COMPANY RESEARCH AND ANALYSIS REPORT

Daiki Axis Co., Ltd.

4245

Tokyo Stock Exchange First Section

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FISCO Ltd. Analyst
Ken Segawa

FISCO Ltd.
http://www.fisco.co.jp

Index

Summary

Issued green bonds that embody the essence of ESG management

Daiki Axis Co., Ltd. <4245> (hereafter, also "the Company") is committed to its corporate mission statement of "Protect the environment. Change the future." Guided by this corporate mission, the Company aims to continue advancing as an environmental innovation and development company. Under the current three-year medium-term business plan, the Company has adopted "Promotion of ESG management" as a key management theme, and is working specifically to realize six of the United Nations Sustainable Development Goals (SDGs). Over the three-year period through FY12/21, the Company has set plans to increase net sales by 10.4% and operating income by 84.2% compared with FY12/18. To realize the sixth SDG, "Clean Water and Sanitation: Ensure availability and sustainable management of water and sanitation for all," it is accelerating overseas business development in its core business. In the next three years, the Company plans to achieve a 2.6-fold increase in its overseas sales. The Company will push ahead with measures directed at the RE100 initiative for renewable energy. At the same time, it has started developing the renewable energy business in earnest. In this area, the core business pillars are selling power from solar power facilities and the compact wind power equipment business.

1. Results trends

Looking at FY12/19 consolidated results, net sales decreased 1.3% year on year (YoY) to ¥35,749mn, while operating income rose 8.4% to ¥1,000mn. Compared to the forecasts, operating income was ¥200mn, or 16.6%, below forecast. Profit was slowed by losses and related items recorded on a Group-wide basis (¥345mn). For example, losses were recorded on unprofitable projects at LEC Industries Ltd., a consolidated subsidiary engaged primarily in the environmental plant business. On December 31, 2019, LEC Industries and DH Aqua Co., Ltd. were merged with Daiki Axis Co., Ltd. for the purpose of strengthening management and improving efficiency. In FY12/20, excluding the aforementioned special factors and the impact of the novel coronavirus from consideration, the Company is targeting net sales of ¥39,400mn, an increase of 10.2% YoY and operating income of ¥1,400mn, an increase of 39.9%.

2.Issuance of green bonds and the Company's solar power business

At the end of February 2020, the Company issued Daiki Axis Green Bonds, a 10-year green bond. The issued amount was ¥3.0bn. The investment institutions are two local regional banks and Japan's three major megabanks. The procured funds will be used for the solar power business and the compact wind power generation business, which are renewable energy-related businesses undertaken by the Daiki Axis Group. DNV GL Business Assurance Japan K.K., a third-party assessor, assessed the qualifications of Daiki Axis Green Bonds.

In FY12/19, net sales from selling power from solar power facilities rose from ¥172mn in the previous fiscal year to ¥569mn. The difference from forecast was tiny, with net sales only 1.2% below forecast. In FY12/20, net sales from this business is forecast at ¥875mn. In projects to install solar panels on the rooftops of existing stores of DCM Group home centers, 122 sites were linked to the grid as of the end of FY12/19. Panel installation work has been largely completed at 130 sites. If the panels start operating at full capacity in FY12/21, the Company estimates that this business will generate net sales of ¥800mn and operating income of ¥400mn.

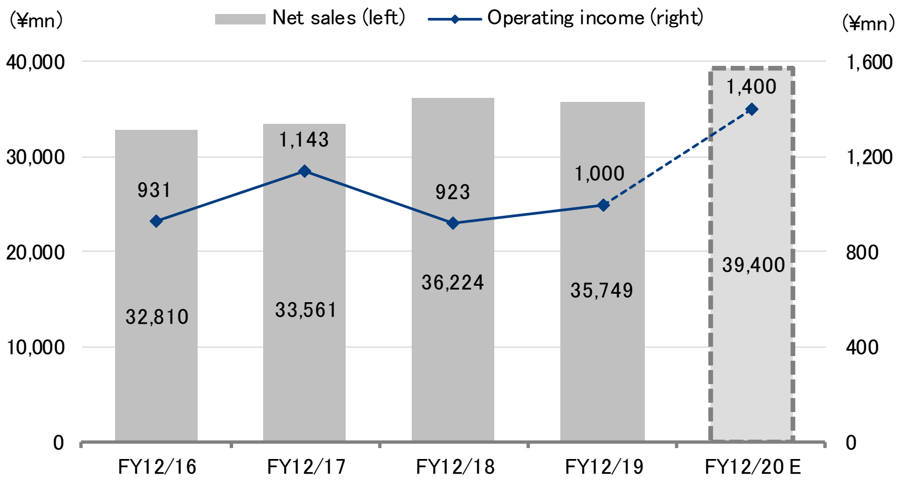
3. Shareholder return policy and shareholder benefit program

The Company's shareholder return policy is premised on a consolidated dividend payout ratio of 30%. In FY12/20, the Company plans to pay an annual dividend per share of ¥24, the same as in FY12/19, for a projected dividend payout ratio of 33.1%. Under the Company's shareholder benefit program, the Company sends an original QUO card worth ¥1,000 to shareholders owning 100 shares (basic unit) or more at period-end. The total return combining dividends and shareholder benefits are set at an attractive level. With an increase in individual shareholders, the number of shareholders had risen to more than 10,256 as of the end of FY12/19, compared with 7,470 as of the end of FY12/18.

Key Points

- Solid trend in FY12/19 business results, with the exception of unprofitable projects and related items (¥345mn)
- The qualifications of Daiki Axis Green Bonds were assessed by a third-party assessor.
- The number of shareholders rose to more than 10,000, reflecting a positive evaluation of the Company's dividend policy and shareholder benefit program.

Results trends



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

Company profile

Promoting ESG management is a priority measure

1. Company profile

The Company seeks to improve the quality of employee lives and contribute to advances in society through steady progress as an environmental innovation and development company. It formulated the Make FOUNDATION Plan, a three-year medium-term business plan that lasts through FY12/21 and aims to promote ESG management. It also retained the existing corporate slogan PROTECT X CHANGE (PROTECT by CHANGE).

In December 2013, the Company newly listed its shares in the chemicals sector of the Tokyo Stock Exchange's Second Section market, and in the following year its listing was upgraded to the Tokyo Stock Exchange's First Section. In March 2019, as part of its measures to enhance corporate governance, it became a company with audit and supervisory committees and introduced an executive officer system.

The Company's FY12/19 results included ¥35,749mn in net sales and ¥1,000mn in operating income. Segment sales shares were environmental equipment business at 51.9%, household equipment business at 41.0%, renewable energy business at 2.0%, and other businesses at 5.1%. Segment operating income and margin results were environmental equipment business at ¥1,068mn and 5.8%, household equipment business at ¥366mn and 2.5%, renewable energy business at ¥256mn and 36.6%, and other businesses at ¥152mn and 8.3%.

2. History

The company began as Ogame Shoji, which sold tiles and hygienic porcelain, in Matsuyama City, Ehime Prefecture, in 1958. It established predecessor Daiki Co., Ltd. in 1964. It started manufacturing aeration Johkasou in 1969. Daiki, which entered the home center business in 1978, formed business alliances with peers Homac Co., Ltd. and Khama Co., Ltd. and decided to merge in 2003. Ahead of the establishment of current DCM Holdings Co., Ltd. <3050> in 2006, Daiki transferred non-home center businesses to Daiki Axis, which was founded as the successor company for those businesses. Capital ties between Daiki Axis and Daiki subsequently ended due to the management buyout (MBO) that established the Company's independence from Daiki, though transactions between the two companies are continuing.

