COMPANY RESEARCH AND ANALYSIS REPORT

MEIKO NETWORK JAPAN CO., LTD.

4668

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Summary

Is building a business foundation toward the regrowth of the Meiko Gijuku business from FY8/20 onwards

MEIKO NETWORK JAPAN CO., LTD. <4668> (hereafter, also “the Company”) offers a variety of educational services centered on the direct and franchise operations of the Meiko Gijuku private tutorial schools, but also medical-related preparatory schools, soccer schools, after-school care, and Japanese language schools for overseas students. Its strengths include its expertise in franchise operations and the Company is aiming to become a top company in human development while expanding business domains with M&A activities.

1. FY8/19 3Q cumulative results

Sales and profits increased in the FY8/19 3Q cumulative period (September 2018 to May 2019) consolidated results, with net sales rising 3.5% year-on-year (YoY) to ¥14,051mn and operating income growing 34.4% to ¥893mn. The main factor for the increase in net sales was ¥996mn from the inclusion of franchise operations management companies in the Meiko Gijuku business, with the consolidation of K. Line Co., Ltd. in the previous 4Q and K.M.G. Corporation Co., Ltd. (hereafter, KMG) in the current 3Q. Conversely, consolidation of these two companies resulted in a reduction in operating income of ¥81mn, including amortization of goodwill. But overall, operating income still grew by double digits due to the reduction in sales promotion expenses. At the end of FY8/19 3Q, the number of schools in the Meiko Gijuku business (including franchise schools) was 1,946 schools, down 4.2% on the end of the previous fiscal year, while the number of enrolled students also continued to decline, down 4.1% to 98,438 students. However, the average number of students per school changed direction and increased, if only slightly, up 0.1% to 50.6 students.

2. FY8/19 outlook

The Company has left its initial forecasts unchanged for the FY8/19 consolidated results with net sales to increase 6.3% YoY to ¥20,320mn and operating income to rise 29.0% to ¥1,860mn. Consolidation of K. Line and KMG is expected to increase net sales from ¥1.2bn to ¥1.3bn, but decrease operating income by tens of millions of yen. In order to achieve the forecasts, the Company will need to increase net sales by 13.1% YoY and operating income by 24.4% in FY8/19 4Q. It seems the Company is aiming to achieve its forecasts by strengthening recruitment of new students and summer learning courses in July and August.

3. Measures aimed at rebuilding the Meiko Gijuku business

In order to recover the Meiko Gijuku business, in which performance results have continued to decline since FY8/16, the Company has been introducing MEIKO Style Coaching,* a new learning guidance method, as a strategy to differentiate itself from its competitors. It started to introduce it into directly operated schools from the fall of 2017, and it then introduced it into all schools, including franchise schools, from April 2019. Further, it is enhancing learning courses that utilize ICT and improving the quality of services, including by increasing the frequency it holds training seminars to improve educational abilities and implementing marketing measures tailored to regional characteristics. It is progressing the scrap & build of schools, and therefore as a whole the number of schools and the number of students may continue to trend downward. But profitability is recovering from the increase in the number of students per schools, and the Company's policy is to establish the foundation on which to achieve regrowth from FY8/20 onwards.

* MEIKO Style Coaching is a learning system that effectively improves students' academic performance through combining "review lessons" and an e-portfolio system (Meiko e-Po). "Review lessons" are a learning guidance method that raises students' understanding capabilities during learning through the tutor giving them hints, and the students then solving problems using their own capabilities and explaining what they have understood in their own words to the tutor, and recording this in review notes. Meiko e-Po is a dedicated app in which students record information, such as learning records and plans, and the parents and guardians can use their smartphones to check on their children's learning status and academic performance at any time.

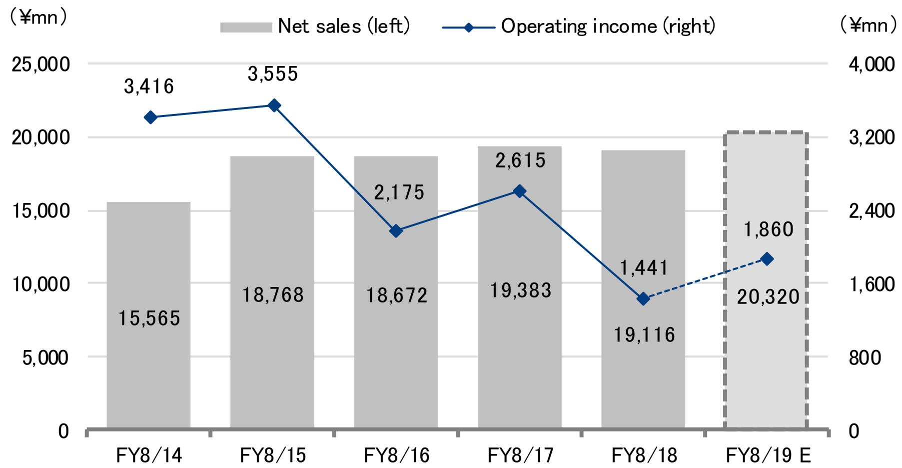
4. Shareholder return policy

There has been no change to the Company's policy of actively returning profits to shareholders. The FY8/19 dividend per share will be ¥30 (dividend payout ratio, 78.1%), down ¥12 YoY, which will be the first decrease since the Company was listed. However, the Company has set 80% as the target standard for the dividend payout ratio. There have also been no changes to the shareholder benefit program, in which the Company gives QUO cards worth ¥1,000 to ¥5,000 to shareholders as of the end of August, according to the number of shares they hold and the length of time that they have held them. The gross investment yield per share unit, including the shareholder benefit program, is at the 4-6% level at the current share price (¥973 as of July 12, 2019).

