

Cybernet Systems Co., Ltd.

4312

Tokyo Stock Exchange First Section

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<https://www.fisco.co.jp>

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Summary

Despite being impacted by the termination of distributor agreement with a main business partner, the Company targets a quick recovery by advancing its growth strategy.

Cybernet Systems Co., Ltd. <4312> (hereafter, also “the Company”) is a major company for CAE (computer-aided engineering) software solution services that are used for design, R&D, and other aspects, centered on the manufacturing industry, and it also handles cloud security and other products. As a leading CAE company, it is a sales vendor for more than 30 companies, mainly of software products, while as a pioneer for CAE solutions, domestically it has as its customers more than 2,000 companies and 500 research institutes and universities. It also has three overseas software development companies as subsidiaries, including conducting a CAE solutions business in the Asia market, mainly in China. More than 50% of net sales on a Company stand-alone basis comes from stock business (license renewals by existing customers), so earnings are highly stable.

1. 1H FY12/21 results overview

In the 1H FY12/21 (January-June 2021) consolidated results, net sales increased 5.4% year on year (YoY) to ¥12,507mn, while operating profit rose 10.2% YoY to ¥2,238mn. In the mainstay CAE Solution Services business, despite weakness in sales of new licenses, strong renewal demand and growth in engineering services, as well as strong sales to Asia, resulted in a 6.5% increase in net sales and a 6.0% increase in segment profit. In the IT Solution Services business, although growth in net sales was only 0.2% YoY, segment profit increased significantly by 72.2% due to large growth in cloud security products which have relatively high profit margins, as well as strong sales of EndoBRAIN®, AI-equipped colorectal endoscopy diagnosis support software, which is one of the Company’s in-house developed products.

2. Outlook for FY12/21

The outlook for FY12/21 is for sales to increase 1.8% YoY to ¥22,056mn, and for operating income to decline 14.1% YoY to ¥2,472mn. These are both downward revisions from the Company’s initial forecasts (net sales of ¥22,400mn and operating income of ¥2,700mn). This downward revision is due to the termination of distributor agreements with a main business partner (Synopsys, U.S.A., <SNPS>) on October 1, 2021, and the resulting absence of related sales in 4Q. The reason for the termination of the agreement was Synopsys’s switch from distribution sales to direct sales on a global basis. The Company’s Synopsys-related net sales were ¥4,657mn in FY12/20, accounting for 21.5% of consolidated net sales. This was second behind ANSYS <ANSS> (U.S.) *, so the Company expects a temporary negative impact on results. In response, the Company has concluded a new distributor agreement with ANSYS for optical CAE software, which was the product offered by Synopsys. In addition to proposing replacement to existing corporate customers, the Company will work to increase sales of other products and services as part of its plan to limit the negative impacts to a minimum.

| * Globally leading CAE software company, with net sales of US\$1,681mn in 2020. |

Summary

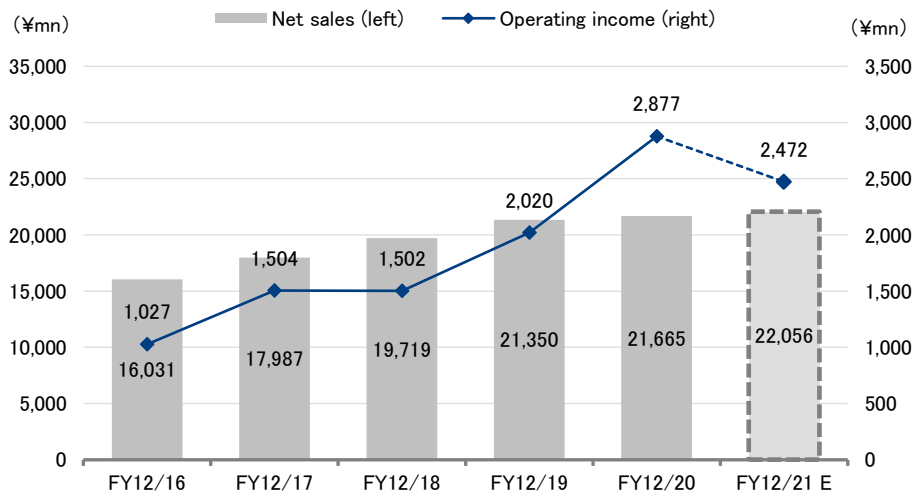
3. Summary of the medium-term business plan

In February 2021, the Company announced the three-year medium-term business plan with FY12/23 as its final fiscal year. The Company has said it will make a new announcement in February 2022 regarding the impact on earnings in FY12/22 on beyond accompanying the termination of the distributor agreement with Synopsys as well as its future plans, but there are no changes to its plans of advancing its original initiatives for its growth strategy. In the CAE solutions field, the Company will work on the three strategies of strengthening core business, DX business expansion, and expanding the use of simulation, while in the IT solutions field, the Company will focus on the cloud security business, for which demand is robust. In terms of strengthening core business, the Company will work to strengthen relationships and collaboration with top vendors and expand sales of in-house products globally. In DX business expansion, as a solution in the CAE domain, the Company will work to provide AR/VR technology utilization and cloud platform services. In terms of expanding the use of simulation, penetration in industries such as the healthcare industry and the construction industry has begun, and the Company plans to acquire new customers. In addition to the above efforts, the Company intends to proactively consider M&A deals that could result in synergies.

Key Points

- In 1H FY12/21, sales and profit increased due to the expansion of overseas sales, especially in Asia, and growth in the cloud security business
- In FY 12/21, expecting an increase in sales and a decline in profit, partly due to the impact of the termination of distributor agreements with Synopsys
- Aiming for growth by strengthening the core business, DX business expansion and expanding the use of simulation, while also strengthening the cloud security business

Results trends



Source: Prepared by FISCO from the Company's financial results

■ Company overview

Has supported manufacturing in Japan for more than 30 years as a leading CAE company

1. History

Cybernet Systems Co., Ltd. was established independently in April 1985 after Control Data Corp. (CDC), a US-based supercomputer pioneer, spun off its cybernet services business, and had previously been CDC's Japanese subsidiary, Nihon CDC K.K. Cybernet is a portmanteau of "cybernetics" (cyber) and "telephone network" (net), and refers to the computer service CDC provided globally from the 1970s to 1990 that allowed people to rent remote access to a computer by the hour. At that time, computers were expensive, so companies and research institutes used this service to carry out tasks such as scientific and technological calculations and simulations.

From 1990, the performance of computers improved dramatically and they became inexpensive, so these users have come to own their own computers, on which they have installed dedicated software to conduct design development, R&D and other tasks. Due to this change in use, as demand for cybernet services declined, the Company concluded sales distributor contracts with leading overseas software vendors, and converted to a business model of conducting sales and providing installation support services for these companies, thereby expanding its business.

In 1989, the Company became a subsidiary of Kobe Steel, Ltd. <5406>, and then in 1999, FUJISOFT ABC Incorporated (currently, FUJI SOFT INCORPORATED <9749>) acquired all of its shares and made it a wholly owned subsidiary, and it is currently FUJISOFT's subsidiary. In October 2001, the Company's shares were listed on the JASDAQ market (currently listed on the Tokyo Stock Exchange (TSE) First Section), and since 2005, it has actively progressed an M&A strategy with the aim of expanding its business area in the CAE field. Domestically, in 2005, it made subsidiaries of KGT Inc. (has advanced visualization technologies and network-related software) and PLAMEDIA CORPORATION (specializes in a plastics CAE business), and then in 2006, it acquired the business rights of Keihin Artwork, Inc. and EDA Connect Co., Ltd. and expanded its business areas. Also, recently in January 2020, it established CYBERNET MBSE Co., Ltd., which mainly provides engineering services related to MBSE*, including outsourced analysis and consulting.

* MBSE (model-based systems engineering) refers to a method for conducting analysis, design, and verification of system requirements from various perspectives using models for systems targeted for development. Alongside the higher performance and multifunctional nature of systems, the process from requirement definitions through to design and verification has become increasingly complex, and MBSE makes possible efficient development through the modelling of these elements.