Daiki Axis was officially founded in 2005, but has designed, manufactured, installed, sold, and maintained various wastewater treatment systems over about half a century since the Daiki era when it completed the first fiber reinforced plastic (FRP) Johkasou in 1965. The household equipment business began handling TOTO <5332> products in 1971. Its business scope is limited to the Kinki, Chugoku, and Shikoku areas, where it has become an important distributor for major residential facilities and equipment manufacturers. It also supplies home center retail materials to group companies under DCM Holdings and provides comprehensive store management services, including construction and cleaning of home center stores. In 2018, it launched a solar power business that leases the rooftops of DCM group stores. Additionally, the Company embarked on a compact wind power generation business in 2019.

Through M&A deals and subsidiary establishments, the Company has strengthened the environmental equipment business, developed overseas markets, and entered new areas. M&A deals are being undertaken as a growth strategy. To date, the Company has acquired nine companies in Japan and two companies overseas.

In October 2019, the Company acquired all shares of two companies headquartered in Matsuyama City, Ehime Prefecture and turned them into subsidiaries. The two companies are Fujiwara Reiki Co., Ltd., whose main businesses are the general equipment business for HVAC, plumbing, and electrical systems, as well as the sale of freezers and refrigerators, and Japan Air Solutions Co., Ltd., which performs the installation of the abovementioned HVAC equipment. For the most recent fiscal year (FY4/19), Fujiwara Reiki posted net sales of ¥1,744mn and operating income of ¥55mn. For FY2/19, Japan Air Solutions reported net sales of ¥256mn and operating income of ¥83mn. The Company expects to generate future synergies by, for example, carrying the products of the new subsidiaries and harnessing their client infrastructure. For the subsidiaries, the deal will lead to an expansion of their business areas through the use of the Company's nationwide household equipment wholesale network.

In December 2019, subsidiaries LEC Industries Ltd. and DH Aqua Co., Ltd. were merged with the Company. For both companies, the mergers assumed the form of a simplified and abbreviated merger of wholly owned subsidiaries. LEC Industries had fallen into insolvency. However, with the recording of a provision for loss on business of subsidiaries and associates, no losses were posted on the merger. LEC Industries, which is headquartered in Tokyo, has received many orders for large construction projects. However, some of those projects had become unprofitable in FY12/19. This merger will upgrade LEC Industries' management system to a level on a par with the Company. In addition, LEC Industries' strengths in inorganic wastewater treatment technology will be put to good use within the Group. DH Aqua is headquartered in Matsuyama City, Ehime Prefecture, as is the Company. Efforts will be made to enhance management efficiency at DH Aqua through the merger.

Business overview

Development company placing emphasis on water and the environment

1. Environmental equipment business

The environmental equipment business handles activities ranging from the manufacturing and sales of plastic Johkasou to the design, installation, and maintenance of large concrete wastewater treatment facilities. It covers a wide range of applications from human waste and residential wastewater for individual homes to industrial wastewater and rural wastewater. In addition to wastewater treatment equipment, it has a clean water business that converts underground water to drinking water and wastewater recycling system for reuse of used clean water. It has built maintenance service operations as joint operations with subsidiaries. Consolidated segment sales totaled ¥18,570mn in FY12/19 with 4.7% in the clean water business, 0.8% in recycled water systems, 9.0% in domestic small community Johkasou (for 5-50 persons), 59.0% in wastewater treatment systems and 26.5% in maintenance, etc.

(1) Strength

An important strength is integrated operations covering design, production, installation, sales, and maintenance of wastewater processing facilities. Provision of maintenance services sustains contact with customers and leads to orders for repairs and expansion projects. Knowledge of customer needs confirmed through on-site interaction is also fed back to R&D activities. The Company has maintenance operations with 24-hour monitoring and spot responses and other services that meet customer requirements handled by a dedicated division.

(2) Overseas business

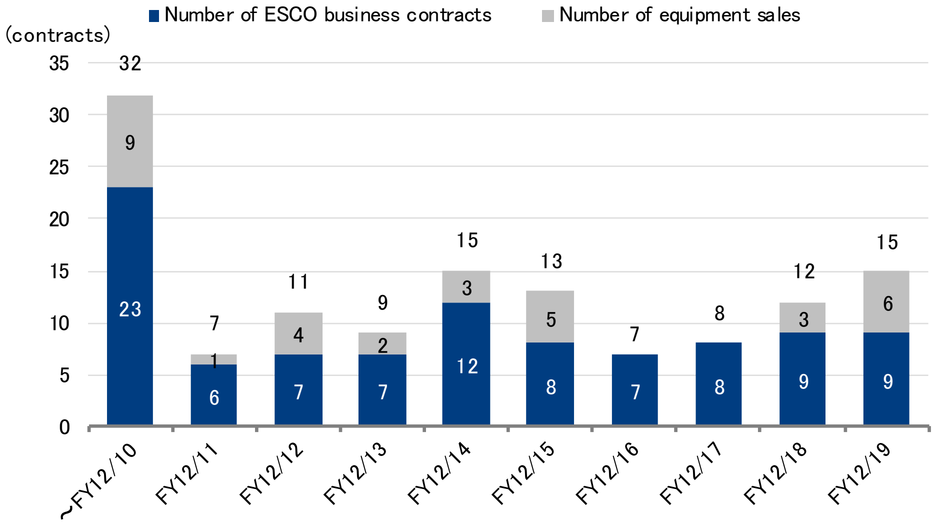
The water infrastructure business consists of three main businesses - materials, parts, and equipment manufacturing; equipment design, assembly, installation, and operation; and business operation, maintenance, and management (water sales). France-based Veolia Water Technologies and SUEZ, US-based GE Water & Process Technologies, and other majors cover all of these areas. Japanese players, meanwhile, specialize in individual areas, such as water treatment equipment, engineering, and organizer. The Company differs from the water majors because it targets smaller wastewater treatment systems. Having the ability to provide the above-mentioned three main businesses enables the Company to differentiate from other Japanese companies. It can handle household wastewater treatment, industrial wastewater treatment, and public water purification.

For the Company, there is the high possibility of obtaining a first-mover advantage with the expansion of the markets for small- and medium-scale wastewater treatment systems in ASEAN, India, and Africa. Under the current three-year medium-term business plan, the Company plans to accelerate growth in net sales in the overseas business to ¥3.0bn, which would represent a 2.6-fold increase over three years.

(3) Clean water business

The clean water business, a new area in the environmental equipment business, is an ESCO service that provides a steady supply of safe low-cost drinking water. This service converts underground water to drinking water and reduces the cost of clean water by 10-30% compared to conventional drinking water. The usage method is exactly the same as clean water from public services with fees charged by usage volume. The Company owns the ESCO clean water facilities. It also installs a remote automated monitoring system that uses IT sensors for 24-hour, 365-day monitoring of facilities operating at customer locations from the headquarters office.