Key Points

- In the FY8/19 3Q results, achieved a double-digit increase in profits from the reduction in sales promotion expenses
- The declines in the number of schools and the number of students in the Meiko Gijuku business may bottom-out in FY8/20
- Although its record of increasing dividends will end for the time being, the Company will maintain an active shareholder return policy

Results trends



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

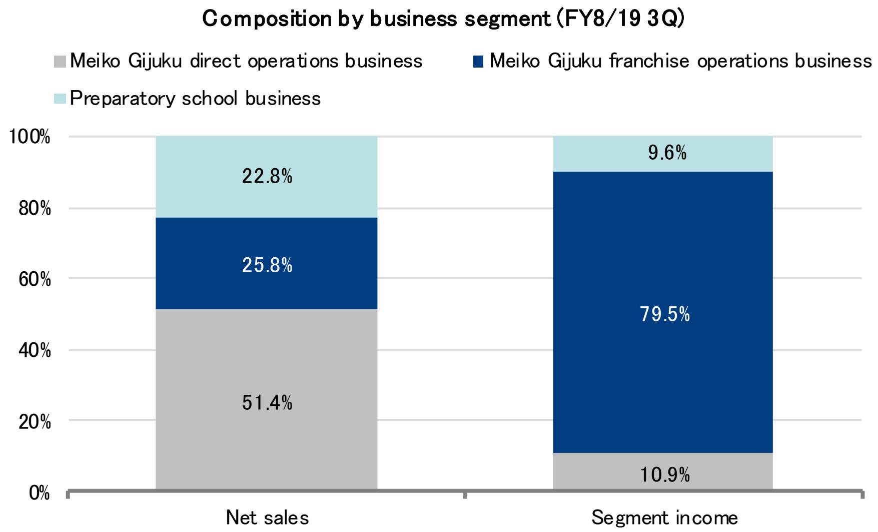
Business overview

Aiming to become a top company in human development through the mainstay Meiko Gijuku business and expanding into other educational services

Based on its educational philosophy of human development through independent learning, the industry leader in private tutorial schools primarily operates the Meiko Gijuku business (direct and franchise operations). The Company is also actively expanding into other businesses related to educational services, aiming to become a top company in human development. Specifically, it operates the Meiko Soccer Schools, soccer schools for children; Waseda Academy Kobetsu schools, which provide tutorial instruction to junior high school and high school students seeking entry into prestigious high schools and universities; and Meiko Kids Schools, which provide nursery care for pre-school children and after-school care for elementary school children. Additionally, its subsidiaries operate Tokyo Ishin Gakuin, preparatory schools that specializes in the medical university field, and Waseda EDU Japanese language schools and JCLI Japanese language schools as schools that cater to overseas students learning Japanese. Other businesses include subsidiary Kotoh Jimusho Co., Ltd., which operates businesses related to university education and exams; subsidiary Youdec Co., Ltd., which publishes an exam information magazine, produces mock exam questions, sells educational materials, and offers private instruction to students at their schools; and Youdec's subsidiary Koyo Shobo Co., Ltd., which is involved in the academic publishing business.

In overseas businesses, the mainstay Company operates a nursery school for Japanese residents in Singapore (non-consolidated subsidiary COCO-RO PTE LTD) and has invested in NEXCUBE Corporation, Inc. (equity-method affiliate; 23.7% stake), which operates private tutorial schools in South Korea, and Taiwan-based Meiko Bunkyo (affiliated company not accounted for by the equity method; 25% stake), which operates the Meiko Gijuku business in Taiwan.

Looking at the percentages of results by business segment in FY8/19 3Q, the Meiko Gijuku business (including direct and franchise operations) served as the main business, providing 77.2% of net sales and 90.4% of segment income. In the preparatory school and other businesses, high percentages of sales and profits are provided by the Japanese language school, school-support and academic publishing businesses.



* Segment income/loss is before the deduction of corporate expenses.
Source: Prepared by FISCO from the Company's financial results

Business performance

In the FY8/19 3Q results, achieved a double-digit increase in profits from the reduction in sales promotion expenses

1. Overview of FY8/19 3Q results

In FY8/19 3Q consolidated results announced on July 11, net sales increased 3.5% YoY to ¥14,051mn, operating income rose 34.4% to ¥893mn, ordinary income rose 29.1% to ¥978mn, and net income attributable to owners of the parent was up 68.9% to ¥461mn. This was the first increase in both sales and profit on a 3Q cumulative basis in two years.

Net sales increased, because even though sales declined in the Meiko Gijuku franchise operations business and the preparatory school and other businesses, they grew in the Meiko Gijuku direct operations business due to franchise operations management companies being made subsidiaries. The consolidated results now include the results of K. Line (which manages 41 schools in the Tokyo, Kanagawa, and Tokai areas) after it was made a subsidiary in the previous 4Q, and KMG (which manages 43 schools in the Kyoto, Shiga, and Nara areas) after it was made a subsidiary in the current 3Q, which caused net sales in the Meiko Gijuku direct operations business to increase ¥996mn.

Conversely, in costs, the cost of sales increased 5.4% YoY mainly due to the rise in personnel expenses (including the increase on making K. Line and KMG subsidiaries), while SG&A expenses fell 7.6%. Looking at the factors causing SG&A expenses to change, amortization of goodwill increased ¥50mn alongside K. Line and KMG being made subsidiaries, but sales promotion expenses decreased approximately ¥400mn. In FY8/18 3Q, the level of sales promotion expenses was higher than in a typical year due to the brand renewal, but in FY8/19, it has returned to the same level as usual. The monetary effect of K. Line and KMG being made subsidiaries was to decrease operating income by ¥81mn, including due to the amortization of goodwill.