Company overview

Conversely, alongside the entry into Asia of Japanese companies and the growth of Asian companies, centered on China, demand is growing for CAE solutions in the Asia region. In this situation, the Company has also been establishing sales subsidiaries in various Asian countries. In 2004, it established CCA ENGINEERING SIMULATION SOFTWARE (Shanghai) CO., LTD. in order to prepare an environment to provide technological services in China at the same level as in Japan, and it began providing technological services relating to CAE, including consulting, outsourced analysis, and education. Next, in 2008, it established CYBERNET SYSTEMS TAIWAN Co., Ltd. in Taiwan to provide CAE Solution Services, including those related to optical, control, and formula processing. Then in 2017, it established CYFEM Inc. in South Korea to provide optical-related CAE solution services, and in 2018, CYBERNET SYSTEMS MALAYSIA SDN. BHD. in Malaysia to provide machinery- and optical-related CAE solution services. In these ways, the Company has been strengthening its business development in the Asia region. Based on the termination of the distributor agreements with Synopsys, the Company has decided to liquidate CYFEM in South Korea before the end of 2021.

Also, in June 2009, the Company's sales distributor contract with The MathWorks, Inc. of the US, which was the main customer providing more than 30% of total sales, ended (due to The MathWorks establishing a Japanese subsidiary) and earnings fell significantly. In this way, the distributor business is exposed to risk, so the Company has strengthened its in-house products. Specifically, in 2009, it made subsidiaries of Sigmetrix, LLC of the United States (hereafter, Sigmetrix; development and sales of tolerance*1 analysis software and consulting) and Waterloo Maple Inc. of Canada (hereafter, Maplesoft; development, sales, consulting and online services for formula analysis software, etc.). Then in 2010, it made a subsidiary of Noesis Solutions NV of Belgium (hereafter, Noesis; development, sales, and technological support for PIDO*2 tools).

*1 Tolerance: The allowable range of variation of the dimensions set at the time of design.

*2 PIDO (Process Integration and Design Optimization): A solutions tool for overall optimization that contributes to improving quality, shortening the development period, and reducing costs through the automation, integration, and optimization of the product development process utilizing CAD/CAE.

History

| Date | Event |
|----------------|---------------------------------------------------------------------------------------------------------------------------------------------------------|
| April 1985 | Control Data Corp. (CDC) of the US separated its cybernet services business and established Cybernet Systems Co., Ltd. |
| April 1989 | Kobe Steel, Ltd. <5406> acquired all of the Company's issued shares. |
| October 1999 | FUJISOFT ABC Incorporated (currently, FUJI SOFT INCORPORATED <9749>) acquired all of the Company's issued shares and made it a wholly owned subsidiary. |
| October 2001 | Listed on the JASDAQ market and increased capital to ¥995mn. |
| August 2003 | Listed on the TSE Second Section. |
| September 2004 | Listed on the TSE First Section. |
| December 2004 | Established subsidiary CCA ENGINEERING SIMULATION SOFTWARE (Shanghai) CO., LTD. in Shanghai, China. |
| April 2005 | KGT Inc. made a subsidiary through acquisition of all shares. |
| August 2005 | PLAMEDIA CORPORATION made a subsidiary through acquisition of 95% of shares. |
| May 2006 | Took over operation of Keihin Artwork Co., Ltd. and EDA Connect Co., Ltd. |
| August 2006 | Established Cybernet CAE Systems (Shanghai) Co., Ltd. (currently, CYBERNET SYSTEMS (SHANGHAI) CO.,LTD.) in Shanghai, China. |
| July 2008 | Established CYBERNET SYSTEMS TAIWAN Co., Ltd. in Hsinchu City, Taiwan. |
| July 2009 | Made Sigmetrix, LLC a wholly owned subsidiary. |
| August 2009 | Merged with PLAMEDIA CORPORATION. |
| September 2009 | Made Waterloo Maple Inc. (Maplesoft) a wholly owned subsidiary. |
| May 2010 | Merged with KGT Inc. |
| July 2010 | Made Noesis Solutions NV a wholly owned subsidiary. |
| March 2012 | Established CYBERNET SYSTEMS KOREA CO., LTD. in Seoul, South Korea (closed in 2015). |
| September 2017 | Established subsidiary CYFEM Inc. in Seoul, Korea. |
| November 2018 | Established subsidiary CYBERNET SYSTEMS MALAYSIA SDN. BHD. in Malaysia. |
| January 2020 | Established CYBERNET MBSE Co., Ltd. |

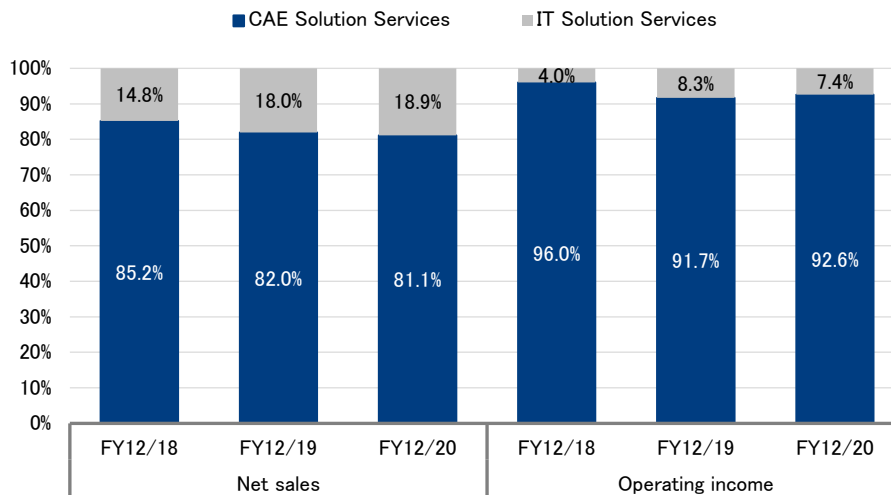
Source: Prepared by FISCO from the Company's website

Is developing the CAE Solution Services Business and IT Solution Services

2. Business description

The Cybernet Group develops solution services businesses in Japan and overseas through software and technology services (technological support, consulting, etc.). As the fields targeted by these businesses are different, it discloses information on two business segments, the CAE Solution Services and IT Solution Services. CAE Solution Services is conducted by the Company and CYBERNET MBSE, and overseas by Maplesoft, Sigmetrix, Noesis, and the four sales subsidiaries in Asia (in China, Taiwan, South Korea, and Malaysia) for the development and sales of in-house products. IT Solution Services is conducted only by the Company. Looking at the breakdown of results by business segment in the most recent 3 years, we see that CAE Solution Services is the main business contributing more than 80% of net sales and more than 90% of segment operating income. At the end of December 2020, there were 622 employees on a consolidated basis and 371 employees on a Company stand-alone basis, while approximately 45% of consolidated employees were engineers.

Breakdown of results by business segment



Note: Calculations for operating income do not include eliminations
 Source: Prepared by FISCO from the Company's financial results

(1) Business model

To simply explain the business model, the Group has concluded sales distributor contracts with more than 30 leading software vendors in Japan and overseas, and it sells software products (including in-house Group products) to customers that include companies, universities, and research institutes. Also, when conducting sales, it provides solution services with added value that meet customer needs, including technological support so customers can skillfully use the products, operations support consulting, and engineering services. In addition, it contributes to improving product capabilities by providing feedback on customer needs to vendors, which are the developers.