ESCO business contracts and equipment sales



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

ESCO service uses a lengthy contract period of 10 years. This is a recurring income-type income business model in which Contracts with existing customers generate stable income over a lengthy period and new contracts steadily add income. Business is profitable from the first fiscal year of beginning supply at the various sites. The Company currently applies an upper limit of 15 projects a year in light of investment costs and production and installation capabilities. Supply facility depreciation employs the straight-line method. While annual depreciation value is constant throughout the contract period, operating margin rises sharply from the second year because operating expenses are no longer needed. Furthermore, profitability increases dramatically if the contract continues after the 10th year when the depreciation period finishes. The Company began the ESCO business in FY12/06 and is likely to see increase in high-profit projects already done with depreciation. In FY12/19, ESCO system results were nine deployment contracts and six acquisitions. ESCO deployments reached 96 sites at the end of FY12/19. The breakdown by industry is as follows: hospitals at 28 sites, welfare facilities at 15 sites, food processing plants at 14 sites, large commercial facilities and sports gyms at 12 sites each, educational institutions at 8 sites, hotels at 5 sites, bathing facility at 1 site and other at 1 site.

(4) Recurring-income business

The Company handles store Johkasou installations and maintenance and store management tasks (cleaning, fire prevention, electricity, and other inspections) at DCM group stores. It aims to expand bulk orders of wastewater treatment equipment and Johkasou maintenance at major convenience store chains and major restaurant chain stores and their central kitchens. While existing service firms provided coverage in local areas, the Company seeks differentiation by not only lowering costs, but also delivering uniform services on a nationwide scale. Furthermore, provision of maintenance tasks enables it to make timely proposals on renovations and facility addition projects and thereby contributes to a positive cycle.

2. Household equipment business

The household equipment business had a sales breakdown in FY12/19 of construction customers at 71.4%, home center retail materials at 14.8%, and housing facilities projects at 13.7%. The newly established e-commerce (EC) business is in a start-up phase, with net sales of ¥5mn in FY12/19.

In the housing equipment business, the Company seeks to shift from its prior course of stability to a growth trajectory. It will establish a presence in new areas by bolstering sales in regions it has yet to develop, as it captures business opportunities and begins carrying new products in the remodeling market through e-commerce (EC). Efforts will be made to boost profitability by adopting a centralized purchasing system.

3. Renewable energy business

Power sales from solar power facilities has been consolidated into Sylphid Co., Ltd., a consolidated subsidiary that conducts the R&D and sales of compact wind power equipment. In June 2019, Sylphid alleviated its insolvency by conducting a capital increase, capital reduction, and a disposal of surplus. Shikoku Energy Fund, the first natural energy fund of Shikoku Alliance Capital (Matsuyama City), which was jointly founded by four regional banks in Shikoku, provided funding of ¥2.0bn to Sylphid. The form of the issuance was a capital increase through a third-party allotment of shares, the number of shares issued was 800, and the type of shares issued was non-voting preferred shares. The fund duration is 10 years. Sylphid has secured a stable source of income by succeeding to the Company's solar power generation equipment.

(1) Selling power from solar power facilities

The Company began selling power from solar power facilities installed on the rented rooftops of DCM Group stores. The application for the Feed-in Tariff (FIT) long-term fixed purchase price was made on the FY2017 price of ¥21/kWh, although it is ¥18/kWh for some facilities. The number of facilities linked to the grid had increased from 81 at the end of FY12/18 to 122 at the end of FY12/19. The installation work at 130 planned sites has already been completed, and the work will successively shift to connecting the facilities to the grid. In the case of high voltage, grid connection will require nearly six months for some facilities, so it is possible that their full fiscal year contribution will be from FY12/21. Based on sunshine conditions in an average year and in the event of full operations throughout the year, it has been estimated that annual net sales will be ¥800mn and operating income will be ¥400mn. The depreciation period of solar power generation facilities is 20 years (straight-line method), the same as the FIT fixed-price purchase period. Moreover, the Company has formed a budget that provides for the dismantlement cost after 20 years to be allocated over the period. The use of the rooftops of existing stores has allowed the Company to order and install a massive number of solar panels in a short space of time. This, in turn, has enabled the Company to achieve savings in solar panel purchasing and installation costs.

(2) Compact wind power generation

The FIT purchase price for compact wind power equipment with a capacity of less than 20kW will be revised from ¥55/kWh through FY2017 to ¥20/kWh, the same category as 20 kW and above, in FY2018. However, the Company has approximately 8,000 IDs for applications already filed for the FIT purchase price of ¥55/kWh through FY2017. While it will depend on the effective period, the business opportunity will end by July 2022. With solar power systems, the mass production of equipment, installation methods and other aspects have been well established. In contrast, no progress has been made on cost savings for compact wind power generation systems. The investment recovery period for compact wind power generation is roughly twice as long as that of solar power. Accordingly, the Group will work to reduce costs and improve efficiency over the next few years.

In FY12/19, the Group inherited IDs from businesses that had already acquired IDs in Kagoshima Prefecture, and began selling power. Net sales amounted to ¥1mn in FY12/19, and are forecast at ¥10mn in FY12/20. The Group has already received new IDs at 7 sites in Hokkaido and 5 sites in Aomori Prefecture, and plans to begin construction this spring. Going forward, it plans to develop 70 sites nationwide.

The Company promotes compact wind power equipment with a vertical axis format that is more suited to wind conditions in Japan commercialized by Sylphid Co., Ltd. to public entities and companies as auxiliary or independent power sources for public facilities and commercial facilities that provides on-site power, rather than for selling power to the grid. It currently supplies a product with 3kW of power capacity and is also developing a 10kW version that is more useful as well as a scaled-down 1kW version.

4. Other businesses

The other businesses segment posted ¥152mn in operating income and ¥1,837mn in sales in FY12/19, with 32.6% of sales from the residential drinking water business that handles home delivery of bottled water, 64.8% from civil works projects added through the DAD acquisition, and 2.6% from rent income.

Results trends

Solid trend in FY12/19 business results, with the exception of unprofitable projects

1. Overview of FY12/19 results

Looking at FY12/19 consolidated results, net sales decreased 1.3% YoY to ¥35,749mn, operating income rose 8.4% to ¥1,000mn, ordinary income increased 4.9% to ¥1,155mn, and profit attributable to owners of parent decreased 9.1% to ¥782mn. Compared to the forecasts, net sales were 3.1% below forecast, operating income was 16.6% below, ordinary income was 11.1% below, and profit attributable to owners of parent was 2.2% below. Operating income increased YoY owing to efforts to keep down SG&A expenses such as personnel expenses.

Profit attributable to owners of parent decreased mainly because of an initially forecast decline in gain on sales of investment securities under extraordinary income (FY12/18: ¥479mn). A reduction in the effective tax rate helped to reduce the shortfall in profit relative to forecast. With regard to tax expense, following the merger of LEC Industries into the Company, the loss carryforwards held by LEC Industries were used to reduce current income taxes. In addition, because solar power facilities for power sales were transferred to Sylphid Co., Ltd., the Group recorded deferred tax assets against Sylphid's loss carryforwards and reduced its deferred income taxes. As a result, the effective tax rate against profit before income taxes decreased from 42.8% in the previous fiscal year to 21.8%. In the course of starting to sell power from solar power facilities, Sylphid conducted a capital increase through a third-party allotment of shares. This led to the posting of profit attributable to non-controlling shareholders of ¥48mn.

