UT Group Co., Ltd.
2146 TSE JASDAQ

22-Aug.-16

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FISCO Ltd. Analyst
Nobumasa Morimoto

Aiming to become a leading Japanese company in the employment services industry

UT Group <2146> primarily operates a manufacturing dispatch and outsourcing services business and also dispatches design and development engineers, construction engineers, and software development outsourcing engineers. Its major customer industries for manufacturing dispatch and outsourcing services are semiconductors and electronic devices, environment and energy, and automotive, and UT Group is the industry leader in manufacturing dispatch and outsourcing service employee volume for the semiconductor industry, which generates half of its sales in this area, with Panasonic <6752>, Sony <6758>, and ROHM <6963> group as key customers. UT Group has been an industry pioneer in hiring for full-time employment, ability-based wages, and other practices and possesses the industry's top retention rate. It has steadily expanded with a unique business model of "outsourcing entire processes (start-to-finish)" that differentiate it from other firms. It acquired UT System Co., Ltd. (formerly, System Revolution Co., Ltd.) in March 2015 with the aim of expanding its engineer dispatching business.

In its financial results for FY3/16, UT Group achieved double-digit increases in sales and profits, with sales up 20.8% YoY to ¥44,050mn, operating profit up 10.3% to ¥2,462mn, and net profit attributable to owners of parent up 28.2% to ¥1,497mn. It recorded higher sales and profits for a sixth straight fiscal year. It provided services to 456 plants (up 18 plants YoY) and dispatched an all-time high of 10,926 technical employees (including 10,022 technicians dispatched for manufacturing and 904 engineers) as of end-FY3/16. UT Group steadily expanded the manufacturing dispatch and outsourcing services business, thanks to solidification of operations for hiring 500 people per month, selective orders acceptance, and other initiatives, and grew the engineer dispatch business at a healthy pace with support from advances at existing subsidiaries and the acquisition of UT System.

UT Group aims for single-digit sales and profit increases in FY3/17, with sales up 8.6% YoY to ¥47,840mn, operating profit up 2.8% to ¥2,530mn, and net profit attributable to owners of parent up 8.2% to ¥1,620mn. This outlook factors in the impact of a rise in idle employees related to the Kumamoto Earthquakes that struck in April (¥200mn setbacks for sales and operating profit as of May). We think guidance that factors in the impact of the Kumamoto Earthquakes is conservative because 1) the earthquake impact is temporary and not a reason for concern, 2) the revised worker dispatch law that took effect in September 2015 is serving as a positive factor for UT Group, 3) demand in core customer industries, such as new vehicles and next-generation smartphones, is vibrant, and 4) UT Group is selectively accepting orders for high-priced, high-margin projects.

The new Medium-Term Business Plan announced in July 2015 (covering FY3/17-21) presents a new vision of "creating jobs nationwide in Japan" as a second "founding phase" in line with a group mission of "creating vigorous workplaces empowering workers," along with goals of 29,000 employees, ¥10,000mn in EBITDA, ¥145,000mn in sales, and ¥8,200mn in operating profit in FY3/21. UT Group aims to become a leading company in Japan's employment service industry. It updated management indicators this time based on conducting aggressive M&A with commitments to an EBITDA growth rate of at least 30% (average growth rate for the five-year plan), a gross D/E ratio* of 1.0 or less (by FY3/21), and a total return ratio of at least 30%.

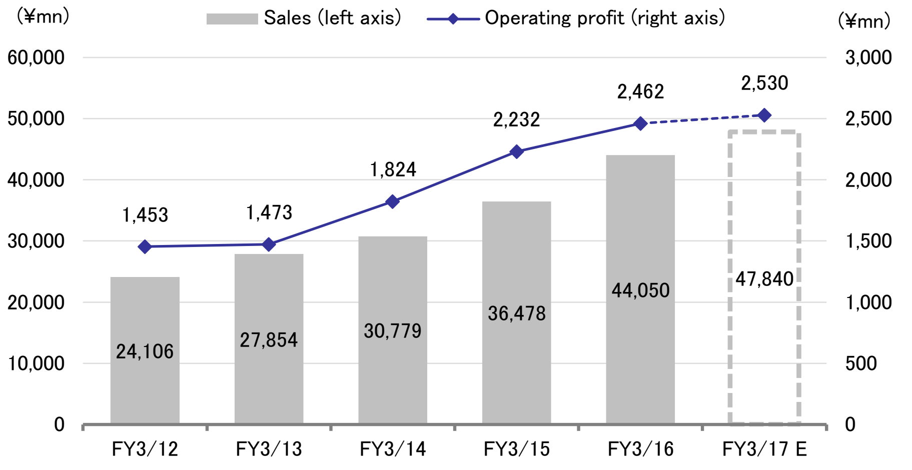
* Indicates the ratio of liabilities to capital as the source of corporate capital. Financial standing is typically healthy when this value is one or less.

For shareholder returns, UT Group has committed to a total return ratio of at least 30% and uses of the PEG ratio value for decisions as its basic policy. It decided to buy up to 2mn shares of its own stock with a budget of ¥750mn in FY3/17 (during May 13, 2016 to March 12, 2017) and already completed the purchases. It also plans to retire all of the purchased shares. UT Group intends to implement profit allocation in FY3/17 with a total return ratio of at least 30% based on a combination of dividends and share buybacks taking into account earnings and stock market trends, in line with the revised commitment in the new Medium-Term Business Plan.

Check Point

- Reported higher sales and profits for a sixth straight year in FY3/16
- Guides for single-digit sales and profit increases in FY3/17 factoring in the impact of the Kumamoto Earthquakes
- Changed the core policy for shareholder returns from a total return ratio of “at least 50%” to “at least 30%” due to plans for aggressive M&A

Business Trends



Business Overview

Mainly operates a manufacturing dispatch and outsourcing services business and also dispatches engineers

(1) Group companies

The group consists of the UT Group Co., Ltd., which functions as the pure holding company for the other group companies, and six consolidated subsidiaries.