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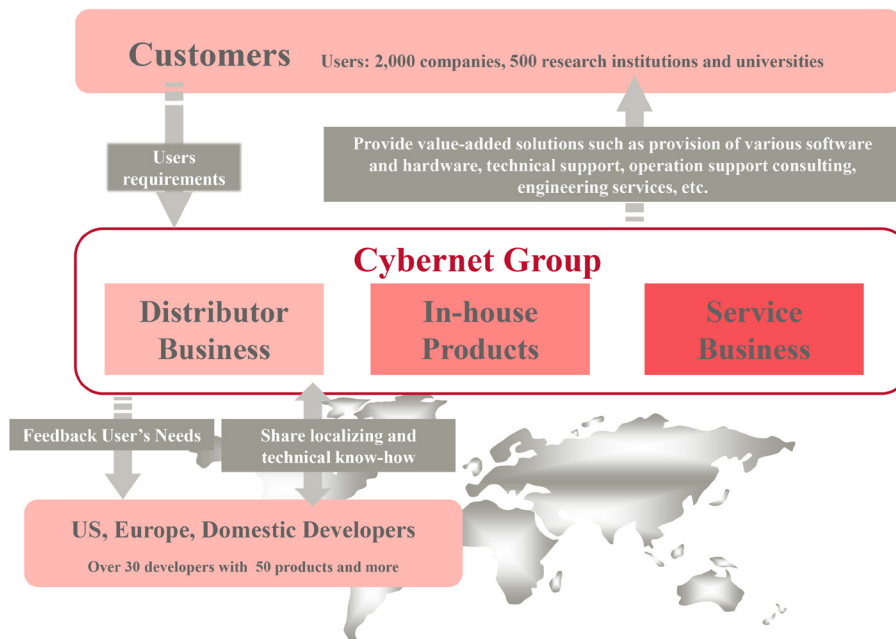
Company overview

In particular, as a pioneering company in the CAE solutions field in Japan, it has accumulated an abundance of experience and technologies across more than 30 years, and it has solution capabilities to guide customers to the solutions to their various problems. Therefore, it has built strong relationships of trust with them, and at the same time, it has acquired an excellent reputation among vendors, which are the developers. For example, ANSYS, Inc. of the US, which is currently its main business-partner vendor, awarded for 7 consecutive years from 2015, certified it as an ANSYS Elite Channel Partner*1, and the Company won two awards*2 in 2020 in recognition of its activity record and digital shift amid the spread of the new coronavirus (COVID-19) (hereinafter, COVID-19 pandemic), indicating its reputation as the company’s leading partner in the Asia region. Its customers in Japan are 2,000 companies and 500 universities and research institutes, and it can be said to be a leading company in the CAE solutions field.

*1 Channel Partner of the Year is the title awarded to the organizations recognized as contributing the most to the sales activities of ANSYS software from among its sales partners throughout the world, and the Company was the winner for the Asia area. ANSYS Elite Channel Partner is the title awarded to sales partners that meet the strictest certification and resource requirements, and the Company was the first distributor in Japan to be awarded the title for seven consecutive years.

*2 The Company received two awards. One was the “Marketing Excellence & Agility in 2020” (presented to partners who, amid the COVID-19 pandemic, produced remarkable results in marketing based on a quick digital shift). The other award received was the “TOP Renewal Performers in 2020” (presented to distributors who continually achieve high contract renewal rates by providing a highly-satisfying technical support to existing customers).

The Company’s business model



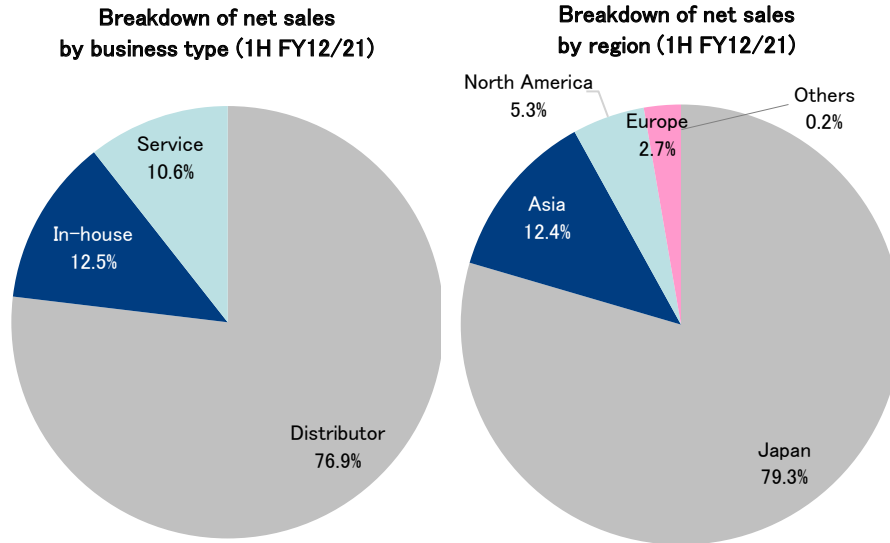
Source: Reprinted from materials provided by the Company

(2) Net sales by business type and region

Net sales can be broken down into three business types: distributor sales for products developed by vendors, sales of in-house products, and sales of various types of solution services (engineering services, education and training services, etc.). In 1H FY12/21 consolidated results, distributor sales contributed 76.9% of total sales, in-house products 12.5%, and services 10.6%. Also, looking at the breakdown of net sales by region, Japan contributed 79.3%, Asia 12.4%, North America 5.3%, and Europe 2.7%, from which we understand that the domestic distributor business is the main business. Going forward, the Company’s strategy is to aim for further growth by increasing sales of in-house products and services and overseas sales, such as in Asia.

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

Company overview



Source: Prepared by FISCO from the Company's results briefing materials

(3) Net sales by contract type and industry

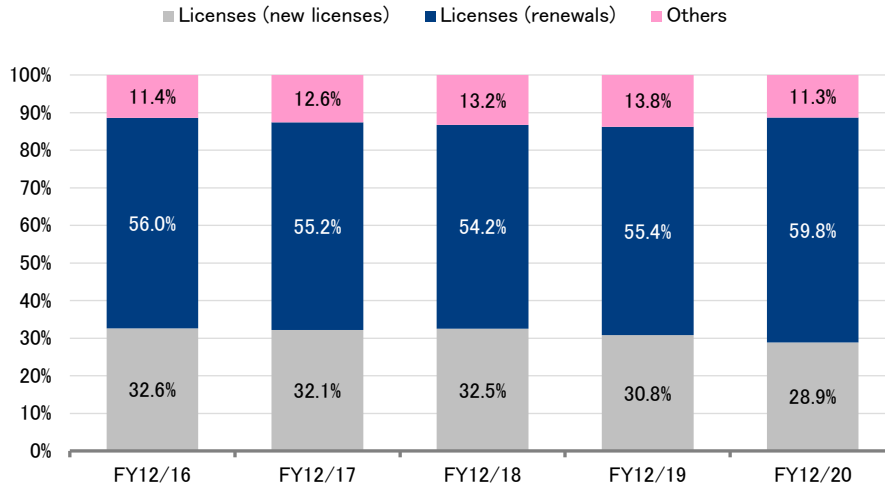
Net sales can be broken down by contract type into licenses and others. Furthermore, licenses are divided into new license fees when installing a new software product (initial installation fee and 1 year usage fee + maintenance fee) and renewal fees from the second year onwards (1 year usage fee + maintenance fee). To this are added various optional services, as necessary for the customer. Conversely, sales other than from licenses include those from engineering services* and education and training services.

* Services in order for customers to effectively use the software, including software installation support, technological support, and outsourced analysis.

Looking at how sales have trended in the last five years on a Company stand-alone basis, license renewals have contributed more than 50%, followed by new licenses at around 30%, and others at around 10%. Major companies, universities, and research institutes constitute more than half of the Company's customers. Once one of the main CAE software products is installed, there are hardly any cases of it being replaced with another company's product from the viewpoint of continuity, and except for situations in which a customer company no longer needs the CAE software, such as due to withdrawing from a business, nearly all companies renew. Therefore, within the Company, renewals are positioned as stock business and a stable earnings foundation.

Company overview

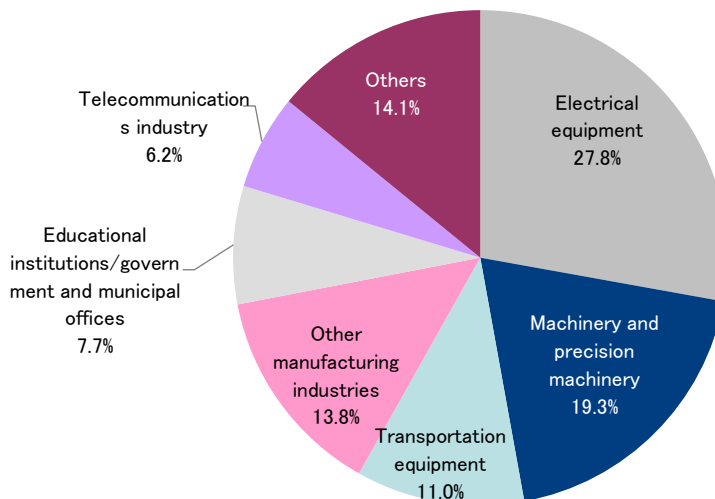
Breakdown of net sales by contract type (stand-alone)



Source: Prepared by FISCO from the Company's results briefing materials

Also, looking at the breakdown of net sales by industry in 1H FY12/21 on a Company stand-alone basis, the highest was electrical equipment at 27.8%, followed by machinery and precision machinery at 19.3%, other manufacturing industries at 13.8% and transportation equipment at 11.0%. Sales to the manufacturing industry was more than 70% of overall sales. However, in the last few years, sales to non-manufacturing industries have been growing due to the growth in the simulation utilization domain, and their share of net sales on an upward trend.