In the mainstay Meiko Gijuku business (including franchise schools), at the end of FY8/19 3Q the number of schools had declined 4.2% on the end of the previous fiscal year to 1,946 schools, while the number of enrolled students also continued to trend downward, falling 4.1% to 98,438 students. However, the average number of students per school changed direction and increased for the first time in 14 fiscal period, up 0.1% to 50.6 students. The main reason for the improvement was the progress made in the scrap & build of schools. Also, the rate of decrease in the number of students is steadily contracting, bottoming-out at a decline of 7.1% in the current 1Q and then improving to declines of 6.2% in 2Q and 4.1% at the end of 3Q, and it is also expected to recover even more in the future. Total system-wide sales fell 3.5% YoY, while the sales unit price per student rose slightly. Courses utilizing ICT, including Meiko Mirai Eigo for elementary school students, Meiko Chugaku Listening for junior high school students, and English learning courses, such as the course to prepare students for the English proficiency test, have been favorably received, which would seem to have led to the rise in the sales unit price per student.

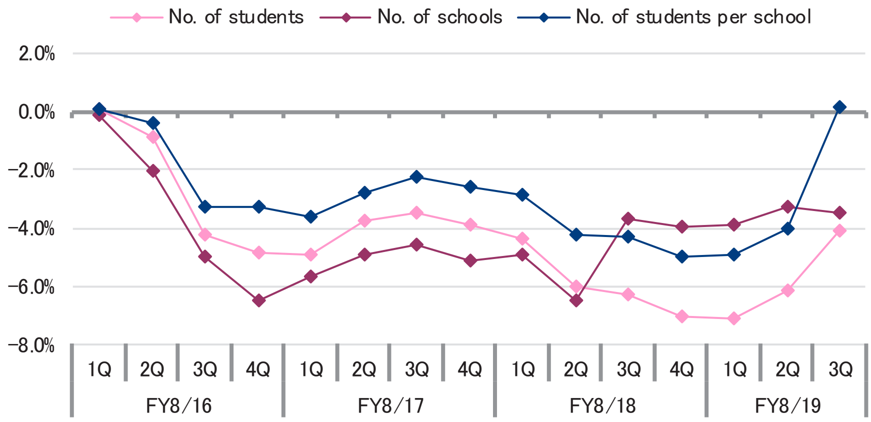
Consolidated FY8/19 3Q results

(¥mn)

	FY8/18 3Q cumulative		FY8/19 3Q cumulative		
	Results	% of sales	Results	% of sales	YoY
Net sales	13,573	-	14,051	-	3.5%
Cost of sales	9,517	70.1%	10,027	71.4%	5.4%
SG&A expenses	3,390	25.0%	3,131	22.3%	-7.6%
Operating income	664	4.9%	893	6.4%	34.4%
Ordinary income	757	5.6%	978	7.0%	29.1%
Net income attributable to owners of parent	273	2.0%	461	3.3%	68.9%
Number of Meiko Gijuku schools, number of enrolled students, and total system-wide sales (direct and franchise operations)					
Number of schools (end of 3Q) (schools)	2,032		1,946		-4.2%
Number of students (end of 3Q) (students)	102,645		98,438		-4.1%
Number of students per school (end of 3Q)	50.5		50.6		0.1%
Total system-wide sales (¥mn)	29,691		28,643		-3.5%

* Total system-wide sales = the sum of 1) total sales of directly operated schools, including lesson fees, fees for educational materials, and test fees, and 2) total sales of franchise operations including lesson fees. Fees for educational materials, tests, etc., at franchise operations are not included. Does not include teaching materials costs, test fees, etc. for franchise schools.
Source: Prepared by FISCO from the Company's financial results

Rates of change in the number of Meiko Gijuku students and schools compared to the end of the previous fiscal year



(as of the end of period)

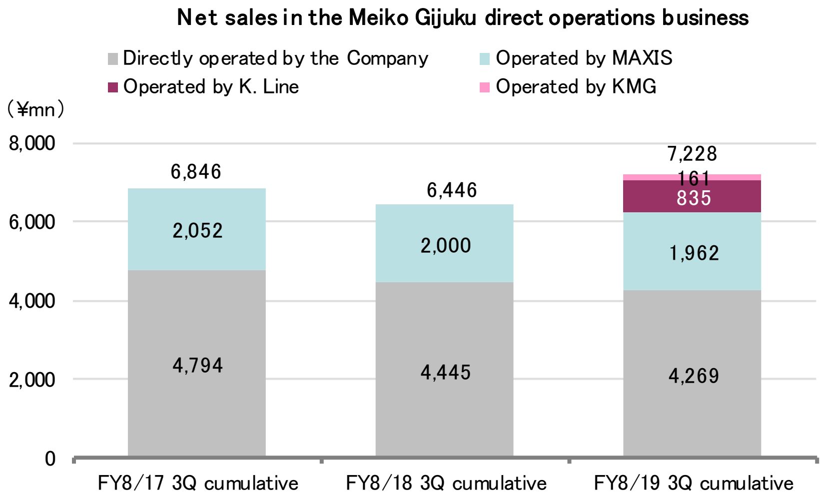
Source: Prepared by FISCO from the Company's financial results

The decline in the number of students per school has been halted in the Meiko Gijuku business, and earnings continue to grow in the Japanese language school and kids school businesses