FY12/19 consolidated results

(¥mn)

	FY12/18		FY12/19			YoY		vs. plan
	Results	Ratio to sales	Plan	Results	Ratio to sales	Change	%	
Net sales	36,224	-	36,880	35,749	-	-475	-1.3%	-3.1%
Environmental equipment business	18,513	51.1%	19,272	18,570	51.9%	56	0.3%	-3.6%
Household equipment business	15,812	43.7%	15,056	14,642	41.0%	-1,169	-7.4%	-2.7%
Renewable energy business	287	0.8%	740	699	2.0%	411	143.3%	-5.6%
Other business	1,611	4.4%	1,810	1,837	5.1%	226	14.0%	1.5%
Gross profit	6,887	19.0%	7,665	6,968	19.5%	81	1.2%	-9.1%
SG&A expenses	5,964	16.5%	6,465	5,968	16.7%	4	0.1%	-7.7%
Operating income	923	2.5%	1,200	1,000	2.8%	77	8.4%	-16.6%
Environmental equipment business	1,394	7.5%	1,363	1,068	5.8%	-326	-23.4%	-21.7%
Household equipment business	569	3.6%	473	366	2.5%	-202	-35.5%	-22.5%
Renewable energy business	-65	-22.8%	183	256	36.6%	321	-	39.7%
Other business	97	6.1%	173	152	8.3%	55	56.6%	-12.1%
Adjustment	-1,072	-	-992	-843	-	-	-	-
Ordinary income	1,100	3.0%	1,300	1,155	3.2%	55	4.9%	-11.1%
Profit attributable to owners of parent	861	2.4%	800	782	2.2%	-78	-9.1%	-2.2%

Note: Segment profit margins based on sales values for the respective businesses
Source: Prepared by FISCO from the Company's financial results and results briefing materials

Trends in each business are discussed below.

(1) Environmental equipment business

In the environmental equipment business, net sales increased 0.3% YoY to ¥18,570mn and operating income decreased 23.4% to ¥1,068mn. Due to the completion of large projects for which net losses were posted, profit recorded in the previous fiscal year through the percentage-of-completion method was reversed. Also, in other projects in which outsourcing construction costs are expected to increase, profit forecasts were revised. The shortfall in consolidated operating income relative to the forecast was ¥200mn. The losses declared for some projects (¥345mn) in the environmental equipment business had an impact. For new orders, outsourcing costs were revised to prevent the recurrence of unprofitable projects. Moreover, LEC Industries, the main reason for the losses, was merged with the Company in December 2019, as part of efforts to strengthen management. Overseas (excluding maintenance), net sales remained mostly flat at ¥1,153mn and were 37.2% below forecast. With many large projects, performance was affected by the timing for recording net sales, despite a surge in business inquiries.

(2) Household equipment business

In the household equipment business, net sales decreased 7.4% YoY to ¥14,642mn and operating income declined 35.5% to ¥366mn. Net sales were sluggish on the whole. Net sales to construction customers decreased 5.7% due to a reduction in medium-to-large projects, net sales of home center retail products decreased 5.9% due to lower sales to existing stores, and net sales from housing facilities projects decreased 16.9% due to a reduction in store construction. Lower net sales were mainly responsible for the drop in profits.

(3) Renewable energy business

In the renewable energy business, net sales increased 143.3% YoY to ¥699mn and operating income was ¥256mn, with operating profitability restored from a loss of ¥65mn in the previous fiscal year. Selling power from solar power facilities, specifically solar panels installed on the rooftops of DCM Group stores, contributed positively to business performance.

(4) Other businesses

In other businesses, net sales rose 14.0% YoY to ¥1,837mn and operating income increased 56.6% to ¥152mn. Net sales in the household drinking water business were mostly unchanged from the previous fiscal year, while net sales in civil works rose substantially by 23.6%.

2. Financial position and cash flow

(1) Financial position

Total assets at the end of FY12/19 stood at ¥29,907mn, an increase of ¥2,871mn from the end of FY12/18. Current assets increased by only ¥142mn. Cash and deposits rose ¥1,151mn, while accounts receivable from completed construction contracts (down ¥595mn), costs on construction contracts in progress (down ¥547mn), and other items decreased. Non-current assets increased by ¥2,728mn, reflecting a ¥1,793mn increase in solar power generation equipment. In the liabilities section of the balance sheet, current liabilities decreased by ¥239mn, mainly due to a decline in accounts payable for construction contracts. Non-current liabilities increased by ¥624mn, due to an increase in long-term borrowings for the acquisition of subsidiaries.

Consolidated balance sheet

(¥mn)

	End-FY12/16	End-FY12/17	End-FY12/18	End- FY12/19	Change
Current assets	14,519	15,033	18,763	18,906	142
Cash and deposits	3,430	4,517	6,013	7,165	1,151
Trade receivables	8,329	7,490	9,230	8,562	-668
Inventories	2,206	2,487	2,998	2,573	-424
Non-current assets	5,504	6,592	8,272	11,001	2,728
Total assets	20,023	21,626	27,036	29,907	2,871
Current liabilities	12,302	13,259	18,863	18,624	-239
Non-current liabilities	1,531	1,542	1,454	2,079	624
Interest-bearing debt	6,911	7,546	11,010	11,529	519
Total net assets	6,189	6,824	6,717	9,203	2,485

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

Financial stability ratios were mostly unchanged, with the current ratio at 101.5%, an increase of 2.0 points from the end of FY12/18 and the equity ratio at 23.9%, down 0.9 of a point from a year earlier.

ROE (Return on Equity), a comprehensive management indicator, stayed above 10% for the fourth straight year, at 11.3%. ROE can be analyzed in terms of its three main components: profit margin, asset turnover, and financial leverage. This analysis shows that the Company's total asset turnover is on a declining trend. In the past three fiscal years, total assets rose by 49.4% (¥9,883mn), while net sales only grew by 9.0% (¥2,938mn).

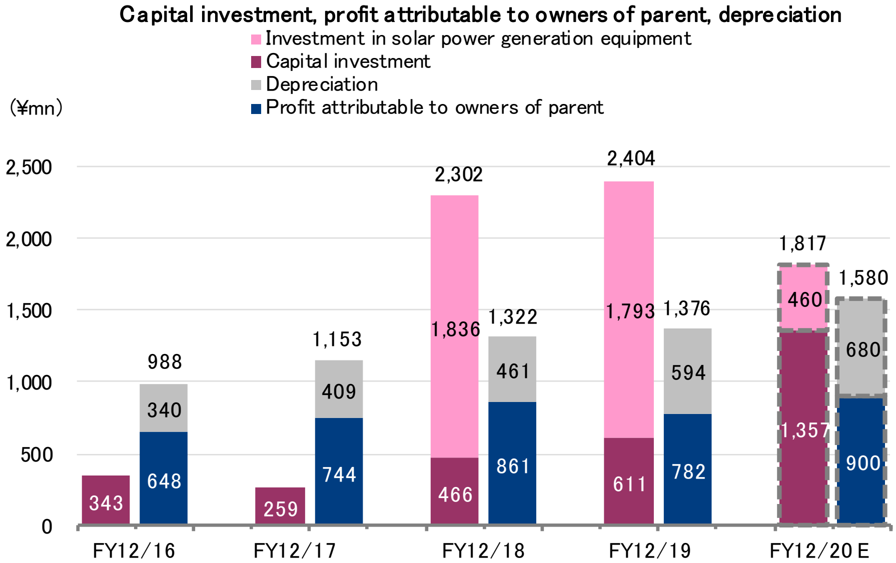
Management indicators and financial ratios