Breakdown of net sales by industry (stand-alone; 1H FY12/21)



Source: Prepared by FISCO from the Company's results briefing materials

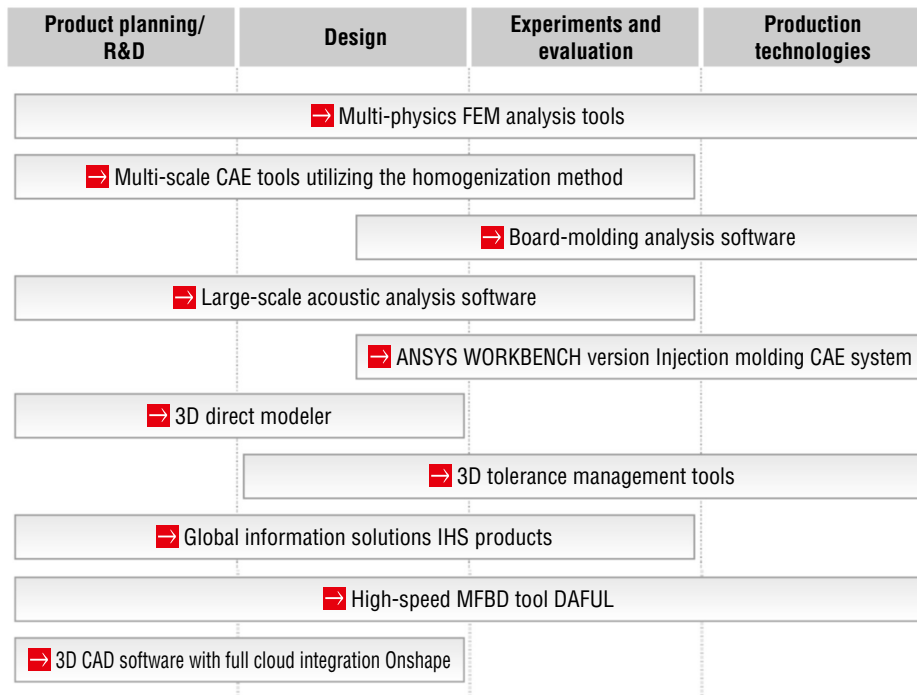
In CAE solutions, the mainstay products are from CAE sector globally leading company ANSYS

3. CAE Solution Services

The mainstay CAE Solution Services business provides various simulation and software products according to each field, including those related to machinery, optical, electrical and electronic, and control. CAE is the name for technologies to simulate and analyze in virtual models created on computers aspects such as tests and experiments that have been conventionally carried out using a prototype in the R&D process for manufacturing. Using CAE software dramatically reduces the number of prototype tests and experiments, and makes it possible to conduct simulations under physical conditions that cannot actually be created in the real world. So it is said to be software that not only improves development efficiency, but also contributes to realizing manufacturing that is considerate to the environment by significantly reducing waste and other materials created in prototype testing. The scope of application is wide, ranging from fields like automotive, electronic equipment and devices to machinery and precision machinery and medical fields.

From among ANSYS's multi-physics analysis tools, the main products include general-purpose analysis tools that make every type of analysis possible, including structure, heat transfer, electromagnetic field, piezoelectric, acoustic, heat fluid, and dropping analyses. Also, for optical systems, the Group was mainly handling the products of Synopsys, but the distributor agreements with Synopsys terminated on October 1, 2021, so the Company is concluding new distributor agreements for ANSYS's optical systems products. Other than these, the Group also handles the products of the leading development vendors in their respective industries and in-house products developed by Group companies. It proposes solutions that are optimized to meet customer needs.

List of machinery-related CAE



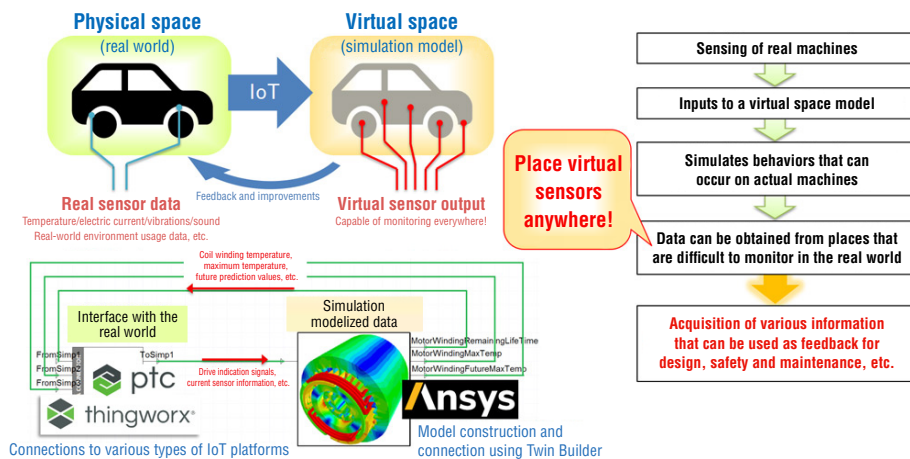
Source: The Company's website

IT solutions mainly handles Broadcom's information security products (Symantec brand)

4. IT Solution Services

The IT Solution Services business is centered on various types of information security software products, such as cloud and endpoint security, and the main business-partner vendor is Broadcom Inc. (formerly, Symantec Corporation), accounting for a significant part of sales. For other solutions as well, it provides advanced solution services, including big data visualization solutions, AR/VR solutions, and digital twin construction support. Digital twin refers to a development method of creating a virtual space (on a computer) of the physical facilities actually operating in manufacturing development sites, collecting information on the physical facilities in real time from IoT and other sensors, and sending this information to the virtual space. This is to realize the same environment in the virtual space as the physical facilities and to evaluate the current conditions of the physical facilities, and to carry out various simulation tests. It is a solution to increase the sophistication of and optimize the manufacturing process by combining real-world verification data and simulation data in a virtual space.

Example of the utilization of IoT/digital twin



Source: The Company's website

In the CAE field, a strength is solution capabilities based on knowhow and technological capabilities accumulated over many years

5. Strengths and business risks

The Company's strengths can be summarized as the following four points.

(1) Sophisticated know-how backed up by experience

It has accumulated a rich track record from over 30 years of providing support for manufacturing R&D and design development through CAE simulation technologies. The know-how and advanced technological capabilities it has accumulated are its assets, and a strength is being able to provide solutions that other companies cannot imitate.

Company overview

(2) Extensive specialty and global partner network

Including ANSYS, the largest CAE software company, the Company collaborates with more than 30 leading vendors in Japan and overseas, and conducts sales and support for more than 50 types of products. Therefore, a strength is its ability to provide optimized solutions to address customers' various issues by combining multiple software and know-how. It also communicates feedback from customers to vendors, which are the developers, and they use that feedback for product improvements. So another strength can be said to be that it is building strong relations with both customers and vendors.

(3) Highly stable earnings structure and industry environment

The majority of the Company's sales are provided by license renewal fees from existing customers, so its earnings are highly stable. Moreover, there are relatively few competitors in the CAE industry, so a feature of the industry environment is that price competition is unlikely to occur. For companies, R&D is a source of their competitiveness, so demand does not cool down greatly even if economic conditions deteriorate somewhat. It is considered that this situation leads to the Company's highly stable earnings.

Competitor companies in the CAE software distributor business include IDAJ Co., LTD. and ITOCHU Techno-Solutions Corporation <4739>, which are ANSYS sales distributors; ARGO GRAPHICS Inc. <7595>, which is a sales distributor of Dassault of France; and Information Services International-Dentsu, Ltd. (ISID) <4812>, which handles products including those of Siemens of Germany.

(4) Wide-ranging customer base

Currently, the Company has 14 consolidated subsidiaries in Japan and overseas, and a strength is that they have many customers, including global companies, universities, and research institutes. Among the customer companies, in Japan alone there are more than 2,000 companies and 500 universities and research institutes, and the majority of major manufacturing industry companies in Japan are its customers.