List of Group Companies

Company name	Founded	Address	Description of business
UT Aim Co., Ltd.	April 1995	Shinagawa Ward, Tokyo	Manufacturing dispatch and outsourcing
UT Pabec Co., Ltd.	July 2013	Shinagawa Ward, Tokyo	Battery product processing and assembly, packaging, and manufacturing dispatch and outsourcing
UT Technology Co., Ltd. (formerly, UT Leading Co., Ltd.)	September 2005	Shinagawa Ward, Tokyo	Design and development engineer dispatch
UT Construction Co., Ltd. (formerly: UT Construction Network Co., Ltd.)	April 2012	Shinagawa Ward, Tokyo	Construction engineer dispatch
UT System Co., Ltd. (formerly, System Revolution Co., Ltd.)	August 1986	Shinagawa Ward, Tokyo	Software development and operational management Specified worker dispatch business
UT Heartful Co., Ltd.	September 2008	Shinagawa Ward, Tokyo	Special subsidiary (office service, design and printing business, etc.)

Source: FISCO Ltd. from company materials

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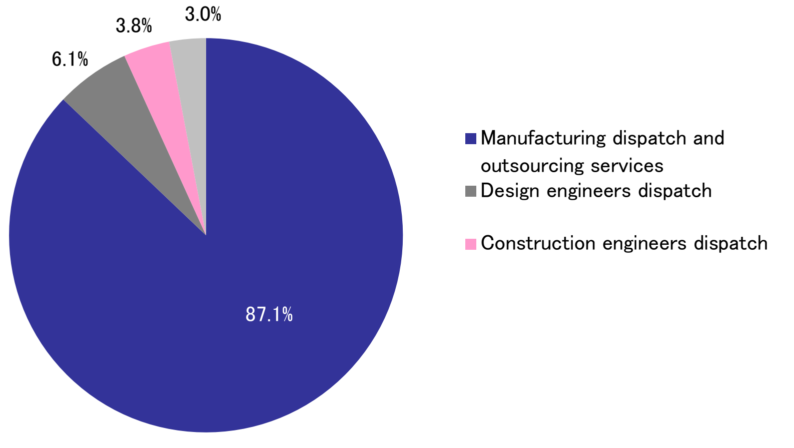
(2) Business content

The two main businesses it is engaged in are the manufacturing dispatch and outsourcing services business and the engineer business, but in terms of financial accounting, it discloses information on one business, the outsourcing business. In FY3/16, percentages of total sales by business (percentage of profit per business prior to internal elimination) were 87.1% from the manufacturing dispatch and outsourcing services business (90.9%) and 12.9% from the engineer business (9.1%). The engineer business breaks down into design engineers (6.1% of total sales), construction engineers (3.8%), and software development engineers (3.0%).

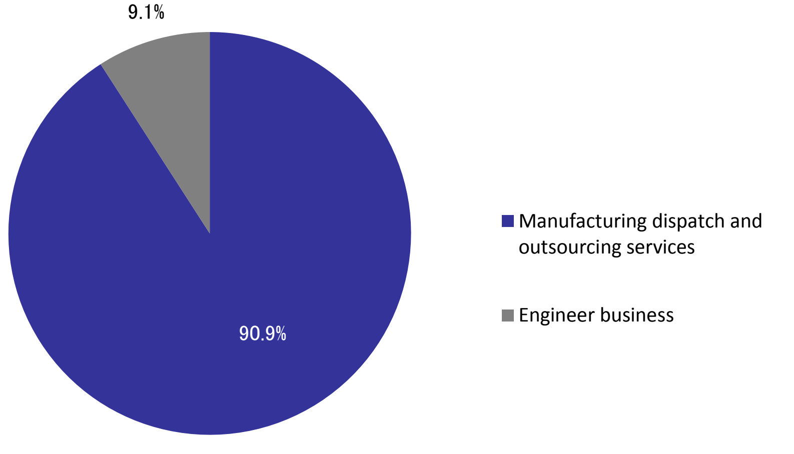
Sales Percentages by Business and Profit Composition (FY3/16)

Sales Percentages by Business (FY3/16)



Source: FISCO Ltd. from results briefing materials

Profit Composition (FY3/16)



Source: FISCO Ltd. from results briefing materials

a) Manufacturing dispatch and outsourcing services business

It dispatches permanent employees and handles outsourcing of in-plant work mainly for Japanese manufacturers. Rather than dispatching individuals for work outsourced to it, UT Group mainly organizes experienced employees into teams, establishes a chain of command, and carries out the work on the unit of an entire process (start-to-finish outsourcing). The group's employees that carry out the outsourcing work are called technicians and their employment formats are divided into permanent employees transferred to locations nationwide (approximately 70% of all employees) and contract employees.

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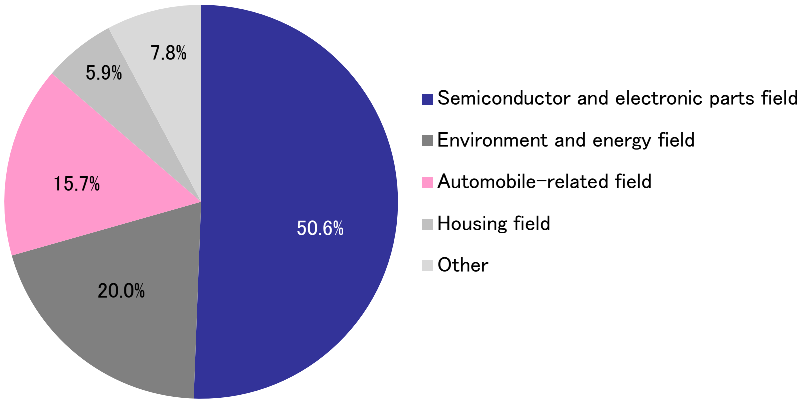
Its main users are manufacturing companies in industries including semiconductor, electronics, environment and energy, automotive, and construction and building materials. Specifically, its main clients include the Sony Group, the Panasonic Group, and the Toshiba <6502> Group. Consolidated subsidiaries UT Aim and UT Pabec carry out this business. As of the end of March 2016, it dispatched technicians to 456 plants (vs. 438 plants at end-FY3/15) and employed 10,022 technicians (vs. 8,597 technicians). Percentages of sales by customer industry were semiconductors and electronic devices at 50.6%, environment and energy at 20.0%, automotive at 15.7%, housing at 5.9%, and others at 7.8%.

