent of FISCO, is strictly prohibited. Any transmission, reproduction, distribution or transfer of the report or its duplications is also strictly prohibited.

The final selection of investments and determination of appropriate prices for investment transactions are decisions for the recipients of this report.

FISCO Ltd.