(5) Risk factors

A risk factor is that the distributor business contributes more than 70% of net sales. In principle, sales distributor contracts with development vendors are non-exclusive, short term and subject to renewal. So changes at the developers, for example a change of sales strategy due to an M&A or a change to the management team, will have a negative impact on results if it causes the distributor agreement to be terminated. However, ANSYS which is the Company's main business partner, is establishing its own Japanese corporations, and in this situation, it has positioned the Company as an excellent sales partner and has built strong business relations with it. So at the current time, the risk of it cancelling the agreement seems to be extremely low.

Meanwhile, the Company announced that the distributor agreements it had with Synopsys, its largest supplier after ANSYS, terminated as of October 1, 2021. The reason was that Synopsys switched its sales style from distributor sales to direct sales on a global basis. As a result, the Company plans to reduce business risk by strengthening its in-house developed products as well as its solution services including engineering services. With respect to the distributor business, the Company's strategy is to continue to search for promising development vendors and expand its product lineup, as well as continue to build strong relationships with development vendors.

Results trends

In 1H FY12/21, sales and profit increased due to the expansion of overseas sales, especially in Asia, and growth in the cloud security business

1. Overview of 1H FY12/21 results

In the 1H FY12/21 consolidated results, sales and profits increased, with net sales rising 5.4% YoY to ¥12,507mn, operating income growing 10.2% to ¥2,238mn, ordinary income climbing 10.7% to ¥2,227mn, and profit attributable to owners of parent increasing 6.2% to ¥1,426mn.

1H FY12/21 consolidated results

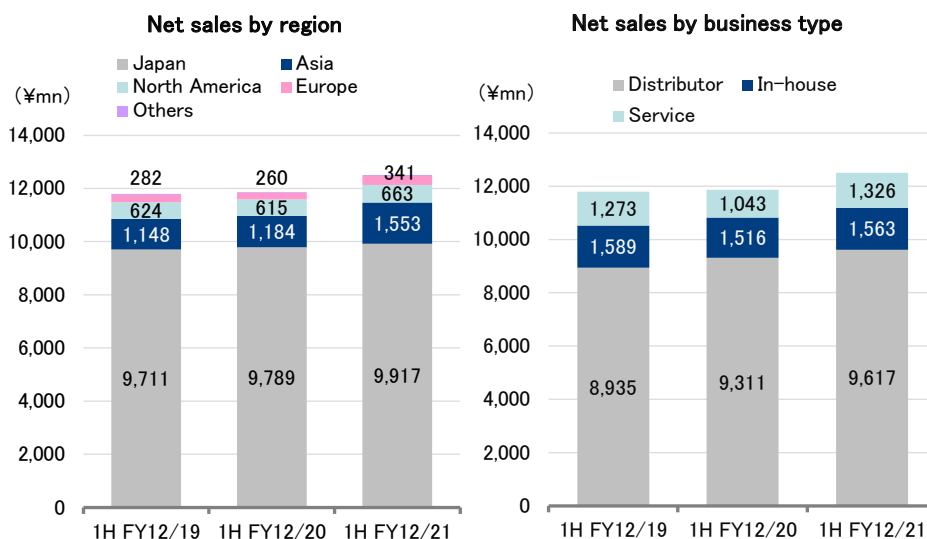
| | 1H FY12/20 | | 1H FY12/21 | | YoY |
|-----------------------------------------|------------|------------|------------|------------|-------|
| | Results | % of sales | Results | % of sales | |
| Net sales | 11,871 | - | 12,507 | - | 5.4% |
| Cost of sales | 6,994 | 58.9% | 7,253 | 58.0% | 3.7% |
| SG&A expenses | 2,845 | 24.0% | 3,015 | 24.1% | 6.0% |
| Operating income | 2,031 | 17.1% | 2,238 | 17.9% | 10.2% |
| Ordinary income | 2,011 | 16.9% | 2,227 | 17.8% | 10.7% |
| Extraordinary loss (income) | -1 | - | -72 | - | - |
| Profit attributable to owners of parent | 1,343 | 11.3% | 1,426 | 11.4% | 6.2% |

Source: Prepared by FISCO from the Company's financial results

Net sales increased due to strong demand for license renewals in CAE Solution Services as well as a recovery in sales of engineering services which were weak in the year-earlier period due to the COVID-19 pandemic. By region, net sales grew a bit sluggishly in Japan, increasing 1.3% YoY to ¥9,917mn, but continued to grow in Asia, increasing 31.2% to ¥1,553mn. In North America, sales rose 7.8% to ¥663mn, while sales in Europe increased 31.0% to ¥341mn, after dipping in both regions in the year-earlier period as a result of the COVID-19 pandemic. By business type, net sales increased 3.3% YoY to ¥9,617mn in the distributor business, grew 3.1% to ¥1,563mn for in-house products, and rose 27.1% to ¥1,326mn for services. The increase in sales of services was due to the recovery in engineering services in the CAE Solution Services business as well as growth in cloud security services in the IT Solution Services business.

As in-person sales efforts have been restricted due to the COVID-19 pandemic, the Company's sales activities to acquire new prospective customers included proactively holding online events and online seminars. In 1H FY12/21, the Company held 187 events (versus 58 in the year-earlier period), and a total of 11,134 people participated in these events (versus 2,468 people a year earlier). Going forward, the Company plans to use both in-person and online sales depending on the situation.

Results trends



Source: Prepared by FISCO from the Company's results briefing materials

Looking at factors affecting operating income, the operating margin increased from 17.1% in the year-earlier period to 17.9%, as the increase in sales and the decline in the cost-of-sales ratio caused by an improvement in the sales mix absorbed the increase in SG&A expenses (primarily an increase personnel costs at overseas subsidiaries). As extraordinary losses, the Company posted an impairment loss of ¥59mn and a provision for loss on business liquidation of ¥11mn. The impairment loss involved an impairment by the full book value for fixed assets that were expected to be scrapped in association with the review of office space in the head office and assets for which investment recovery was determined to be difficult following the termination of the distributor agreements with Synopsys. With respect to the provision for loss on business liquidation, in conjunction with the termination of the distributor agreements with Synopsys, the Company has decided to liquidate CYFEM in South Korea, its sales subsidiary for optical system CAE software, and posted the liquidation-related losses that it currently expects to incur.

(1) Results trends by segments

a) CAE Solution Services

In CAE Solution Services, net sales increased 6.5% YoY to ¥10,346mn and segment profit grew 6.0% to ¥2,669mn. Domestically, although sales of new licenses for mainstay products, such as multi-physics and optical-related analysis tools were weak, license renewals were strong and sales of engineering services grew due to factors including the acquisition of large orders from the machinery and precision machinery sectors.

At overseas sales subsidiaries, sales were strong of multi-physics and optical-related analysis tools, particularly for China. In the development subsidiaries also, earnings were boosted by sales of technological support services and software developed in-house, including Maplesoft's STEM* computing platform, Sigmetrix's tolerance analysis management tools, and Noesis's optimal design support tools. In the year-earlier period, sales activities were restricted due to the lockdowns caused by the COVID-19 pandemic, but since the start of 2021 Maplesoft and Sigmetrix have seen an increase in sales due to the return of normal sales activities.

* STEM is the general name for the comprehensive field comprised of Science, Technology, Engineering and Mathematics.

Results trends

b) IT Solution Services

In IT Solution Services, sales and profits increased, with net sales rising 0.2% YoY to ¥2,160mn and segment profit growing 72.2% to ¥333mn. Despite weak sales of end-point security products, sales of security solutions for the cloud environmental increased 115.0% YoY in conjunction with the spread of teleworking among companies. Specific contributors to the increase in sales were OneLogin (cloud-based single sign-on/access control solution), Box (a newly handled product that is a cloud-based content management and sharing system), and Mobileiron (the world's first a zero-trust platform centered on mobile, that is the foundation for integrated end point management functions).

Sales of the EndoBRAIN® series (software to support diagnosis in colorectal endoscopy using artificial intelligence), which are products developed in-house for the healthcare sector, were strong due to efforts to enhance the functions (bolster the user interface, improve precision). EndoBRAIN® is software that uses AI to analyze endoscopic images captured by ultra-high magnification endoscopes and general purpose endoscopes manufactured by Olympus <7733>, and assists doctors in detecting lesions by alerting when it detects a lesion. This product was approved as managed medical equipment (class II) in 2020, and is being sold to medical institutions as a set along with endoscopes manufactured by Olympus.