Percentage of Sales by Client Business Category (Manufacturing Only)
(FY3/16)



Source: FISCO Ltd. from results briefing materials

b) Engineer business
The business involves software outsourced development; machinery, electrical, and electronic design development (including design work using 3D CAD); and the dispatch of construction engineers. Software development is carried out by UT Technology Co., Ltd. and UT System, while the dispatch of engineers for machinery, electrical, and electronic design development is handled by UT Technology. The construction engineer dispatch business is carried out by UT Construction Co., Ltd. Main clients for software development and dispatch of engineers for machinery, electrical, and electronic design development are major electronics manufacturers. Clients in the construction engineer dispatch business include major construction companies, primarily super general contractors. As of the end of March 2016, the group employed 904 engineers in this business (vs. 702 at the end of FY3/15).

■ Financial Results Trends

Reported higher sales and profits for a sixth straight year, surpassed 10,000 technical employees for the first time

(1) FY3/16 consolidated results

In its financial results for FY3/16, UT Group achieved double-digit increases in sales and profits, with sales up 20.8% YoY to ¥44,050mn, operating profit up 10.3% to ¥2,462mn, and net profit attributable to owners of parent up 28.2% to ¥1,497mn. It recorded higher sales and profits for a sixth straight fiscal year. It provided services to 456 plants (up 18 plants YoY) and dispatched an all-time high of 10,926 technical employees (including 10,022 people dispatched for manufacturing and 904 engineers) as of end-FY3/16.

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FY3/16 Results Review

(unit: ¥mn)

	FY3/15		FY3/16				
	Results	Ratio (to sales)	Period-start plan	Results	Ratio (to sales)	Change versus the plan (%)	Change YoY (%)
Sales	36,478	-	40,000	44,050	-	10.1%	20.8%
Cost of sales	29,718	81.5%	32,440	35,303	80.1%	8.8%	18.8%
Gross profit	6,760	18.5%	7,560	8,747	19.9%	15.7%	29.4%
SG&A expenses	4,528	12.4%	5,160	6,284	14.3%	21.8%	38.8%
Operating profit	2,232	6.1%	2,400	2,462	5.6%	2.6%	10.3%
Ordinary profit	2,157	5.9%	2,240	2,421	5.5%	8.1%	12.3%
Net profit attributable to owners of parent	1,168	3.2%	1,320	1,497	3.4%	13.4%	28.2%

Source: FISCO Ltd. from the results statement

Key sales drivers were 1) upbeat expansion of manufacturing dispatch and outsourcing services business thanks to a steady rise in technician employee volume through establishment of a hiring program for 500 people per month and higher contracted plant volume and 2) strong growth in engineering business at over 70% led by growth at existing subsidiaries and the addition of UT System acquired as a subsidiary. Gross profit accompanying higher sales climbed 29.4% YoY to ¥8,747mn, and gross margin improved by 1.4ppt from FY3/15's 18.5% to 19.9%. Margin improvement reflected the benefits of selective acceptance of high-margin orders in the manufacturing dispatch and outsourcing services business and a larger sales ratio for the lucrative engineer business. SG&A expenses, meanwhile, increased sharply with a 38.8% rise to ¥6,284mn, mainly due to a steep expansion of hiring costs from aggressive hiring activity that factored in large back-order volume for FY3/17 and additions to employees with financial expertise to prepare for ramp-up of M&A activities. UT Group hence posted a double-digit rise in operating profit, but operating margin slipped by 0.5ppt from 6.1% to 5.6%.

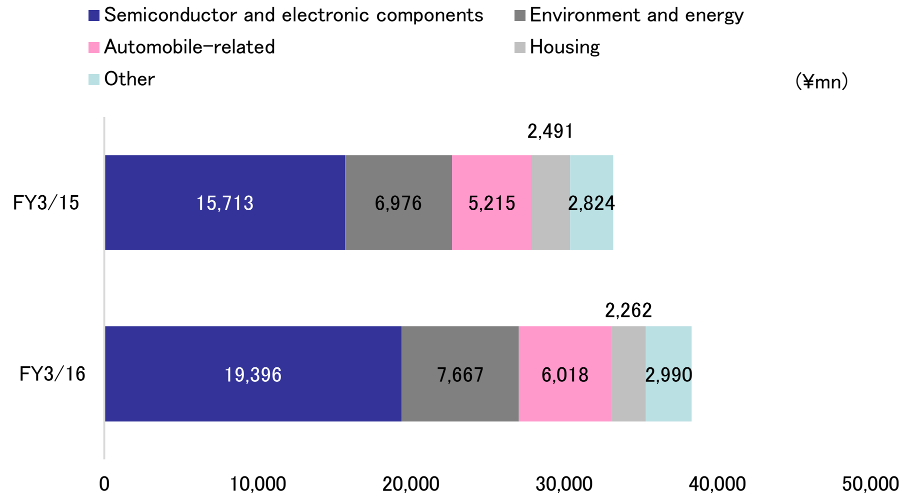
Sales and profits beat guidance (¥40,000mn in sales, ¥2,400mn in operating profit, and ¥1,320mn in net profit attributable to owners of parent). We think primary upside drivers were healthier gains in electronic devices and automotive businesses and increased share at existing customers as well as steady progress with new customer acquisition and successful boosts in contract pricing for the manufacturing dispatch and outsourcing services business. Large upside in net profit attributable to owners of parent stemmed from a smaller value under corporate taxes and other adjustments owing to a decline in carryover losses and reduced tax rate.