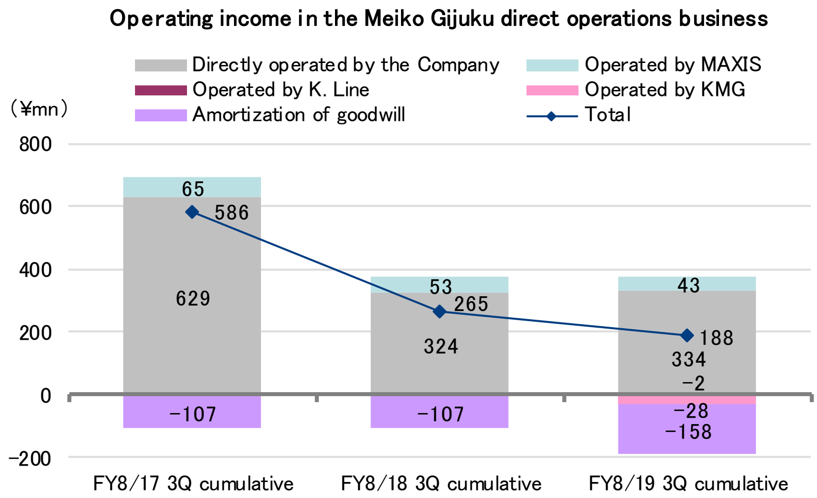
2. Segment trends

(1) Meiko Gijuku direct operations business

In the FY8/19 3Q cumulative period in the Meiko Gijuku direct operations business, net sales increased 12.1% YoY to ¥7,228mn, but segment income decreased 29.0% to ¥188mn. K. Line and KMG being made subsidiaries caused net sales to rise ¥996mn but operating income to fall ¥81mn. Looking on an existing-business basis after excluding this factor, net sales decreased 3.3% YoY and segment income increased 1.3%. Also, the amortization of goodwill rose ¥50mn to ¥158mn.



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



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

Looking by company, in the Company's direct operations business, sales decreased but profits increased, with net sales falling 4.0% YoY to ¥4,269mn and operating income rising 3.1% to ¥334mn. Sales declined mainly due to the fall in the number of students, but the Company progressed the scrap & build of schools (a reduction of 13 schools on the end of the previous fiscal year) and worked to keep down fixed costs and other costs, which lead to the rise in profits. However, in the subsidiary MAXIS Education Co., Ltd., (hereafter, MAXIS), net sales decreased 1.9% to ¥1,962mn and operating income declined 18.9% to ¥43mn. At the end of FY8/19 3Q, the number of students had risen 3.0% on the end of the previous fiscal year, which was the first increase in 13 fiscal periods. However, the main reasons for the lower sales and profits were the sluggish performance of the winter learning courses and the decline in the percentage of junior high school students who take many classes. In K. Line, net sales were ¥835mn and the operating loss was ¥2mn, while in KMG, net sales were ¥161mn and the operating loss was ¥28mn. Although both companies recorded operating losses, the impact of seasonality on their results is significant (their earnings are concentrated in 2Q and 4Q) and they are expected to be profitable for the full fiscal year. Incidentally, looking at the operating income margin by company in 3Q (March to May 2019), the Company was -20.7%, MAXIS was -23.3%, K. Line was -20.4%, and KMG was -17.4%.

Number of directly operated schools and number of students

	Directly operated by the Company			Operated by MAXIS			Operated by K. Line			Operated by KMG		
	FY8/18 3Q	FY8/19 3Q	Change	FY8/18 3Q	FY8/19 3Q	Change	FY8/18 3Q	FY8/19 3Q	Change	FY8/18 3Q	FY8/19 3Q	Change
Number of schools (end of 3Q) (schools)	234	221	-5.6%	93	92	-1.1%	-	41	-	-	43	-
Number of enrolled students (end of 3Q) (students)	13,936	13,719	-1.6%	5,618	5,787	3.0%	-	2,397	-	-	1,944	-
Average number of students per school (students)	59.6	62.1	4.2%	60.4	62.9	4.1%	-	58.5	-	-	45.2	-

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

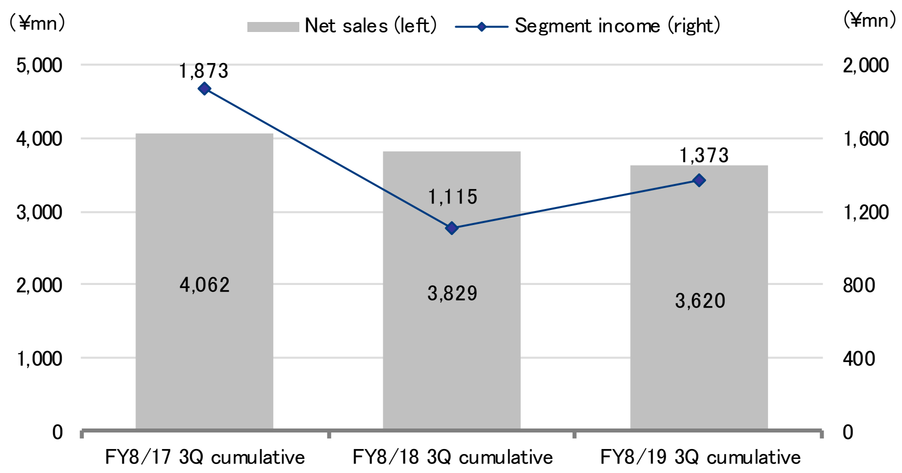
Looking at the end of FY8/19 3Q, indicators have been improving every fiscal quarter, as the average number of students per school for schools operated by the Company and MAXIS have changed direction and increased, and the number of enrolled students at MAXIS schools has also changed direction and is increasing rapidly. Although the effects from introducing MEIKO Style Coaching have been limited, it is considered that the effects of marketing and other measures that are tailored to regional characteristics are gradually starting to appear.

(2) Meiko Gijuku franchise operations business

In the FY8/19 3Q cumulative period in the Meiko Gijuku franchise operations business, net sales declined 5.4% YoY to ¥3,620mn, but segment income increased 23.1% to ¥1,373mn. In addition to the impact of K. Line and KMG being made subsidiaries, the main factors behind the fall in sales were the declines in other franchise schools and student numbers. On the other hand, operating income increased mainly due to the reduction in sales promotion expenses.