Profits increased significantly despite only a slight increase in sales due to the increase in sales of EndoBRAIN®, a product developed in-house in which sales increases connect directly to profit.

Net sales by segment

| | (¥mn) | | | | |
|-----------------------|---------------|---------------|---------------|---------------|-------------|
| | 1H FY12/18 | 1H FY12/19 | 1H FY12/20 | 1H FY12/21 | YoY |
| CAE Solution Services | 9,182 | 9,732 | 9,714 | 10,346 | 6.5% |
| IT Solution Services | 1,565 | 2,066 | 2,157 | 2,160 | 0.2% |
| Total | 10,748 | 11,798 | 11,871 | 12,507 | 5.4% |

Source: Prepared by FISCO from the Company's financial results

Profits by segment

| | (¥mn) | | | | |
|-----------------------|--------------|--------------|--------------|--------------|--------------|
| | 1H FY12/18 | 1H FY12/19 | 1H FY12/20 | 1H FY12/21 | YoY |
| CAE Solution Services | 1,515 | 2,186 | 2,517 | 2,669 | 6.0% |
| IT Solution Services | 83 | 204 | 193 | 333 | 72.2% |
| Elimination | -550 | -765 | -680 | -764 | - |
| Total | 1,048 | 1,624 | 2,031 | 2,238 | 10.2% |

Source: Prepared by FISCO from the Company's financial results

(2) Sales trends by industry and contract type (stand-alone basis)

On a stand-alone basis, net sales increased 1.0% YoY to ¥9,830mn. Looking at how sales trended by industry, they decreased 2.6% YoY for electrical equipment as the decline trend continued. Meanwhile, there was a 10.5% increase in machinery and precision machinery, and 3.9% growth in transportation equipment. Also, net sales declined 1.3% for other manufacturing industries, decreased 1.8% for educational institutions/government and municipal offices, and rose 9.8% for the telecommunications industry, turning positive.

Results trends

In electrical equipment, the decline was caused by a low level of new orders received for multi-physics analytical tools amid the lingering impact of the COVID-19 pandemic. Meanwhile, the main causes of the increase in net sales to the machinery and precision machinery sectors were the winning of large orders for engineering services, receiving new licensing orders for optical system analysis tools, and growth in EndoBRAIN® for Olympus. In transportation equipment, although net sales increased due to the impacts of the COVID-19 pandemic running their course, sales were still lower than two years earlier as the recovery was slow. Net sales to the telecommunications industry recovered to the level of two years prior due to an increase in orders received for optical system analysis tools.

Net sales by industry (stand-alone)

| | (¥mn) | | | |
|-----------------------------------------------------------|--------------|--------------|--------------|-------------|
| | 1H FY12/19 | 1H FY12/20 | 1H FY12/21 | YoY |
| Electrical equipment | 2,998 | 2,804 | 2,730 | -2.6% |
| Machinery and precision machinery | 1,486 | 1,718 | 1,899 | 10.5% |
| Transportation equipment | 1,430 | 1,043 | 1,084 | 3.9% |
| Other manufacturing industries | 1,170 | 1,374 | 1,356 | -1.3% |
| Educational institutions/government and municipal offices | 803 | 773 | 759 | -1.8% |
| Telecommunications industry | 604 | 555 | 610 | 9.8% |
| Others | 1,261 | 1,465 | 1,390 | -5.1% |
| Total | 9,754 | 9,735 | 9,830 | 1.0% |

Source: Prepared by FISCO from the Company's results briefing materials

Looking at how net sales trended by contract type on a Company stand-alone basis, among licenses, new licenses decreased 9.7% YoY to ¥2,439mn, but renewals were solid, rising 1.0% to ¥6,307mn. The main factors for the decline in new licenses were the recoil decline following a large project in the year-earlier period, and slumping sales of Synopsys products. The factor behind the for the increase in renewals stopping at 1.0% was the delay in putting in place the internal system for renewals of ANSYS products (mainly for SMEs) in 1Q. As a result, net sales in 1Q declined 7.2% YoY, but then rebounded to a 5.8% increase in 2Q after the internal system had been put in place.

Net sales other than from licensees increased significantly by 37.2% YoY to ¥1,082mn. The main factors included the acquisition of large orders in engineering services and strong sales of cloud security services.

Net sales by contract type (stand-alone)

| | (¥mn) | | | |
|---------------------------------|--------------|--------------|--------------|-------------|
| | 1H FY12/19 | 1H FY12/20 | 1H FY12/21 | YoY |
| Licenses | 8,688 | 8,945 | 8,747 | -2.2% |
| New licenses | 2,807 | 2,702 | 2,439 | -9.7% |
| Renewals | 5,880 | 6,243 | 6,307 | 1.0% |
| Others | 1,066 | 789 | 1,082 | 37.2% |
| Total | 9,754 | 9,735 | 9,830 | 1.0% |
| (Stock-type sales ratio) | 60.3% | 64.1% | 64.2% | |

Source: Prepared by FISCO from the Company's results briefing materials

Under debt-free management, has financial assets of over ¥14bn and a solid financial foundation

2. Financial condition

Looking at the financial condition at the end of FY12/20, total assets were up ¥1,306mn compared to the end of the previous fiscal year to ¥23,548mn. The main influencing factors in current assets included notes and accounts receivable-trade increasing by ¥1,183mn. In addition, short-term loans receivable (transactions from the cash management system) for FUJISOFT, the parent company decreased ¥1,149mn, and short-term investment securities decreased ¥500mn in current assets. Meanwhile, cash and deposits increased by ¥1,655mn. As the total of these, financial assets were up ¥5mn compared to the end of the previous fiscal year to ¥14,894mn. In noncurrent assets, intangible assets increased ¥105mn in conjunction with the deployment of a core operating system, while investments and other assets decreased ¥57mn.

Total liabilities were up ¥118mn compared to the end of the previous fiscal year to ¥7,881mn. In current liabilities, the main factors were the increases accounts payable-trade and income taxes payable. Total net assets were up ¥1,187mn compared to the end of the previous fiscal year to ¥15,667mn. Retained earnings increased by ¥970mn due to the posting of profit attributable to owners of parent, while foreign currency translation adjustment increased ¥138mn in conjunction with the depreciation of the yen.

Looking at the management indicators, the capital adequacy ratio was 65.4% and is trending at a level above 60%. Also, under the Company's debt-free management, financial assets are at a level of above ¥14bn, from which its finances can be judged to be in extremely good condition. An issue for the future will be how the Company can use its abundance of financial assets to bring about earnings growth.

Consolidated balance sheet

| | (¥mn) | | | |
|------------------------------------|---------|---------|---------|------------|
| | FY12/18 | FY12/19 | FY12/20 | 1H FY12/21 |
| Current assets | 17,440 | 19,022 | 20,205 | 21,462 |
| (Financial assets*) | 11,554 | 13,379 | 14,888 | 14,894 |
| Noncurrent assets | 1,775 | 1,799 | 2,037 | 2,086 |
| Total assets | 19,215 | 20,821 | 22,242 | 23,548 |
| Current liabilities | 4,972 | 5,925 | 6,488 | 6,629 |
| Noncurrent liabilities | 1,375 | 1,259 | 1,273 | 1,252 |
| Total liabilities | 6,348 | 7,185 | 7,762 | 7,881 |
| (Interest-bearing debt) | - | - | - | - |
| Total net assets | 12,867 | 13,636 | 14,480 | 15,667 |
| (Stability) | | | | |
| Capital adequacy ratio | 66.3% | 64.7% | 64.2% | 65.4% |
| Interest-bearing debt ratio | - | - | - | - |

* Financial assets = cash and deposits + short-term investment securities + short-term loans receivable
 Source: Prepared by FISCO from the Company's financial results

Results trends

The outlook for FY12/21 is for net sales to increase but for operating income to decline, partly due to the termination of the distributor agreements with Synopsys

3. Outlook for FY12/21

The outlook for the FY12/21 consolidated results is for net sales to increase 1.8% YoY to ¥22,056mn, operating income to decrease 14.1% to ¥2,472mn, ordinary income to fall 13.3% to ¥2,462mn, and profit attributable to owners of parent to decrease 1.6% to ¥1,536mn. The downward revisions were due to the impacts from the termination of distributor agreements with a main business partner on October 1, 2021.