We review conditions for the business segments.

a) Manufacturing dispatch and outsourcing services business

This business posted double-digit increases in sales and operating profit with gains of 15.4% YoY to ¥38,333mn and 23.4% to ¥4,166mn respectively. Technical employees surpassed the 10,000-person level for the first time at 10,022 people at period-end with support from establishment of a program for hiring 500 people per month and rising demand mainly in electronic devices and automotive industries. Viewed by customer industry, sales rose at robust pace in the three main areas of semiconductors and electronic devices, environment and energy, and automotive. Segment profit margin climbed from 10.2% to 10.9% owing to selective acceptance of higher-margin deals and results from sales activities aimed at raising in-house share.

Sales Trend by Client Business Category

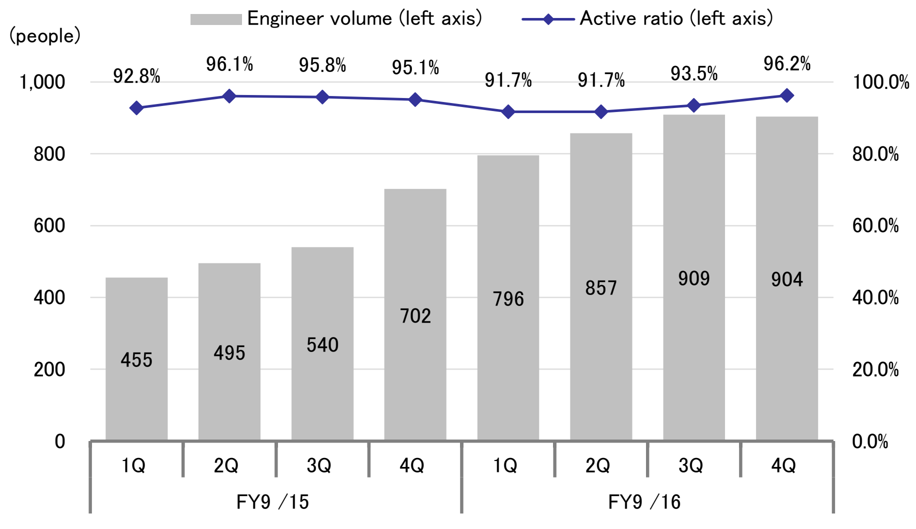


b) Engineer business

This business reported double-digit increases in sales and operating profit with gains of 78.7% YoY to ¥5,699mn and 61.4% to ¥418mn respectively. Key drivers were upbeat expansion at existing subsidiaries, such as UT Technology and UT Construction, amid strong demand and a full-year contribution from UT System added as a subsidiary in March 2015. The number of engineer employees for the engineer business expanded by 202 people from the end of the previous fiscal year to 904 people, including a boost from One UT* (career change within the group; added 130 people).

* Unique program in which the UT Group works jointly to support employee career advances and new challenges. Anybody can enter the program regardless of age or work experience. Participants learn specialty knowledge and skills while working. There are currently two courses running – Construction Engineer and Design and Development Engineer.

Engineer Volume and Active Ratio Trends for the Engineer Business (Quarterly Basis)



Source: FISCO Ltd. from results briefing materials

Moderate upward trend in the shareholders' equity ratio

(2) Financial conditions

As of the end of March 2016, total assets had increased ¥712mn from the end of the previous fiscal period to ¥17,139mn. Breaking this down, current assets increased ¥669mn from the end of the previous fiscal period, despite a decline in cash & deposits (¥689mn), thanks to a rise in accounts receivable (¥1,250mn). Fixed assets increased ¥49mn from the end of the previous fiscal period, even with a decline in investments and other assets (¥225mn) due to lower deferred tax assets, thanks to increases in tangible fixed assets (¥84mn) and intangible fixed assets (¥190mn) related to headquarter renovations and other factors.

Liabilities increased ¥88mn from the end of the previous fiscal period to ¥12,891mn. While corporate bonds fell ¥420mn, loans (short-term and long-term loans) climbed ¥631mn. Net assets rose ¥623mn from the end of the previous fiscal period to ¥4,248mn. This was mainly due to retirement of treasury shares and the increase in retained earnings of ¥497mn from booking net profit attributable to owners of parent.

Next, we review cash flow trends. Cash and cash equivalents fell ¥606mn from the end of the previous fiscal period to ¥6,511mn at end-FY3/16. Operating cash flow had a surplus of ¥517mn, despite booking ¥876mn in corporate tax and other payments and a ¥1,250mn rise in accounts receivable value, thanks to booking ¥2,353mn in net profit prior to taxes and other adjustments. Investment cash flow posted a deficit of ¥334mn due to ¥153mn in outlays for acquisition of tangible fixed assets and ¥223mn in spending from acquiring intangible fixed assets. Financing cash flow had a deficit of ¥789mn, even with ¥2,990mn in income from long-term loans, due to ¥1,622mn in spending to repay long-term loans, a ¥736mn net decline in short-term loans, ¥999mn in outlays to acquire treasury shares, and ¥420mn in outlays to repay corporate bonds.

Indicators of financial health modestly improved because of changes in balance-sheet composition accompanying stronger earnings. Operating margin, which reflects profitability, meanwhile, weakened from the previous year due to a steep rise in hiring costs in order to handle back orders in FY3/17. Yet we do not see a problem because the source of the decline is temporary.