At the end of FY8/19 3Q, the number of schools was down 9.1% on the end of the previous fiscal year to 1,549 schools (down 4.2% when including K. Line and KMG), the number of enrolled students decreased 10.2% to 74,591 students (down 5.0%), and the average number of students per school decreased 1.2% to 48.2 students (down 0.8%). In particular, compared to the end of the previous fiscal quarter, the number of schools was down 72 schools (including K. Line and KMG). This is a significantly more than the decline of 33 schools compared to the end of the same period in the previous fiscal year, and we can see that the decrease in the number of schools is directly linked to the decline in the number of students. In terms of the timings of the school closures, in a typical year there are many closures in March, the end of the fiscal year, so the peak is in the Company's 3Q. From FY8/16 onwards, the continued decrease in the number of students per school and the increase in the number of unprofitable schools seem to have led to the decline in the number of franchise schools. Therefore, first, the most important task is recovering the number of students per school. Toward this, in April 2019, the Company introduced MEIKO Style Coaching at all schools, and it is also conducting student recruitment activities that are tailored to regional characteristics and enhancing the support centers. Although the effects of these measures have not yet appeared in the numerical results, at schools operated by the Company's and MAXIS, where the measures were implemented in advance, the numbers of students per school have changed direction and are increasing, and it is expected that the same effect will start to appear in each of the franchise schools as well.

Meiko Gijuku franchise operations business



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

Number of franchise schools and enrolled students

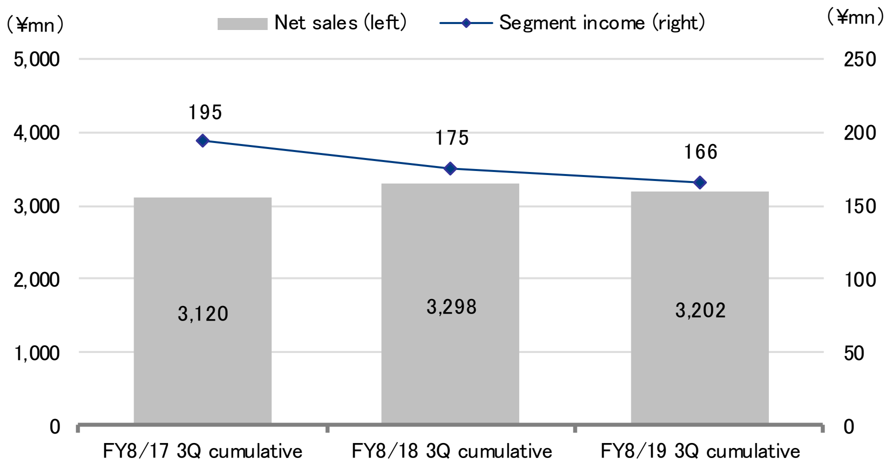
	FY8/18 3Q	FY8/19 3Q	Change	FY8/19 3Q*	Change
Number of schools (end of 3Q) (schools)	1,705	1,549	-9.1%	1,633	-4.2%
Number of enrolled students (end of 3Q) (students)	83,091	74,591	-10.2%	78,932	-5.0%
Average number of students per school (students)	48.7	48.2	-1.2%	48.3	-0.8%

* Includes schools operated by K. Line and KMG
Source: Prepared by FISCO from the Company's financial results

(3) Preparatory school and other businesses

In the FY8/19 3Q cumulative period in the preparatory school and other businesses, net sales decreased 2.9% YoY to ¥3,202mn and segment income declined 5.4% to ¥166mn. Sales and profits declined because although results are steadily expanding in the Japanese language school and kids school businesses, they slumped in the preparatory school, school-support and academic publishing businesses. The results trends by business are as follows.

Preparatory school and other businesses



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

The FY8/19 3Q cumulative period results in the preparatory school and other businesses

(¥mn)

	Net sales	YoY	Operating income	YoY	Note: Figures in parentheses are YoY increases/ decreases
Japanese language schools	1,017	3.7%	81	28.6%	No. of students 1,494 (+73)
School-support and academic publishing businesses	1,084	-11.5%	109	-55.1%	Results were strong in Kotoh Jimusho, but weak in Youdec and Koyo Shobo
Preparatory schools	276	-11.9%	-28	-	No. of schools 2 (-1), No. of students 62 (-17)
Waseda Academy Kobetsu schools	375	2.7%	-8	-	No. of schools 35 (±0), No. of students 2,435 (+224)
Kids schools	267	30.2%	6	-	No. of schools and consignment operations 25 (+6), No. of students 1,122 (+153)
Soccer schools	103	-1.0%	8	700.0%	No. of schools 14 (+1), No. of students 873 (+23)
Other	80	-23.9%	-2	-	MAXIS (English schools), study clubs, etc.
Total	3,202	-2.9%	166	-5.4%	

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

a) Japanese language school business

In the Japanese language school business for overseas students, net sales increased 3.7% YoY to ¥1,017mn and operating income rose 28.6% to ¥81mn. This business consists of two chains of schools, the Waseda EDU Japanese language schools managed by consolidated subsidiary Waseda EDU and the JCLI Japanese language schools managed by Kokusai Jinzai Kaihatsu Co., Ltd. At the end of FY8/19 3Q, the total number of students in the two schools was up 5.1% on the end of the previous fiscal year to 1,494 students and is continuing to steadily increase. In addition to this increase in the number of students, the main reason for the higher profits was the absence of relocation expenses recorded in the previous fiscal year. As amortization of goodwill of ¥127mn was recorded, the operating income margin before the amortization of goodwill, which indicates actual profitability, was approximately 20%, and this is a highly profitable business.