	FY12/16	FY12/17	FY12/18	FY12/19	Change
Profitability					
ROE	10.9%	11.4%	12.7%	11.3%	-1.4
ROA	5.8%	6.4%	4.5%	4.1%	-0.4
Ordinary income margin	3.5%	4.0%	3.0%	3.2%	0.2
Net profit margin	2.0%	2.2%	2.4%	2.2%	-0.2
Total asset turnover rate (times)	1.66	1.61	1.49	1.26	-0.23
Financial leverage (multiple)	3.31	3.20	3.59	4.11	0.52
Stability					
Current ratio	118.0%	113.4%	99.5%	101.5%	2.0
Equity ratio	30.9%	31.6%	24.8%	23.9%	0.9

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

(2) Trends in capital investment

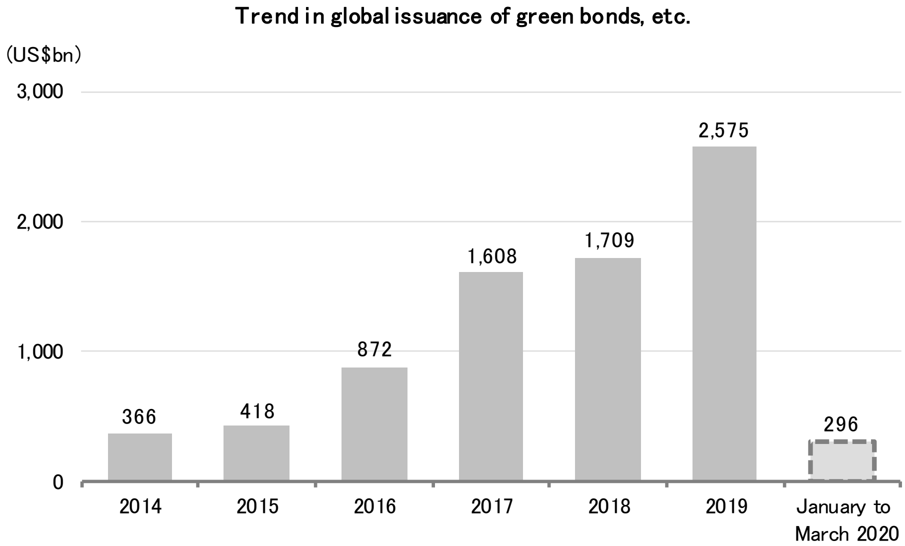
In the past, annual capital investment has either been within the range of cash flows, computed as the sum of profit attributable to owners of parent and depreciation, or slightly above this range. With the start of full-scale development of the renewable energy business, capital investment has expanded significantly from FY12/18. Investment in the solar power business was concentrated in two fiscal years: FY12/18 (investment: ¥1,836mn) and FY12/19 (investment: ¥1,793mn). In FY12/20, capital investment in the solar power business will decline to ¥460mn. There has been no need for new land development because solar power facilities are installed on the rooftops of existing stores of DCM Group home centers. The Group has nearly completed the installation of solar power facilities at 130 sites in a comparatively short space of time. For FY12/20, the forecast for the renewable energy business calls for net sales of ¥1,012mn and operating income of ¥350mn. This means that the operating margin will be 34.6%, indicating a highly profitable business. Selling power from solar power facilities requires very little additional investment or operating costs, and will generate stable income over the long term.



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

(3) Issuance of green bonds

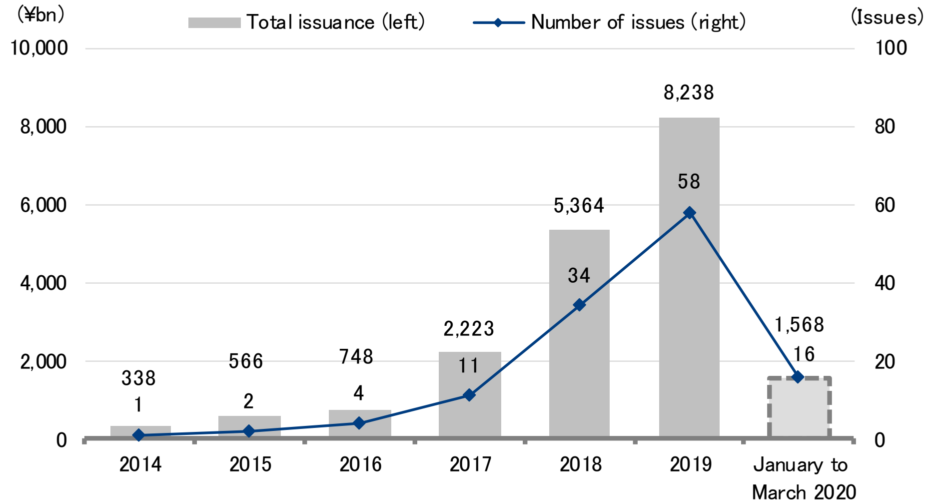
Green bonds are attracting attention as a means of raising funds for environmental projects. Green bonds are debt securities issued for the purpose of raising funds for initiatives to solve environmental issues, such as global warming mitigation measures and renewable energy. In 2019, global green bond issuance rose 50.7% YoY to US$257.5bn, or roughly ¥28tn.



Source: Prepared by FISCO from the Ministry of the Environment website (research by UK-based Climate Bonds Initiative (CBI), an international NGO)

Issuance of green bonds, etc. by Japanese companies and related entities has been gaining momentum since 2017. Aiming to become a Smart City, the Tokyo Metropolitan Government issued Tokyo Green Bonds in 2017. According to statistics compiled by the Ministry of the Environment, the total number of green bond, etc. issues and the amount issued by Japanese companies and related entities was as follows: 11 issues worth ¥222.3bn in 2017, 34 issues worth ¥536.4bn in 2018, and 58 issues worth ¥823.8bn in 2019. In 2020, 16 issues worth ¥156.8bn had been issued as of March. Issuance of green bonds, etc. in 2019 rose 53.6% YoY.

Track record of issuance of green bonds, etc., by Japanese companies and related entities



Note: Foreign currency-denominated bonds issued were converted into yen at the exchange rates of US$1=¥110, €1=¥135, A$1=¥90.
Source: Prepared by FISCO from the Ministry of the Environment website

Daiki Axis Green Bonds are green bonds issued by the Company at the end of February 2020. They are 10-year bonds, and the issued amount was ¥3.0bn. The investment institutions are The Iyo Bank, Ltd. <8385>, The Ehime Bank, Ltd. <8541>, Sumitomo Mitsui Banking Corporation, MUFG Bank, Ltd., and Mizuho Bank Ltd. The procured funds will be used for the solar power business and the compact wind power business within the renewable energy business pursued by the Group. These efforts are part of the Company's ESG management activities, which aim to promote a better environment and achieve a sustainable society. DNV GL Business Assurance Japan assessed the qualifications of the Daiki Axis Green Bonds as a third-party assessor.