Balance Sheet, Cash Flow Statement, and Business Indicators

Balance Sheet (unit: ¥mn)

	FY3/15	FY3/16	Change	Breakdown
Current assets	13,194	13,863	669	Sales receivable +1,250, cash and deposits -689
Fixed assets	3,213	3,262	49	Tangible fixed assets +84, intangible fixed assets +190, Investments and other assets -225
Total assets	16,427	17,139	712	
Current liabilities	8,285	7,835	-450	Long-term loans slated for repayment within a year +355. Short-term borrowings -736
Fixed liabilities	4,517	5,056	538	Long-term debt +1,011, corporate bonds -410
Total liabilities	12,803	12,891	88	
(Balance of interest-bearing debt)	6,856	7,049	193	Loans +631, corporate bonds -420
(Net cash)	817	-84	-901	
Net assets	3,624	4,248	623	Surplus profit (+497)
Total liabilities and net assets	16,427	17,139	712	

Cash Flow Statement

Operating CF	3,131	517	
Investment CF	-679	-334	
Financing CF	515	-789	
Balance of cash and cash equivalents	7,117	6,511	-606

Business Indicators

Soundness		
Liquidity ratio	159.3%	176.9%
Shareholders' equity ratio	21.4%	23.9%
D/E ratio	1.95	1.72
<Profitability>		
ROE	35.3%	39.3%
ROA	15.1%	14.4%
Operating margin	6.1%	5.6%

Source: FISCO Ltd. from results statements

Conservative guidance factoring in the impact of the Kumamoto Earthquakes

(3) FY3/17 outlook

UT Group aims for single-digit sales and profit increases in FY3/17, with sales up 8.6% YoY to ¥47,840mn, operating profit up 2.8% to ¥2,530mn, and net profit attributable to owners of parent up 8.2% to ¥1,620mn.

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Overview of FY3/17 Guidance

(unit: ¥mn)

	FY3/16		FY3/17					
	Results	Ratio (to sales)	Period-start guidance	Ratio (to sales)	Change YoY (%)	Prior to the impact of the Kumamoto Earthquakes	Ratio (to sales)	Change YoY (%)
Sales	44,050	-	47,840	-	8.6%	48,040	-	9.1%
Cost of sales	35,303	80.1%	38,660	80.8%	9.5%	38,860	80.9%	10.1%
Gross profit	8,747	19.9%	9,180	19.2%	5.0%	9,380	19.5%	7.2%
SG&A expenses	6,284	14.3%	6,650	13.9%	5.8%	6,850	4.3%	9.0%
Operating profit	2,462	5.6%	2,530	5.3%	2.8%	2,730	5.7%	10.9%
Ordinary profits	2,421	5.5%	2,430	5.1%	0.4%			
Net profit attributable to owners of parent	1,497	3.4%	1,620	3.4%	8.2%			

Source: FISCO Ltd from company materials

This outlook for just single-digit gains primarily stems from factoring in the impact of a rise in idle employees related to the Kumamoto Earthquakes that struck in April (¥200mn setbacks for sales and operating profit as of May). However, UT Group aims to separately build a framework that can support stable hiring of 750 people per month, based on current operations with hiring at 500 people per month, and toward a goal of over 12,000 employees at the period-end in order to promote diversification of customer industries and stabilization of the income foundation. While it targets a 5.0% YoY rise in gross profit to ¥9,180mn, the gross margin guidance indicates a 0.7ppt decline from FY3/15's 19.9% to 19.2% because of factoring in the impact of the Kumamoto Earthquakes and other trends. Yet UT Group also hopes to suitably control SG&A expenses by raising hiring efficiency and keeping hiring costs within 3% of sales and thereby reduce the SG&A expenses ratio from FY3/16's 14.3% to 13.9%. It projects just a single-digit increase in operating profit and a 0.3ppt decline in operating margin to 5.3% based on these trends.

UT Group commented in early May regarding the impact of the Kumamoto Earthquakes that “While damage occurred at 20 plants of customer companies in the Kyushu area, many plant buildings and facilities were unaffected thanks to BCP measures and other activities and a majority of plants restored operations after the Golden Week holidays. However, some plants (mainly semiconductor sites) are behind schedule in resuming output.” Although UT Group temporarily shifted employees working at plants that suspended output to other plants and implemented recovery measures such as replacement and holiday operations to cover the portion missed during customer plant suspensions, it factored in impacts of ¥200mn each on sales and operating profit based on idling of 400 employees for two months. Subsequent shifts to plants in western Japan, particularly Kyushu, appear to have kept the earthquake impact at a very temporary level and removed concerns.

Below we review strategies and initiatives by business segments.

a) Manufacturing dispatch and outsourcing services business

UT Group hopes to establish operations with 11,000 technical employees by the end of FY3/17. Revenue and sales measures in this effort will involve continued expansion of in-house shares at existing customers and new sales activities targeting deals with appropriate contract terms at new customers. UT Group plans to build a hiring framework for stable addition of 750 people per month. It aims to raise the retention rate by setting up a format that allows for salary increases through enhanced education and training and skill improvement and strengthening the career formation assistance structure.

b) Engineer business

UT Group seeks to achieve at least 20% YoY growth in the engineer business as it cultivates a second business pillar. In this effort, it plans to build hiring infrastructure and expand mid-career hiring activities and offer positions to new graduates throughout the year. It also hopes to raise sales by lifting the matching rate and average utilization rate through enhanced sales measures that increase new quality customers. It intends to make introductions to client companies from the manufacturing dispatch and outsourcing services business too through collaboration with the latter. It is providing employees with education and training menus, such as the Siemens TPP Program*, and striving to cultivate efficient engineers and boost salaries through the One-UT Project.

We think guidance that factors in the impact of the Kumamoto Earthquakes is conservative because 1) the earthquake impact is temporary and not a reason for concern, 2) the revised worker dispatching law that took effect in September 2015 is serving as a positive factor for UT Group, 3) demand in core customer industries, such as new vehicles and next-generation smartphones, is vibrant, and 4) UT Group is selectively accepting orders for high-priced, high-margin projects.