The Immigration Bureau has made visa issuance stricter, and there were concerns about the impact that this would have on the number of new students in April 2019. But in the Company, although the number of enrolling students from some countries, such as Sri Lanka and Myanmar, decreased, this was covered by the increases from China and Vietnam, so overall its impact was limited. Although this issue will strengthen the check system for overseas students in Japan, there has been no change to the underlying trend of the increase in demand for Japanese language schools. So the Company's policy is to expand this business by strengthening services in the future not only for Japanese language education, but also for providing guidance for continuing on into higher education.

b) School-support and academic publishing businesses

In the school-support and academic publishing businesses, net sales decreased 11.5% YoY to ¥1,084mn and operating income declined 55.1% to ¥109mn. At the consolidated subsidiary Kotoh Jimusho, inquiries were solid, such as for university entrance exam assessments and sample questions. But at Youdec, there was a decline for mock entrance exam services and in Koyo Shobo, the number of new publications decreased, and these weak results impacted the results as a whole.

c) Preparatory school business

In the preparatory school business, which is conducted by the consolidated subsidiary Tokyo Ishin Gakuin Co., Ltd., net sales decreased 11.9% YoY to ¥276mn and operating loss was ¥28mn (compared to operating loss of ¥36mn in the same period in the previous fiscal year). Regarding medical-related preparatory schools, competition is intensifying each year and the decline in the number of new students resulted in lower sales. For profits, the extent of the loss contracted through cost-reduction efforts, including to consolidate the two school buildings into one building for commuting students and currently enrolled high school students. At the end of FY8/19 3Q, the number of students was down 21.5% on the end of the previous fiscal year to 62 students. Although it is likely that the severe earnings environment will continue for the time being, the Company intends to minimize the extent of the decline in earnings by strengthening student recruitment and the summer learning courses.

d) Waseda Academy Kobetsu school business

In the Waseda Academy Kobetsu school business, net sales increased 2.7% YoY to ¥375mn and the operating loss was ¥8mn (compared to ¥21mn in the same period in the previous fiscal year). At the end of FY8/19 3Q, the number of schools was unchanged from the end of the previous fiscal year at 35 schools (8 directly operated schools, 5 MAXIS schools, 10 franchise schools, and 12 directly operated Waseda Academy Kobetsu schools). The number of enrolled students at all schools had increased 10.1% to 2,435 students, and the average number of students per student had also risen 10.1% to 69.6 students, so both indicators steadily increased. Although no franchise schools were newly established in FY8/19 (2 in 2Q of the previous fiscal year), sales increased, albeit slightly, by 14.6% YoY in 3Q as 1 franchise school became a directly operated school.

Going forward, the Company will strengthen its alliance with Waseda Academy <4718>, including for educational administration meetings, advertising and publicity meetings, and joint tutor training, and work to improve the quality of exam guidance services, with the aims of accumulating a track record of its students passing the entrance exams for prestigious, difficult-to-enter schools and increasing the number of students. Also, its policy for school development is to increase the number of franchise schools.

e) Kids school business

In the kids school business, net sales increased 30.2% YoY to ¥267mn and operating income was ¥6mn (compared to a loss of ¥4mn in the same period in the previous fiscal year). At the end of FY8/19 3Q, there were 25 schools (7 directly operated schools, 3 nursery care facilities, and 15 franchise schools, consignment operations, and related facilities), which was an increase of 6 schools on the on the end of the previous fiscal year (up 2 nursery care facilities and 4 franchise schools, consignment operations and related facilities). The number of enrolled students also steadily increased, up 15.8% to 1,122 students. The demand for nursery care and after-school care continues to be strong, so going forward the Company intends to strengthen this business by developing franchise operations and consignment operations services that can generate earnings at an early stage.

f) Soccer school business

In the soccer school business, net sales decreased 1.0% YoY to ¥103mn and operating income was ¥8mn (compared to income of ¥1mn in the same period in the previous fiscal year). At the end of FY8/19 3Q, the number of schools had increased by 1 on the end of the previous fiscal year to 14 schools (13 directly operated schools and 1 franchise school). The number of enrolled students also increased for the first time in 13 fiscal periods, up 2.7% to 873 students. In addition to working to strengthen the schools' management capabilities and the training of coaches, the Company conducted activities to promote enrollments by holding events, including trial lessons and spring camps, and these measures proved successful.

The Company will hold a camp in Spain for the first time in the summer of 2019 (August 17th to 25th, 5 applicants). Students will participate for about one week in a joint camp conducted by the lower organization of a local professional team, and a stadium tour is also planned. As soon as the recruitment of students was started, there was a large response and all the available places were quickly filled. Therefore, if this camp is successful, the Company is considering expanding its scale and holding it on an ongoing basis.

Continues to have an abundance of cash on hand and to maintain essentially debt-free management, and its financial condition is highly stable

3. Financial position and management indicators

Looking at the Company's financial condition at the end of FY8/19 3Q, total assets were down ¥570mn on the end of the previous fiscal year to ¥18,113mn. The main influencing factors were a decrease of ¥344mn in accounts receivable - trade and an increase (decreasing effect) of ¥62mn in allowance for doubtful accounts in current assets. Also, in non-current assets, property, plant and equipment increased ¥119mn, but investment securities decreased ¥127mn. Goodwill was ¥3,164mn.

Total liabilities were up ¥21mn on the end of the previous fiscal year to ¥4,367mn. In current liabilities, there were increases in short-term loans payable of ¥62mn, income taxes payable of ¥67mn, and provision for bonuses of ¥152mn, while accrued expenses decreased ¥258mn. In non-current liabilities, long-term loans payable of ¥68mn was recorded, but long-term accounts payable-other to officers and employees decreased ¥78mn and deferred tax liabilities declined ¥78mn. Net assets were down ¥591mn to ¥13,745mn. This was because retained earnings decreased ¥494mn, mainly due to the payment of dividends, and valuation difference on available-for-sale securities declined ¥87mn.