(4) Cash flow statement

Cash and cash equivalents increased by ¥1,154mn from the end of FY12/19 to ¥7,124mn. Net cash provided by operating activities was ¥2,401mn. Net cash used in investing activities was ¥2,846mn, mainly due to investment in solar power generation equipment. Net cash provided by financing activities was ¥1,657mn, mainly due to ¥2,000mn in proceeds from share issuance to non-controlling shareholders.

Consolidated cash flow statements

(¥mn)

	FY12/16	FY12/17	FY12/18	FY12/19	Change
Cash flows from operating activities	608	1,867	-105	2,401	2,506
Cash flows from investing activities	-104	-121	-1,402	-2,846	-1,443
Cash flows from financing activities	-451	-634	3,030	1,657	-1,373
Cash and cash equivalents	3,332	4,456	5,969	7,124	1,154

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

Outlook

Forecasting a 10.2% YoY increase in net sales and a 39.9% increase in operating income

For FY12/20, the Company is forecasting net sales of ¥39,400mn, up 10.2% YoY; operating income of ¥1,400mn, up 39.9%; ordinary income of ¥1,500mn, up 29.8%; and profit attributable to owners of parent of ¥900mn, up 15.0%. These forecasts are assumed to be in line with the current medium-term business plan. They are not believed to take into consideration the recent negative impact of coronavirus disease 2019 (COVID-19) on business results.

Operating income is forecast to increase by ¥400mn (after adjustments on consolidation). By business, operating income is projected to increase by ¥516mn in the environmental equipment business, ¥105mn in the housing equipment business, ¥94mn in the renewable energy business and ¥4mn in other businesses. Operating income will be reduced by ¥320mn as a result of adjustments on consolidation. In the environmental equipment business, the Company does not expect a recurrence of the unprofitable projects recorded in FY12/19. It foresees an increase in domestic wastewater treatment systems and expects to generate steady profit from recurring-income business. In the housing equipment business, the Company expects to achieve a general recovery in sales and to incorporate profits from subsidiaries acquired in FY12/19. That said, at the very least, it will be impossible for the Company to avoid the impact in FY12/20 Q1 (January-March) of a shortage in housing equipment products arising from stagnation in global supply chains caused by the impact of COVID-19. This impact will be more significant than that of “the toilet paper shortage issue,” which was based on unfounded rumors. The Company has a long-standing business relationship with TOTO and a strong presence in its business areas of Shikoku and areas of the Chugoku and Kinki regions facing the Seto Inland Sea. For this reason, the Company is expected to be given high priority for receiving the supply of housing equipment products.

Outlook for FY12/20 consolidated results

(¥mn)

	FY12/19		FY12/20		YoY	
	Results	Ratio to sales	Forecast	Ratio to sales	Change	%
Net sales	35,749	-	39,400	-	3,651	10.2%
Environmental equipment business	18,570	51.9%	20,237	51.4%	1,667	9.0%
Household equipment business	14,642	41.0%	16,254	41.3%	1,612	11.0%
Renewable energy business	699	2.0%	1,012	2.6%	313	44.8%
Other business	1,837	5.1%	1,895	4.8%	58	3.2%
Gross profit	6,968	19.5%	8,160	20.7%	1,192	17.1%
SG&A expenses	5,968	16.7%	6,760	17.2%	792	13.3%
Operating income	1,000	2.8%	1,400	3.6%	400	39.9%
Environmental equipment business	1,068	5.8%	1,584	7.8%	516	48.4%
Household equipment business	366	2.5%	471	2.9%	105	28.6%
Renewable energy business	256	36.6%	350	34.6%	94	36.9%
Other business	152	8.3%	157	8.3%	5	3.0%
Adjustment	-843	-	-1,162	-	-	-
Ordinary income	1,155	3.2%	1,500	3.8%	345	29.8%
Profit attributable to owners of parent	782	2.2%	900	2.3%	118	15.0%

Note: Segment profit margins based on sales values for the respective businesses
Source: Prepared by FISCO from the Company's results briefing materials

Medium- to long-term growth strategy

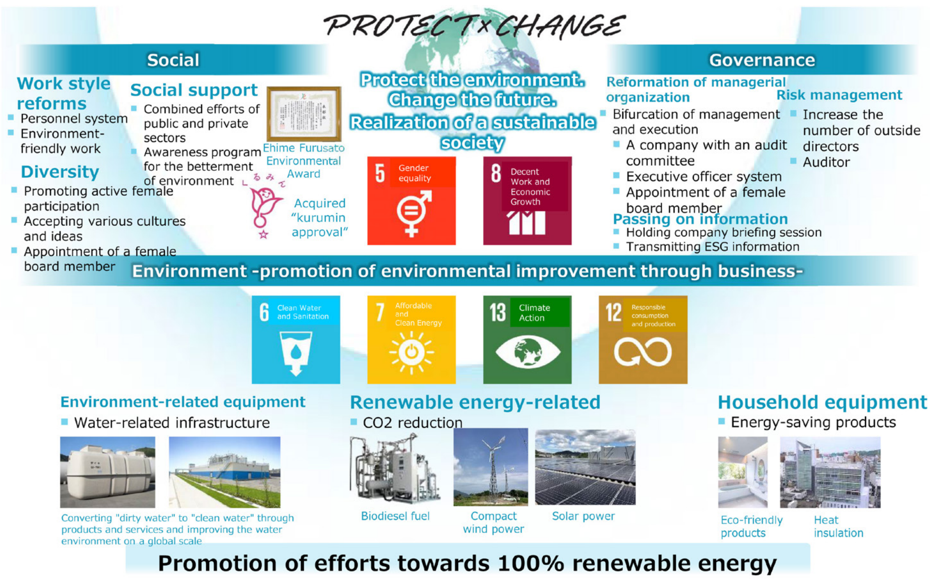
Working to realize 6 SDGs by promoting ESG management

1. Medium-term business plan "Make FOUNDATION Plan - Promoting ESG Management"

Based on results from the previous medium-term business plan “V-PLAN60,” the Company formulated “Make FOUNDATION Plan – Promoting ESG Management,” a three-year business plan lasting through FY12/21. It retained the existing corporate slogan PROTECT By CHANGE and a stance that "the Daiki Axis Group aims to 'protect the environment and change the future' and contributes to improvement in employee lives as well as enhancement of society through continuation of its development as an environmental innovation and development company."

The Company is working to achieve six SDGs by promoting ESG management. For the fifth SDG of “Achieve gender equality,” and the eighth of “Decent work and economic growth,” it is progressing “workstyle reforms” and “diversity” in Society. In its promotion of the activities of women, it has acquired the Kurumin Certification and it has also appointed women to be members of the Board. For the Environment, it is working to realize the sixth SDG of “Ensure availability and sustainable management of water and sanitation for all,” the seventh, “Ensure access to affordable, reliable, sustainable and modern energy for all,” the twelfth, “Ensure sustainable consumption and production patterns,” and the thirteenth, “Take urgent action to combat climate change and its impacts.” To “Ensure availability and sustainable management of water and sanitation for all,” it is building manufacturing bases for wastewater treatment systems in countries with large populations, namely China, India, and Indonesia. For the sales network, in addition to the above three countries, it has concluded sales agency agreements with local companies in Vietnam, Myanmar, and Sri Lanka in Asia, and in Kenya in Africa. In places where a water quality inspection system for wastewater treatment systems and wastewater treatment facilities have not been established, it is lobbying the government administration and others toward the creation of public works projects. Moreover, the Company provides maintenance training and education not only for the staff in its own local companies, but also the staff in agencies. For the twelfth goal, “Ensure sustainable consumption and production patterns,” each business is focusing its efforts on measures like adopting energy-saving products and materials.