* Concluded a Training Partner Program contract with Siemens K.K., the local entity of US-based Siemens PLM Software aimed at training and provision of talented PM (product lifecycle management) personnel and promotion of education program to improve careers.

Medium-Term Business Plan

Aims to expand into a leading company in Japan's employment service industry by FY3/21

UT Group completed the five-year Medium-Term Business Plan lasting through FY3/16 and has entered the new Medium-Term Business Plan period covering the five years from FY3/17 to FY3/21 announced in July 2015. The plan presents a new vision of "creating jobs nationwide in Japan" as a second "founding phase" in line with a group mission of "creating vigorous workplaces empowering workers," along with goals of 29,000 employees, ¥145,000mn in sales, ¥10,000mn in EBITDA, and ¥8,200mn in operating profit in FY3/21. UT Group aims to become a leading company in Japan's employment service industry.

While UT Group had committed to "an EPS growth rate of at least 30%" and "total return ratio of at least 50%" in the existing Medium-Term Business Plan, it revised indicators this time based on conducting aggressive M&A to commitments of an EBITDA growth rate of at least 30% (average growth rate for the five-year plan), a gross D/E ratio* of 1.0 or less (by FY3/21), and a total return ratio of at least 30%. To achieve these goals, it formulated specific policies and strategies aimed at its two main clienteles - dispatched workers/employees and user companies.

(1) Policy and strategy for employees and job applicants

UT Group implements a strategy based on themes of reliability, bonding, and empowerment for employees and job applicants. It offers "reliability" by raising its share at customer sites and thereby giving employees a secure job environment. It supports "bonding" by seeking to raise the retention rate with extensive career counseling and other measures and providing work that enables employees to feel connected with peers, the company, and local society via their jobs. It facilitates "empowerment" by supplying an environment that lets employees feel growth through work with a target of lifting the average annual salary by 20% within five years via provision of education and training programs and opportunities.

(2) Policy and strategy for customer companies

UT Group carries out a strategy for themes of matching, risk management, and assistance in human resource strategy formulation. As "matching," it proposes utilization of human resources that delivers volume, quality, and speed to customer companies by strengthening responsiveness to change and sales capabilities. For "risk management," it complies with the worker dispatch law, Labor Contract Act, and other worker-related laws and reduces risk related to amended laws. UT Group also strives to lower labor management risk and reputation risk at customer companies by ensuring compliance. For "human resource strategy formulation assistance," it is expanding tools, holding seminars, consulting on use of non-regular labor resources, giving proposals for utilization of foreign workers, and broadening the service menu in other ways to discover and resolve issues in human resource utilization at customer sites.

Shareholder Returns

Changed the commitment for the total return ratio to 30% or more from FY3/17

For shareholder returns, UT Group has committed to a total return ratio (the sum of dividends paid and share buybacks as a ratio of consolidated net income; ratio of shareholder returns to net profit) of at least 30% and use of the PEG ratio* value for decisions regarding shareholder returns as its basic policy.

* Price Earnings Growth Ratio = PER ÷ annual EPS growth rate

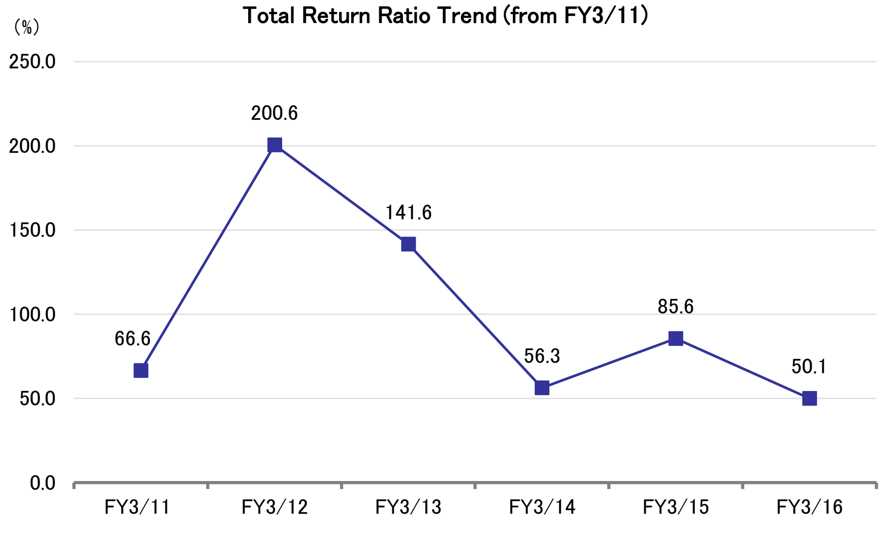
UT Group comprehensively reaches conclusions on shareholder returns policy in line with the following basic policy stance and also striking balance with investments.

(1) PEG ratio less than 1x: Undervalued

Management comprehensively considers dividends and share buybacks in this phase. For example, it is implementing share buybacks this fiscal year with shares trading at about 1x, which is considered inexpensive.

(2) PEG ratio above 2: Management deems that investors are sufficiently assessing the shares at this level and fundamentally relies on dividends.

Given this policy, it decided to buy up to 2mn shares of its own stock (5.43% of outstanding shares excluding treasury shares) with a budget of ¥750mn in FY3/17 (during May 13, 2016 to March 12, 2017) and already completed the purchases. It plans to retire all of the purchased shares as part of its shareholder return policy. UT Group intends to implement profit allocation in FY3/17 with a total return ratio of at least 30% based on a combination of dividends and share buybacks, taking into account earnings and stock market trends, in line with the revised commitment in the new Medium-Term Business Plan.