FY12/21 consolidated results outlook

| | FY12/20 | | FY12/21 | | | YoY | 2Q progress rate |
|-----------------------------------------|---------|------------|------------------|--------------------|------------|--------|------------------|
| | Results | % of sales | Company forecast | Revised forecasts* | % of sales | | |
| Net sales | 21,665 | - | 22,400 | 22,056 | - | 1.8% | 56.7% |
| Operating income | 2,877 | 13.3% | 2,700 | 2,472 | 11.2% | -14.1% | 90.6% |
| Ordinary income | 2,840 | 13.1% | 2,670 | 2,462 | 11.2% | -13.3% | 90.5% |
| Profit attributable to owners of parent | 1,561 | 7.2% | 1,680 | 1,536 | 7.0% | -1.6% | 92.8% |
| Net income per share (yen) | 50.09 | | 53.88 | 49.27 | | | |

* The revised forecasts were those announced on June 25, 2021.
 Source: Prepared by FISCO from the Company's financial results

Synopsys-related net sales were ¥4,657mn in FY12/20, and accounted for 21.5% of total consolidated net sales, which was second only to ANSYS. The profit margin was also on par with the Company-wide average. Sales of these products are skewed towards 2Q when most license renewals take place, so the impact on 4Q FY12/21 net sales is expected to be only several hundred million yen. The real impact will be seen in FY12/22. In response, on October 2, the Company concluded a new distributor agreement for optical system CAE software* with ANSYS, and it plans to recommend that customer companies using Synopsys products replace them with ANSYS products. Synopsys products held the leading market share in Japan, so getting customers to replace them will not be easy, but in addition to replacements based on the Company's strengths in solutions capabilities based on its experience and technology cultivated over more than 35 years, the Company will also work to acquire new customers. Additionally, by focusing energy on expanding sales of products it handles other than Synopsys products and products it has developed on its own, as well as on engineering services and cloud security solutions, the Company will keep the negative impacts accompanying the termination of the distributor agreements with Synopsys to a minimum.

* The Company began handling dimensional optical analytics software ANSYS Speos®, VR solution ANSYS VRXPERIENCE™, and photonics analytics software ANSYS Lumerical.

The forecast of a decline in profit despite an increase in net sales is mainly due to the fact that the Company is expecting an increase in travel and transportation expenses and advertising expenses in 2H, after these expenses had declined in FY12/20 due to the impacts of the COVID-19 pandemic, as well as the fact that the Company is not expecting subsidies that it posted for overseas subsidiaries in the previous fiscal year. Another factor is that the Company will carry out personnel investment and system investments in order to build a foundation for future growth. The progress rate on operating income through 1H was 90.6%, which is a high level, and at FISCO we believe that the Company will be able to achieve its full-year forecast. The percentage decline in profit attributable to owners of parent is expected to be small due to the fact that the extraordinary loss of ¥425mn recorded in FY12/20 will decline significantly.

■ Medium-term business plan

Aiming for growth by strengthening the core business, DX business expansion and expanding the use of simulation, while also strengthening the cloud security business

1. Summary of the medium-term business plan

In February 2021, the Company announced its three-year medium-term business plan up to FY12/23. In the plan, it newly formulated “Creating a sustainable society and inspiring the world through technology and ideas” as the vision, and “Guide customers towards breakthrough solutions with vigorous creativity” as the mission to realize this vision. Also, the three medium- to long-term basic policies it is working on in order to continue to grow as the simulation leading company are “Contributing to society through simulation,” “Growing into a global company,” and “Promoting diversity and strengthening the HR development.”

Previously, simulation technologies were mainly utilized for engineering to support manufacturing. But recently, the areas they are utilized for have been expanding to society as a whole, including for people’s lives and health and for the natural environment, and the Group companies propose solutions including for these areas. To grow as global companies, they are also developing the solutions business cultivated in Japan for the Asia market, centered on China, and expanding the distributor business, at the same time as working to increase sales of in-house Group products. In addition, to realize the vision and the mission, the policies are to continuously work to strengthen human resource development and organizational capabilities and to promote diversity.

In the CAE Solution Services business, the Group’s growth strategies include: 1) strengthening core business; 2) DX business expansion; and 3) Expanding the use of simulation. In the IT Solution Service business, the growth strategy is to strengthen the cloud security business. Regarding the results forecasts for FY12/22 and beyond, considering the impact from the termination of distributor agreements with Synopsys, the Company has decided to make an announcement on its direction again in February 2022. In its initial forecast, the Company had set targets of net sales of ¥26.0bn and operating income margin of 12% in FY12/23.

2. Status of initiatives in growth strategies

(1) CAE Solution Services

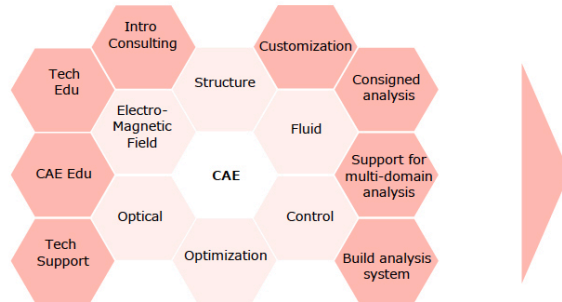
a) Strengthening the core business

In order expand the core business, the Group will strengthen its relationship and collaboration with top vendor ANSYS. Also, the Group is aiming to launch new products at an early stage to supplement the development vendors and to strengthen technologies and expand the product lineup, meet the needs for advanced simulation in cutting-edge fields, and strengthen relationships with leading vendors in IoT and cloud platforms that support the CAE infrastructure, and thereby grow sales. The cutting-edge fields include CASE* in the automotive industry, and development fields such as carbon neutral, sensing, and next-generation materials.

* CASE is the acronym of Connected (always connected to the Internet), Autonomous (driving), Shared, and Electric (vehicles). It is a field in which R&D is being actively progressed by various companies on the theme of developing next-generation vehicles.

Medium-term business plan

Strengthening the core business



- Autonomous
- Electrification
- Connected
- Carbon Neutral
- Sensors
- Next generation materials

Source: Reprinted from the medium-term business plan materials

As a new product handled, in April 2021 the Company launched sales of “Vuforia,” * an AR development platform, and in May 2021 the Company started sales of discrete element method software “ANSYS Rocky.” In October 2021, the Company started sales of optical-related CAE software.

* In April 2021, the Company concluded a distributor agreement with PTC Japan KK, and launched sales and technical support for “Vuforia,” which is developed by PTC (U.S.) <PTC>. By deploying this platform, the Company will promote the utilization of simulation and digital twin technology, and expand sales as a tool that supports remote work/DX in the manufacturing sector.

Also, the manufacturing industry has come to be centered on regions such as China and South East Asia, and in this situation, the world’s global companies are starting to develop R&D bases in these countries, so demand for CAE solutions in the Asia region is forecast to increase in the future. The Company has established sales subsidiaries in China, Taiwan, and Malaysia, and it transfers to the engineers of these sales companies the technological capabilities and know-how it cultivated in Japan, and its strategy is to aim to grow sales locally with solution services as a strength. Locally also, its policy is to secure distributor contracts with leading vendors, the same as in Japan, and to grow the businesses while aiming to strengthen structures, such as for human resource development. In the medium-term business plan, the aim is for net sales to Asia of ¥4.0bn by FY 12/23 (actual results in FY 12/20 were net sales of ¥2.5bn).