Specific measures for ESG



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

The Company has not joined RE100, but it is advancing measures to achieve 100% renewable energy. RE100 is an abbreviation of "Renewable Energy 100%." It is an initiative launched by The Climate Group, an international NGO, in 2014. The companies joining RE100 have set a target to source 100% of the electricity they need in their businesses from renewable sources. As of February 2020, the number of RE100 member companies was 225 globally, including 31 Japanese companies (15 companies as of January 2019). The RE100 initiative will act as a tailwind for the Company's power sales from solar and wind power facilities.

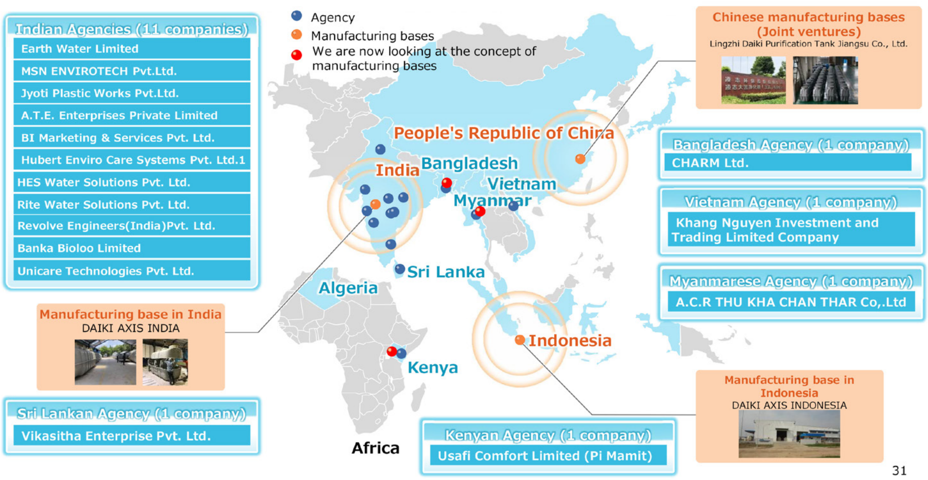
2. Growth strategies and numerical targets

The Company's growth strategies are to rapidly expand its overseas business, which offers prospects for massive demand for infrastructure related to water, and to continue to build up recurring income businesses, such as maintenance and water supply, in Japan.

(1) Overseas business development

The Company is stepping up the shift to overseas local production, increasing cost competitiveness and stimulating demand, with the target of increasing overseas net sales 2.6-fold over three years to ¥3.0bn in FY12/21. The overseas business network comprises three bases in China (two sales bases and 1 manufacturing joint venture base), three bases in Indonesia (1 manufacturing base and 2 sales bases), two bases in India (1 manufacturing base and 1 sales base), one base in Singapore (1 regional headquarters, 1 sales base) and 1 base in Kenya (sales).

Overseas business development



Source: The Company's results briefing materials

a) China

In July 2018, the Company established Lingzhi Daqi Johkaso (Jiangsu) Co., Ltd. as a joint venture to manufacture household combination-treatment wastewater treatment systems. In terms of investment ratios, a local company, Lingzhi Environmental Protection Co., Ltd. (Yixing, Jiangsu) owns 51% and the Company owns 49%, making the joint venture an equity-method affiliate of the Company. In China, much of household wastewater contains edible oils and the living practices are different to those in Japan, such as bathing in a bathtub, so raw water concentrations are high. The Company is expected to develop and introduce wastewater treatment systems that take into consideration local living practices to achieve both low costs and high wastewater treatment capacities.

b) Indonesia

In October 2013, the Company acquired an Indonesian local company (currently, PT. DAIKI AXIS INDONESIA) and made it a consolidated subsidiary, and thereby obtained a beachhead into Southeast Asia. It will construct a new plant in this country, which will expand the production capacity to 5 times the previous level, and at the same time it will progress automation by introducing new equipment and establishing Japanese-levels of product quality, while also improving productivity. In terms of products, since the weather is warm all year-round in Southeast Asia, low-temperature measures are not required, so it is able to narrow down functions and reduced costs. The production capacity will be from 200 to 250 units for each of large-, medium-, and small-sized systems. The Company has participated in large development projects by local Japanese companies, such as condominiums and large retail facilities, and has succeeded in winning new orders for projects such as major automakers' factories and LNG plants. As the Company develops relationships with new agencies and expand its sales channels, it will shift projects from those centered on the large projects of Japanese companies to the projects of local companies.

c) India

With the aim of accelerating business development in India, in August 2019 the Company increased its investment in DAIKI AXIS INDIA PRIVATE LIMITED, a Group company. In April 2017, in India as a whole, the government strengthened the regulation for BOD (Biochemical Oxygen Demand), which expresses the pollution status of water quality, from the previous value of BOD 30 to BOD 10 for commercial facilities of more than 18,000 square meters and residences with a total floor area of more than 2,000 square meters. While enormous demand is being generated for new constructions alone, the regulation also extends to existing facilities. Existing septic tanks cannot meet these strengthened regulations.

In the spring of 2019, the Company provided manufacturing equipment such as metal molds and technological guidance to Jyoti Plastics Works Pvt Ltd., its production subcontractor in India, and it began local production. The production subcontractor is also the Company's agency. The annual production capacity has doubled to 200 units, from 100 units initially. The size of the wastewater treatment systems will correspond to use by 20 to 50 households. The Company has entered into sales agency agreements with 11 companies in India, and in response to the increasing demand, it is considering enhancing the production line, decentralizing plants, and establishing joint ventures.

In September 2019, the Company established a joint venture with one of its agencies, Earth Water Limited. Daiki Earth Water Private Limited Company (the Company's investment ratio, 74%) was established with the aim of developing a wastewater treatment business and Water KIOSK, which is a business to sell drinking water, through BOT*1 and BOO*2 within India. Water KIOSK is a business to install drinking water purification equipment in public facilities, train stations, and other locations, and to sell drinking water for a fee. In addition, the joint venture is working to acquire public projects from local governments in the wastewater treatment systems-related area as well, and if it succeeds with this, the projects are likely to require a fairly large number of wastewater treatment systems.

*1 BOT (Build Operate Transfer) is a method to transfer the ownership of facilities that had been built, maintained, and operated by the private sector to the public after the end of the contract period.

*2 BOO (Build Own Operate) is a method in which facilities had been built, maintained, and operated by the private sector and continue as private-sector facilities even after the end of the contract period, or in which the facilities are dismantled and removed and the business is ended.

d) Other countries

In Myanmar, along with the increase in pollution that has accompanied economic development, the Myanmar government has strengthened regulatory implementation and it has standardized the BOD value, which indicates the degree of pollution in water, as BOD 20. In Yangon, Myanmar's largest city, and Mandalay, a tourist city, it has been made obligatory to install large wastewater treatment facilities and wastewater treatment systems. The Company exports products from Indonesia. In order to respond to steady demand, it is making preparations to establish a subsidiary, Daiki Axis Myanmar Co., Ltd. (provisional name) to realize local production, develop a water quality testing system, and put in place a training and human resources development framework for local subsidiaries' staff and agencies.