Source: FISCO Ltd. from company materials

■ Corporate Overview and History

After the financial crisis (Lehman Shock), it decided to return to dispatching technicians in the manufacturing industry

(1) Corporate overview

With a group mission of “creating vigorous workplaces empowering workers,” UT Group primarily operates a manufacturing dispatch and outsourcing service business with full-time employees for in-house work, mainly in domestic and semiconductors and electronic devices, environment and energy, and automotive industries, and also dispatches engineers. It is the industry leader in manufacturing dispatch and outsourcing service employee volume for the mainstay semiconductor industry with Panasonic, Sony, and other key customers. The engineer business dispatches engineers mainly to domestic customers for software outsourced development and machinery, electric equipment, and electronics design and development. UT Group has been an industry pioneer in hiring for full-time employment, ability-based wages, and other practices and possesses the industry’s top retention rate. It has steadily expanded with a unique business model of “outsourcing entire processes (start-to-finish)” that differentiates it from other firms.

(2) History

The group was founded in April 1995 based on the philosophy of President, Representative Director & CEO Yoichi Wakayama of contributing to both people looking for a job and companies wanting people. The group's corporate history can be categorized into three periods: a) its founding period up to 2001, b) its first growth period up to 2009, in which it adopted a niche strategy of specializing in the semiconductor field, and c) its second growth period from 2010, in which it returned to the manufacturing outsourcing industry in order to escape from its reliance on semiconductors by converting to a market leader strategy.

a) The founding period (1995 to 2001)

The origins of the group were the founding in April 1995 in Yokohama of Aim CIC Company for the business of contractual on-site work. In July 1996, Aim CIC was renamed Nihon Aim Co., Ltd. Since its founding, it has focused on the manufacturing field, and one after another it adopted employment systems that ran contrary to the prevailing wisdom in the industry at that time, such as permanent employment, 100% employee participation in social insurance and a skill-based wage system. In such ways, it was successfully able to increase its employee retention rate and production efficiency. Furthermore, it created an independent business model in which instead of dispatching individuals, it dispatches entire teams to provide its start-to-finish outsourced production service in which the team is responsible for an entire process, and implemented various reforms of employees' ways of working. These initiatives helped to improve the management efficiency at its corporate clients, which further increased client numbers, and established the business foundations for its first growth stage.

b) First growth stage (2001 to 2009)

Due to the collapse of the IT bubble, the performance of companies in the manufacturing industry, which are the group's clients, deteriorated, and so inevitably the group's results also worsened. In this situation, it decided to convert to a niche, growth strategy of specializing in the semiconductor field which requires high-level expertise and is appropriate for outsourcing work on the unit of an entire process. In October 2002, it established the Semiconductor Market Development Team (currently the Tsukuba Training Center), which promotes the start-to-finish outsourced production service for semiconductor device manufacturers and carries out planning to improve the abilities of functional employees specializing in the semiconductor business. These efforts bore fruit and up to 2007 prior to the Lehman Brothers' collapse, it had established its position as No.1 in the manufacturing outsourcing industry in terms of number of manufacturing outsourced and dispatched employees to the semiconductor-related industry. In April 2006, in order to advance into the semiconductor device design business, it made a subsidiary of ARTISTA Co., Ltd. (merged with Comm Leading Co., Ltd. in December 2011), thereby entering into the design and development engineers dispatch business.

Further, in April 2007 it established a joint holding company called United Technology Holdings Co., Ltd. (name changed to UT Holdings Co., Ltd. in January 2009; changed to UT Group in July 2015) with Apex Inc., which sells used semiconductor manufacturing equipment and provides technical services. Next, in June 2007, Nihon Aim Co., Ltd. (name changed to UT Aim Co., Ltd in July 2012) made a subsidiary of Micro Engineering Inc., which manufactures and sells semiconductor manufacturing equipment, thereby entering into the business of manufacturing and selling semiconductor equipment and accelerating its strategy of expanding the scope of its semiconductor business.

However, it had to abandon its expansion of its semiconductor business due to the deterioration of the performance of companies in the semiconductor industry following the worldwide recession triggered by the Lehman Brothers' collapse. In June 2009, it sold Micro Engineering and then in November it sold Apex, and decided to return to the engineer business in the manufacturing field, which had been its business domain since its founding.

In December 2003, the group's predecessor Nihon Aim listed on the over-the-counter market, with one of its objectives being "to create a company that could have its employees as the top shareholder." Incidentally, this was the first IPO of an outsourcing company, and its formation of an employee shareholder plan was also a first for its industry.

c) Second growth stage (2010 to the present)

From the group's decision to return to its original business of manufacturing outsourcing, in addition to cultivating further transactions in its main manufacturing dispatch and outsourcing services business and expanding into client growth fields, such as the environment and energy field, the automobile-related field, and the housing field, it aimed to develop its business foundations by expanding its engineer business (dispatch of design and construction engineers). In this way, it implemented a market leader strategy of escaping from a reliance on semiconductors and becoming the No.1 outsourcing company, at the same time as implementing financial restructuring. Even though its business environment was working against it, such as the shift of the manufacturing industry overseas due to the Great East Japan Earthquake and the strong yen, the 2012 problem*1 worked to the advantage of the group thanks to its policy of permanent employment, and its number of client plants increased, its results recovered, and its expansion trend accelerated.

In order to expand its business foundations, in January 2010 the group established Comm Leading Co., Ltd. (design and development engineers dispatch business)*2, and then in March it established Comm Agent Co., Ltd. (distribution and retail dispatch business)*3. In addition, in July 2013, it acquired 81% of the shares of Panasonic Battery Engineering Co., Ltd. and made it into a subsidiary (at the same time, its name was changed to UT Pabec Co., Ltd.). Further, in March 2015, with the objective of expanding its engineer business even further, it made a subsidiary of System Revolution, which operates a software development business*4. Management positioned 2015, the 20th anniversary of the company's founding, as a new founding year and presented a new vision of "creating jobs nationwide in Japan" in July 2015. It also renamed itself from UT Holdings to UT Group and updated the brand mark*5.