Looking at the management indicators, the equity ratio decreased slightly, down from 76.6% at the end of the previous fiscal period to 75.8%, but as before it remains at a high level. The interest-bearing debt balance is also only ¥200mn and the Company is essentially maintaining debt-free management, so it can be judged that its financial condition is excellent.

Consolidated balance sheet and management indicators

(¥mn)

	FY8/16	FY8/17	FY8/18	FY8/19 3Q	Change
Current assets	6,865	10,431	8,959	8,403	-556
(Cash and deposits)	4,633	7,822	6,508	6,518	10
Non-current assets	10,105	8,883	9,723	9,709	-13
Total assets	16,970	19,314	18,683	18,113	-570
Current liabilities	3,059	4,168	3,563	3,625	61
Non-current liabilities	701	729	782	742	-40
Total liabilities	3,760	4,897	4,346	4,367	21
(Interest-bearing debt)	82	70	70	200	130
Net assets	13,209	14,416	14,336	13,745	-591
Management indicators					
(Stability)					
Equity ratio	77.4%	74.5%	76.6%	75.8%	-0.8pt
Interest-bearing debt ratio	0.6%	0.5%	0.5%	1.5%	1.0pt

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

Business outlook

In FY8/19, the Company is rebuilding the Meiko Gijuku business as its top priority

1. FY8/19 outlook

For the FY8/19 consolidated results, the Company has left its initial forecasts unchanged with net sales to increase 6.3% YoY to ¥20,320mn, operating income to rise 29.0% to ¥1,860mn, ordinary income to grow 24.5% to ¥1,940mn, and net income attributable to the owners of the parent to climb 55.2% to ¥1,020mn. To achieve these forecasts, it is calculated that in 4Q, the Company will need to increase net sales by 13.1% YoY and operating income by 24.4%. Looking at the progress made up to 3Q, it is possible that net sales will be below forecast, but the operating income forecast seems to be in range.

At FISCO, we think the consolidation of K. Line and KMG is expected to increase net sales from ¥1.2bn to ¥1.3bn, but decrease operating income by tens of millions of yen. Therefore, the main reason for the higher profits YoY will be the reduction of SG&A expenses, mainly sales promotion expenses.

FY8/19 outlook (consolidated)

(¥mn)

	FY8/18			FY8/19		
	Results	% of sales	YoY	Forecast	% of sales	YoY
Net sales	19,116	-	-1.4%	20,320	-	6.3%
Cost of sales	13,020	68.1%	2.5%	14,080	69.3%	8.1%
SG&A expenses	4,654	24.3%	14.3%	4,380	21.6%	-5.9%
Operating income	1,441	7.5%	-44.9%	1,860	9.2%	29.0%
Ordinary income	1,558	8.2%	-44.5%	1,940	9.5%	24.5%
Net income attributable to owners of the parent	657	3.4%	-67.8%	1,020	5.0%	55.2%
EPS (¥)	24.74			38.41		

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

In order to achieve the regrowth of the Meiko Gijuku business, which is the Company's mainstay business, it has positioned FY8/19 as the period to rebuild its business foundation. It is working on various measures for this, including strengthening competitiveness by introducing MEIKO Style Coaching into all schools, enhancing learning content that utilizes ICT (including for English and programming courses), bolstering marketing measures that utilize the Internet, and improving customer satisfaction by expanding the support centers. As it continues to conduct the scrap & build of schools, for the time being the number of schools and the number of students may continue to trend downward. But the Company intends to build the foundation with the aim of achieving regrowth by FY8/20.

Also, in July 2019 the Company announced that it had newly established 3 committees – the Coaching School Business Committee, the Systems Committee, and the Business Reform Committee – to serve as the ancillary organizations to the Business Strategy Council, which it has established as the organization to formulate business policy in the medium- to long-term. The Tutorial Schools Business Committee will promote measures to share the strengths and initiatives of each business, such as Meiko Gijuku, Waseda Academy Kobetsu schools, and study clubs*, to further improve educational abilities and strengthen student recruitment. The Systems Committee will review departmental systems and Company-wide systems to enhance the marketing functions and improve productivity. The Business Reforms Committee will work on reforms to the business-process framework, centered on customers, from the viewpoint of overall optimization.

* As a new style of private tutorial school, the Company launched study clubs in earnest in the spring of 2018 and was managing 3 clubs in the Tokyo metropolitan area at the end of June 2019. Through utilizing EdTech, one teacher is able to deal with many students. Students are able to effectively improve their academic abilities by solving individually optimized problems using tablet terminals and digital teaching materials equipped with AI functions. The Company provides study clubs to elementary, junior high, and high school students.

The declines in the number of schools and students in the Meiko Gijuku business may bottom-out in FY8/20

2. Outlook by business segment

Net sales by segment

(¥mn)

	FY8/16	FY8/17	FY8/18	FY8/19 E	Growth ratio
Meiko Gijuku direct operations business	10,123	9,647	9,530	10,544	10.6%
Meiko Gijuku franchise operations business	5,597	5,586	5,242	5,205	-0.7%
Preparatory school and other businesses	2,950	4,149	4,343	4,570	5.2%
Total net sales	18,672	19,383	19,116	20,320	6.3%

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

In the outlook for sales by segment in FY8/19, in the Meiko Gijuku direct operations business, net sales are forecast to increase 10.6% YoY to ¥10,544mn; in the Meiko Gijuku franchise operations business, to decrease 0.7% to ¥5,205mn; and in the preparatory school business and other businesses, to rise 5.2% to ¥4,570mn.