In Vietnam, the Company has concluded sales agency agreements with local businesses. In the near term, the Company will export products from Indonesia. In Sri Lanka, the Company has also concluded sales agency agreements with local businesses. The Company has a track record of delivering Japanese wastewater treatment systems to customers, and will strive to increase market visibility by displaying products at exhibitions. In Bangladesh, the Company has received business inquiries from candidate agencies.

In Kenya in Africa, the Company is currently establishing the joint venture DAIKI-USAFI LIMITED (the Company's investment ratio: 51%) to advance the wastewater treatment business based on the BOO method. In Algeria, the Company has a track record of winning projects and delivering products to customers. It has received business inquiries related to new large Japanese plant projects.

(2) Expansion of recurring-income businesses

The Company has set the expansion of recurring-income business as one of its growth strategies. Maintenance net sales have been growing steadily each year, increasing to ¥4,958mn in FY12/19. Under the current medium-term business plan, the Company continues to aim for sustained growth. Bulk orders for the installation and maintenance of wastewater treatment systems are increasing not only from DCM Group stores, but also from major convenience stores and major restaurant chains. All chain stores are required to comply with legal-inspection requirements, but there are concerns about variations in compliance among franchisee stores. The Company has built a new IT system to respond to the needs of these clients. It is working to reduce opportunity loss through consolidating and aggregating daily maintenance reports and providing reports to the chain's headquarters and quick proposals for renovation and facility-expansion work.

(3) Technological capabilities and product development capabilities

The Company is increasing its competitiveness through product development that is highly cost competitive and efficient. In overseas markets, it develops products that are optimized to the water conditions in each country, with the aim of improving quality at the same time as reducing costs. For the domestic market, the Company has reduced costs by reducing parts materials and the number of parts, and by developing highly efficient products through structural changes. DAC2-S, which is a new disposer system for use in multiple-dwelling residential facilities, has greatly improved workability because it has been made more compact. Its total length has been shortened by more than 25% compared to the previous product to 6.4 m, which is the smallest size in the industry. In July 2019, the Company released the XH model as the standard model for household-use, advanced treatment-type wastewater treatment systems. The XH model realizes benefits such as a highly reliable and stable wastewater treatment performance, lower main body weight, highly efficient maintenance and management, reduced maintenance and inspection work, and easier cleaning. Launched in March 2019, the XF model was developed as a new household wastewater treatment system for areas with phosphorous restrictions.

(4) Numerical goals

Consolidated FY12/21 numerical goals in the plan are ¥40,000mn in sales (+10.4% vs. FY12/18's result), ¥1,700mn in operating income (+84.2%), at least 13.2% in ROE (vs. FY12/18's 12.7%), and at least 5.5% in ROIC (vs. 4.2%). Segment sales goals are environmental equipment business at ¥20,770mn (51.9% of overall sales; +12.2% vs. FY12/18 results), household equipment business at ¥16,266mn (40.7%; +2.9%), and renewable energy and other businesses at ¥2,963mn (7.4%; +56.1%). The plan targets ¥3,000mn in overseas sales (7.5%; +160.0%).

Goals in the new medium-term business plan
"Make FOUNDATION Plan - Promoting ESG Management"

(¥mn)

	FY12/18		FY12/21		Compare to FY12/18	
	Results	Ratio to net sales	Plan	Ratio to sales	Change	%
Net sales	36,224	100.0%	40,000	100.0%	3,775	10.4%
Environmental equipment business	18,513	51.1%	20,770	51.9%	2,257	12.2%
(Overseas sales portion)	1,153	3.2%	3,000	7.5%	1,846	160.0%
Household equipment business	15,812	43.7%	16,266	40.7%	453	2.9%
Renewable energy business, other business	1,899	5.2%	2,963	7.4%	1,064	56.1%
Operating income	923	2.5%	1,700	4.3%	776	84.2%
Ordinary income	1,100	3.0%	1,800	4.5%	699	63.5%
Profit attributable to owners of parent	861	2.4%	1,100	2.8%	238	27.7%
ROE	12.7%		13.2% At least		0.5pt At least	
ROIC	4.2%		5.5% At least		1.3pt At least	

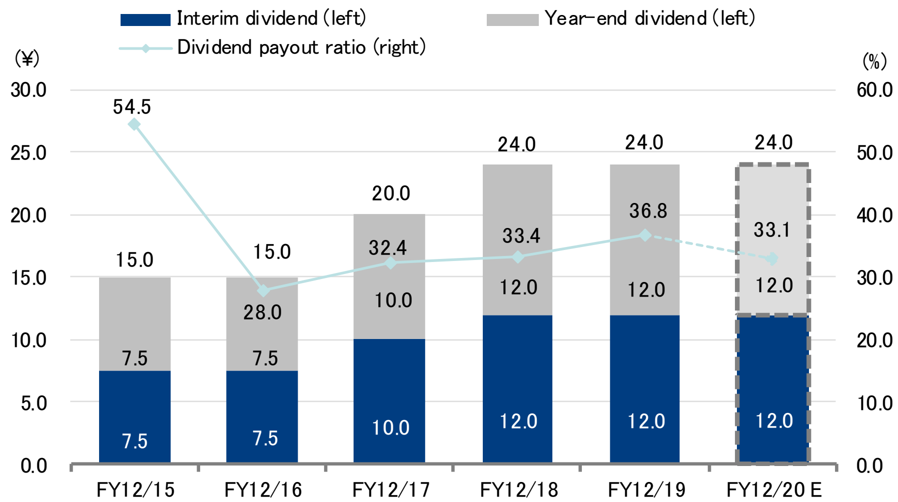
Source: Prepared by FISCO from Company materials

Shareholder return policy

The number of shareholders rose to more than 10,000, reflecting a positive evaluation of the Company's dividend policy and shareholder benefit program

The Company's shareholder return policy is premised on a consolidated dividend payout ratio of 30%. In FY12/19, the Company paid an annual dividend per share of ¥24, the same as in FY12/18, for a 36.8% dividend payout ratio. In FY12/20, the Company plans to continue paying an annual dividend per share of ¥24 (interim dividend of ¥12), for a projected dividend payout ratio of 33.1%. Under the Company's shareholder benefit program, which was introduced in FY12/16, the Company sends an original QUO card worth ¥1,000 to shareholders owning 100 shares (basic unit) or more at period-end. The total return combining dividends and shareholder benefits are set at an attractive level. With an increase in individual shareholders, the number of shareholders had risen to more than 10,256 as of the end of FY12/19, compared with 7,470 as of the end of FY12/18.

Dividend per share (after the split) and dividend payout ratio



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

Information security measures

As information security measures, the Company has developed information infrastructure facilities and constantly runs system operation and management software and monitors and restricts security. For employees, it has formulated an information security policy and seeks to raise awareness. Security education is given to all employees each year through e-learning and security measures are making inroads in the organization.

Disclaimer

■ For inquiry, please contact: ■
FISCO Ltd.
5-11-9 Minami Aoyama, Minato-ku, Tokyo, Japan 107-0062
Phone: 03-5774-2443 (Financial information Dept.)
Email: support@fisco.co.jp