Company History

April 1995	Aim CIC Company was founded for the business of dispatching personnel for in-plant work
July 1996	Aim CIC was renamed Nihon Aim Co., Ltd.
October 2002	The Semiconductor Market Development Team was established (currently the Tsukuba Training Center)
December 2003	Nihon Aim was listed on the over-the-counter market (JASDAQ)
April 2006	ARTISTA Co., Ltd. was made a subsidiary in order to enter into the design and development engineer dispatch business
April 2007	Nihon Aim and Apex Inc. jointly transferred shares to establish United Technology Holdings Co., Ltd. (currently UT Group Co., Ltd.) as a pure shareholding company. It was listed in the JASDAQ market (Nihon Aim became unlisted)
January 2009	United Technology Holdings was renamed UT Holdings Co., Ltd.
November 2009	All shares of Apex were acquired by HACHITOKU Co., Ltd.
January 2010	Comm Leading Co., Ltd. was established in order to strengthen the group's design and development engineers dispatch business
March 2010	Comm Agent Co., Ltd. was established in order to enter into the distribution and retail dispatch business
January 2011	ARTISTA and Comm Leading were combined to form Comm Leading
April 2012	The name of Comm Agent Co., Ltd. was changed to UT icom Co., Ltd. and a manufacturing dispatch and outsourcing business was launched. UT Career Co., Ltd. was established (entered into the outplacement business). UT Construction Network Co., Ltd. was established in order to enter into the construction engineer dispatch business.
June 2012	The distribution and retail dispatch business of UT icom Co., Ltd. was spun-off and UT Agent Co., Ltd. was established
July 2012	To enhance the UT Group's brand power, some subsidiaries were renamed to make corporate names of all subsidiaries start with UT
October 2012	UT Life Support was established in order to expand welfare services to employees
July 2013	81% of shares of Panasonic Battery Engineering Co., Ltd. were acquired to make it a subsidiary that was renamed UT Pabec Co., Ltd.
May 2015	System Revolution Co., Ltd. was made into a subsidiary
July 2015	UT Holdings Co., Ltd. was renamed UT Group Co., Ltd.
October 2015	Renamed UT Leading as UT Technology Co., Ltd., UT Construction Network as UT Construction Co., Ltd., and System Revolution as UT System Co., Ltd.

*1 The 2012 problem that affected the group was that in conjunction with the rapid expansion in production following the Lehman Brothers' collapse, from 2009 the re-utilization of dispatch workers started once again in the manufacturing industry. But then the temporary employment periods of the dispatched workers that started at that time all came to an end at the same time in 2012. Manufacturing companies, which are the group's main clients, were required to decide whether to directly employ their dispatch workers and workers on a fixed-term employment contract, or to switch to outsourcing. Since then, the shift toward outsourcing has accelerated even outside of the semiconductor industry.

*2 In July 2012, its name was changed to UT Leading Co., Ltd., and in October 2015, it was renamed again as UT Technology.

*3 In April 2012, its name was changed to UT icom Co., Ltd., and at the same time it launched a manufacturing dispatch and outsourcing business. But then in June 2012, it spun-off the distribution and retail dispatch business and established UT Agent Co., Ltd. In April 2013, UT Agent transferred its business to UT icom (UT icom was merged with UT Aim in April 2014).

*4 The acquisition cost was ¥1,000mn. Renamed UT System in October 2015.

*5 Developed with an image of robust human resources, teamwork, and growth.

Strengths and Business Risks

Strengthened human resource cultivation and training programs and has the industry's highest retention rate

(1) Strengths and competition

The group's strengths are its systems of permanent employment and 100% employee participation in social insurance. In addition, by introducing Job Grade, which is a skill evaluation system on 25 levels; Entry System, in which employees can fairly become candidates for management; and an Employee Stock Ownership Plan (ESOP), it has achieved the lowest employee turnover rate in its industry (specifically, its current turnover rate is around 3 to 4%, which is significantly below the industry average of 8%). In addition, it has enhanced its system for developing and training human resources, including through the One-UT Project (a career progression program for design engineers), the Super Manager School (an executive training school), and MTM Training (a management leadership development program). This is considered to be a factor behind its ability to maintain the quality of its employees, which has been highly evaluated by its corporate clients.

Further, another one of its strengths seems to be that it can contribute to the improved management efficiency of its clients through the format of its outsourcing contracts, in which a team provides a start-to-finish outsourced production service.

The group is leveraging its strengths to differentiate itself from competitors in the semiconductor field, which is where its main clients are located, and has established an unshakeable position as the No.1 company in the manufacturing outsourcing industry in terms of the number of manufacturing outsourced and dispatched employees. On the other hand, competition is fierce for manufacturing outsourcing in growth fields like automobiles, where the group has been aiming to expand its business to escape from its reliance on the semiconductor field through developing a market leader strategy. But despite this competition, the group is steadily increasing client numbers through leveraging its strengths. Specific competitors in this field include Nikken Sogyo, NISSO, Outsourcing <2427>, and World Holdings <2429>.

(2) Business risks

The group's business risks can be summarized into two points; a) its high reliance on the manufacturing and semiconductor-related industries and b) securing human resources.

As the group's clients are in the manufacturing industry, they are likely to be affected by fluctuations in the macro economy, like a strong yen and the domestic economic climate. Further, while the percentage of sales from the semiconductor field is declining due to the progress the group is making in its strategy of escaping from its reliance on the semiconductor-related field, this business still provides around 40% of sales, so the group could be affected by changes in the performance of its semiconductor-related corporate clients.

The group's source of revenues is its human resources and securing them is its biggest challenge. It may not be able to secure the engineers it requires due to conditions in the labor market. Or if its employee retention rate declines, this may have a negative impact on earnings due to an increase in hiring expenses. In addition, its hiring system in its main manufacturing dispatch and outsourcing services business is founded upon hiring locally in each region, so if it has difficulties hiring in one region, it will have to hire from other regions and will incur relocation expenses, which may cause profitability to decline.

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