In the mainstay Meiko Gijuku business, since April the increase in the number of newly enrolled students has slowed down. But the Company is strengthening student recruitment activities for July and August, which is the student-recruitment season, and by the end of FY8/19 it is aiming to have caught-up the number of students to the level of the same period in the previous fiscal year. The number of schools is forecast to continue to moderately decline toward the end of the period due to the ongoing scrap & build, such as the closures of unprofitable schools. However, the declining trend in the number of students per school has halted, and the investment mindsets of the owners of the franchise schools is expected to improve as the profitability of schools increases in the future. In particular, although competition in the metropolitan areas is fierce, there is still room for expansion, and at FISCO we forecast that openings of new schools will increase from FY8/20 onwards. The sales unit price per students is also expected to trend solidly in the future due to the strong performance of new content, such a Meiko Mirai Eigo.

In this situation, in the Meiko Gijuku direct operations business in FY8/19, net sales are expected to be basically in line with the Company's forecast due to the effects of the higher sales from K. Line and KMG being made subsidiaries. On the other hand, in the Meiko Gijuku franchise operations business, up to 3Q the decreases rates for the number of schools and the number of students grew larger, so achieving the full fiscal-year forecasts would appear somewhat difficult. However, the Company is aiming to achieve them by strengthening measures, including through student recruitment activities and summer learning courses.

In the other businesses, results for the preparatory school, school-support, and academic publishing businesses are trending below forecast, so it is possible that sales will be slightly below forecast. However, due to increases in student numbers in the kids schools, Japanese language schools, and Waseda Academy Kobetsu schools, the outlook is still for sales to increase YoY. In particular, the focus is being placed on the kids school and Japanese language school businesses as the growth businesses, because their markets are expected to continue to expand in the future against the backdrop of the changes to the societal environment.

In addition, the programing schools for elementary school students that started in FY8/18 have been favorably received and have steadily expanded to more than 100 schools. In addition, for the study clubs, which were fully launched from the spring of 2018 as a new style of private tutorial school, the Company is currently building an earnings model and plans to develop franchise operations at the stage when they can be expected to generate earnings.

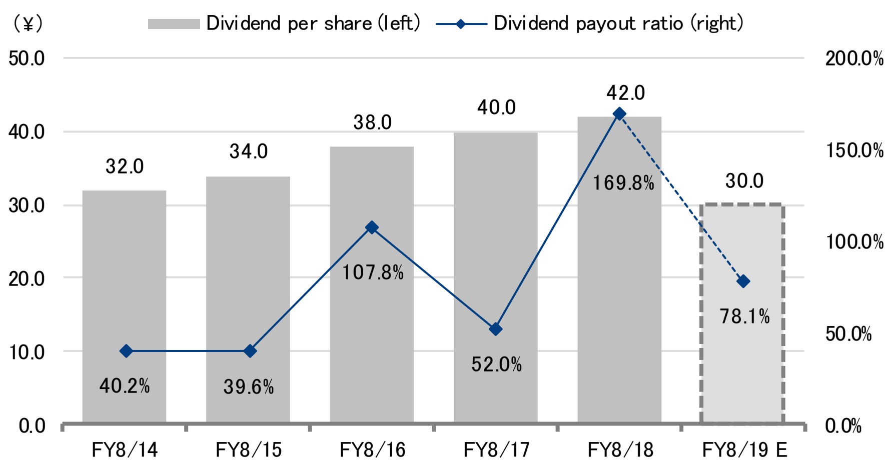
Shareholder return policy

Although its record of increasing dividends will end for the time being, the Company will maintain an active shareholder return policy

Since it was listed on the JASDAQ market in April 1997, the Company has continuously increased its dividend. But for FY8/19, it has announced it will decrease dividends for the first time, down ¥12 YoY to ¥30.0 (dividend payout ratio of 78.1%). This is because the Company judged that temporarily diverting funds for the purpose of investment into rebuilding its mainstay Meiko Gijuku business would be best for shareholders. However, the Company plans to keep the dividend payout ratio at the 80% level, and if profits continue to trend upward, we can expect it to increase dividends again from FY8/20.

Under the shareholder benefit program, the Company continues to give QUO cards worth ¥1,000-5,000 to shareholders as of the end of August, according to the number of shares they hold and the length of time that they have held them. Those holding 100 shares for less than three years will receive a ¥1,000 QUO card, while those holding the same number of shares continuously for three years will receive cards with a value of ¥3,000. The gross investment yield per share unit, including the shareholder benefit program, is at the 4-6% level at the current share price (¥973 as of July 12, 2019). The Company's capital policy is unchanged to strengthen its equity and to flexibly consider acquiring treasury stock when possible, taking into account the share price and financial position.

Dividend per share and payout ratio



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

Shareholder benefit program

QUO card distribution (once annually, for shareholders as of August 31)		
Number of shares held	Value of gift cards for holding stock for less than three years	Value of gift cards for holding stock for three years or more
100–499 shares	Equivalent to ¥1,000	Equivalent to ¥3,000
500–999 shares	Equivalent to ¥2,000	Equivalent to ¥4,000
1,000 or more shares	Equivalent to ¥3,000	Equivalent to ¥5,000

Note: Shareholders became eligible for the program from August 31, 2016.
Source: Prepared by FISCO from Company materials

Information security policy

The Company manages tutorial schools and also concludes contracts with member companies based on its own franchise system, and it provides continuous school management guidance. In the school management process, it obtains personal information on students, parents and guardians, and tutors. It manages this personal information in accordance with its Regulations on the Protection of Personal Information. It also examines measures to prevent the leakage of information through the Risk Management Committee and verifies the operational status of measures to protect personal information.

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