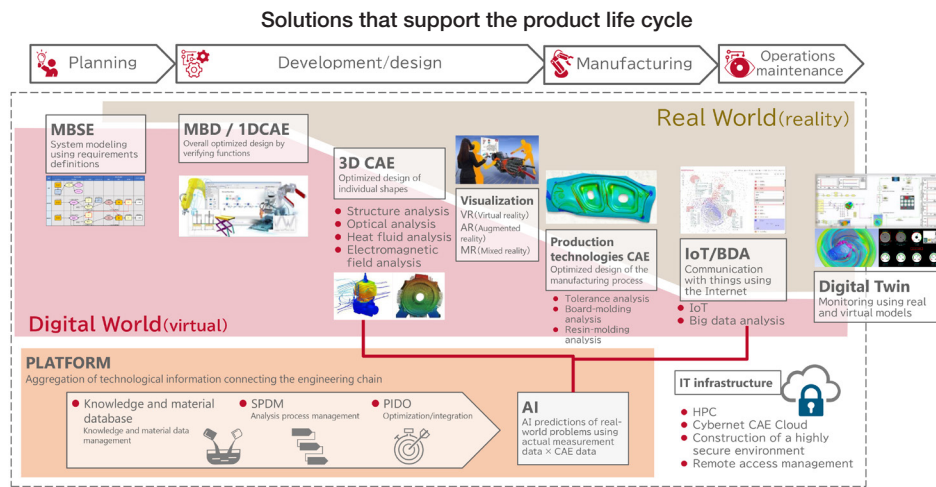
Furthermore, the Group is working to globally expand sales of its in-house products. For Maplesoft, in January 2021 the Company began sales of MapleLearn™ (English version), a formula analysis-use software that can be used in an online environment, to the education market. Also, in March the Company started sales of an English version of MapleFlow™, a mathematics software that enables engineers to perform design calculations in a whiteboard style, and then launched sales of a Japanese version in May 2021. In addition to the current main business targeting the education market, the Company plans to strengthen development for the manufacturing sector.

For Sigmetrix, an upgraded version of its mainstay tolerance analysis software CETOL 6σ (CETOL Six Sigma) with new features to improve user experience was released in June 2021, and the Company is now widely selling this product. The Company is not only selling this product, but is also focusing on online training and consulting service, and it plans to expand sales globally.

Medium-term business plan

b) DX business expansion

The Group is increasing sales by providing high-value-added solutions through combining big data analysis, AI technologies, and AR/VR with CAE simulation technologies, and by supporting the promotion of DX (digital transformation) at development sites, stating that expansion of the DX business is a growth strategy. For example, combining CAE simulation and AI technologies makes possible the provision of new added-value in the design development process, including greatly reducing the time required for analyses and improving accuracy and quality. It has also started to provide new solutions to simplify and support the maintenance work of operations managers through constructing a digital twin environment that links IoT and CAE and combines AR/VR technologies.



Source: Reprinted from materials provided by the Company

Since the start of 2021, the Group has been advancing the following three initiatives. The first is providing more solutions for materials. Specifically, in May 2021, the Company concluded a business alliance with KIGUCHI TECHNICS INC., one of the largest independent materials testing labs in Japan, and began providing total solutions for materials to the manufacturing sector. Amid the international price competition and stronger efforts to promote weight reduction, durability, and response to environmental regulations, there are growing needs to apply scientific technologies to materials data and reduce costs and develop high value-added products, and these is a solution in response to those needs. As a first stage, the Company will provide a service to create and utilize high-quality metals and composite materials property data and realize high-precision simulations. Also, going forward, by strengthening the partnership with KIGUCHI TECHNICS, the Company will build a materials data base exclusively for customers utilizing the materials information management platform that the Company sells, and plans to offer a consulting service in order to select materials.

The second initiative is provision of visualization technology by VR. The Company installed its new technology “method of visualization of results of simulation with virtual reality/mixed reality,” which is patent pending in collaboration with Honda Motor Co., Ltd. <7267>, as an optional function, and began sales in April 2021. Designers can use this tool to perform visual inspections of CAE analysis results in their own VR space, which was formerly difficult to do, and both shortens development periods and improves product quality by reducing rework.

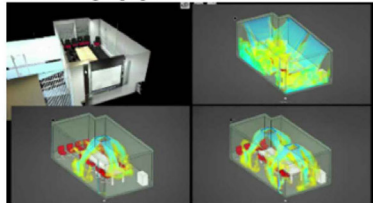
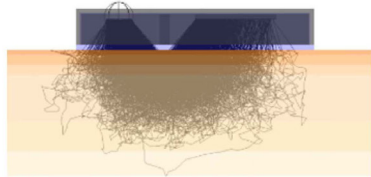
The third initiative is expanding the provision of cloud platforms. The Company is providing a secure and high-performance cloud CAE environment, and has begun providing it in combination with pay-for-use CAE licenses. Customers are able to build CAE environments without large initial costs, and it makes possible efficient research and development by providing an environment which is easy to use and secure.

Medium-term business plan

c) Expanding the use of simulation

In the last few years, in addition to for manufacturing support, simulation technologies have been applied to an increasingly wide range of fields, including weather forecasting, natural disaster measures, life infrastructure like communication and electricity, beauty and medical care. So the Company's policy is to grow sales by actively developing businesses not only for the manufacturing industry, but for fields other than the manufacturing industry as well. As examples of solutions in 2021, the Company implemented a ventilation performance of air conditioning equipment simulation using 3D coordinate data, which is point cloud data, for the construction sector, and developed a solution for the healthcare sector that reduces development time and costs for optical heart rate sensors.

Expanding the use of simulation

| Solution of ventilation performance evaluation with point cloud data | Solution for optical heart rate sensors |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>■ Solution overview</p> <ul style="list-style-type: none"> In environment such as wards and clean rooms for which CAD data does not exist, a CAD model is created based on point cloud data measured by 3D scanning, and ventilation performance simulation related to the arrangement of air conditioning equipment is realized  <p>Modeling and ventilation performance simulation by CAD data created by point cloud data</p> | <p>■ Solution overview</p> <ul style="list-style-type: none"> In design of optical heart rate sensor, cost reduction and time shortening of prototyping are realized by implementation of simulation regarding situation of arriving on light receiving part of light passing through skin tissue  <p>Simulation of light rays passing through skin tissue</p> |

Source: The Company's results briefing materials

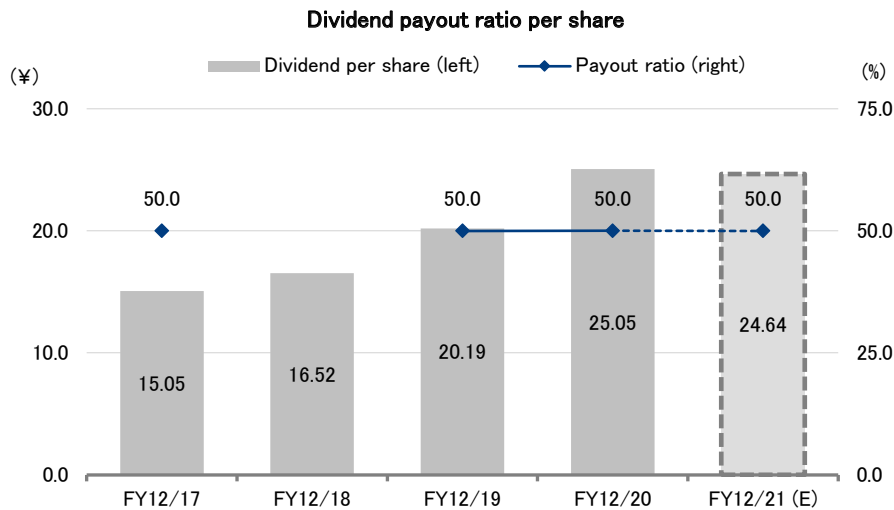
(2) IT Solution Services

In the IT Solution Services business, the Company is working to strengthen the cloud security business. The Company capture the needs for information security response under a remote environment, amid the entrenchment of new work styles such as working from home. As discussed above, net sales of cloud environment security solutions significantly increased by 115.0% YoY in 1H FY12/21, and are expected to continue to grow going forward.

Shareholder return policy

Policy is to pay dividends targeting a high dividend payout ratio of 50% and a high dividend to net assets ratio of 3%

The Company considers the payment of dividends to shareholders to be one of its most important issues. Its basic policy for returning profits to shareholders is to stably and continuously pay dividends, while also working to strengthen and expand the earnings foundation to respond to the rapid developments and changes in the manufacturing industry and to secure internal reserves to prepare for active business development. In addition to this policy, it targets a dividend payout ratio of 50% and a dividend to net assets ratio of 3.0%, both of which are high reference values for determining the dividend amount. It comprehensively determines the dividend amount after considering these reference values and the medium- to long-term investment amount toward improving enterprise value in the future. In FY12/21, the Company plans to pay a dividend per share of ¥24.64, a decrease of ¥0.41 YoY, targeting a dividend payout ratio of 50%.



Source: Prepared by FISCO from the Company's financial results

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