COMPANY RESEARCH AND ANALYSIS REPORT

Sanki Engineering Co., Ltd.

1961

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Summary

A comprehensive engineering company conducting the Facilities Construction Business and the Plant & Machinery Systems Business with strengths of advanced technology and credibility cultivated over a long history

Sanki Engineering Co., Ltd. <1961> (hereafter, “the Company”) is an engineering company whose main business is the planning, design, manufacture, supervision, installation, sale and consultation of systems and equipment for construction and plant facilities, in office buildings, schools, hospitals, shopping centers, industrial plants, R&D centers and other facilities. The Company’s strengths include comprehensive engineering capabilities across a diverse range of business operations, combined with advanced technology and credibility accumulated over a history of nearly 100 years.

1. FY3/21: Orders received increased 0.8% despite 8.5% YoY decrease in net sales

In FY3/21, the Company reported ¥195,580mn in orders received (up 0.8% year-on-year (YoY)), balance carried forward was ¥141,676mn (up 4.0%), ¥190,067mn in net sales (down 8.5%), ¥7,498mn in operating income (down 29.7%), ¥8,196mn in ordinary income (down 27.0%), and ¥5,901mn in profit attributable to owners of parent (down 22.1%). Although sales declined, it has a significant balance of outstanding orders. Through continued efforts including to thoroughly manage costs and to strengthen the site-support systems, although the gross profit margin declined 0.4. of a percentage point (pp) YoY to 15.1%, it is still being maintained at a high level (15% range). Due to the impact of the novel coronavirus pandemic (hereafter, COVID-19), orders for large-scale and long-term projects declined only slightly, but orders for small-scale maintenance and repairs projects and other projects were affected.

2. FY3/22 results outlook: operating income is forecast to increase 26.7% YoY

For the FY3/22 results, the Company is currently forecasting orders received of ¥200,000mn (up 2.3% YoY), net sales of ¥200,000mn (up 5.2%), operating income of ¥9,500mn (up 26.7%), ordinary income of ¥10,000mn (up 22.0%), and profit attributable to owners of parent of ¥7,000mn (up 18.6%). These forecasts are calculated based on the current orders received, etc., and these forecast values are also the targets for the third year (final year) of the medium-term management plan “Century 2025” Phase 2. The Company has stated that “The future impact of COVID-19 is unclear and it may affect results, but we are resolutely progressing the “Century 2025” Phase2 plan toward achieving the targets.”

3. Promoting the targets in "Century 2025" Phase 2, the medium-term management plan

In March 2016, the Company announced "Century 2025" as its long-term version as a 10-year goal toward the 100th anniversary of its foundation. It has positioned the first three years of this plan as "Century 2025" Phase 1, and for FY3/19, which is the final fiscal year of Phase 1, the Company have achieved the numerical targets it had set, which was net sales of ¥195bn and operating income of ¥7.5bn, but it has already achieved these targets. Following on from this, it has announced Phase 2, and while the three key initiatives are a continuation of Phase 1, it has added "Disclose financial & capital policies and ESG policies" and "Reinforce Information Transmission." It has also set management targets in addition to financial performance targets in its quantitative targets for FY3/22, including an ordinary profit margin of 5.0% or above, an annual dividend of ¥60 or above, the acquisition of 5mn or more treasury stock (three years from FY3/20), total return ratio of 70% or above, and ROE of 8.0% or above. It is unclear for how long into the future the impact of COVID-19 will extend, but at the current point in time the Company has not changed its targets and its policy is to continue to progress the plan toward achieving them.

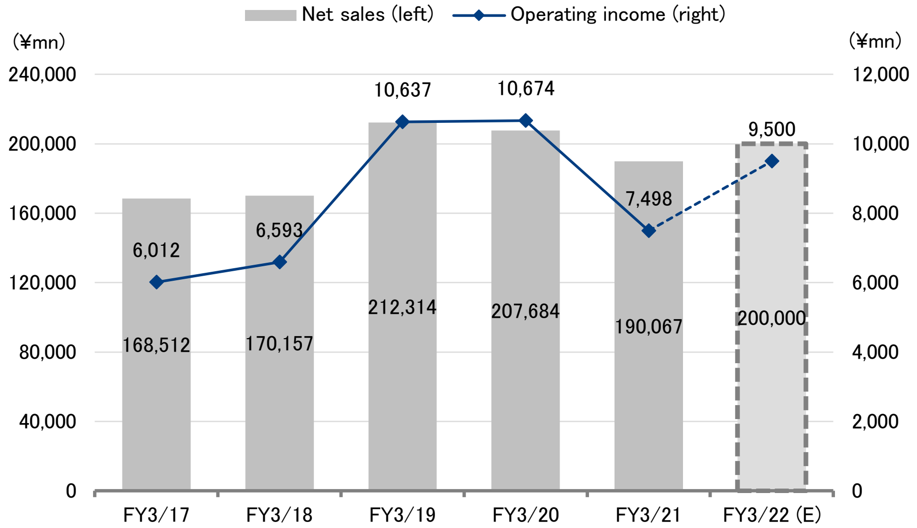
4. Actively returns profits to shareholders: the total return ratio (weighted average) for the last eight years is 85.7%

The Company has proactively conducted shareholder returns with stable dividends up to now, dividend hikes in recent years, and acquisition of treasury stock. For the annual dividend, it paid ¥60 in FY3/19, ¥95 in FY3/20 (including an extra dividend of ¥25), and ¥80 in FY3/21 (including an extra dividend of ¥10). In FY3/22, it plans to pay a regular dividend of ¥70. The Company retired 1,000,000treasury stocks in August 2020, and has furthermore completed acquisition of 1,000,000 treasury stocks as of October 31, 2020. As a result, the total return ratio (weighted average) for the last eight years, including FY3/21, is 85.7%. As such, we think the Company is deserving of high marks for its proactive shareholder return policy.

Key Points

- Mitsui-affiliated, domestically-leading facilities company that is currently implementing measures to improve the profit margin
- In FY3/22, operating income is forecast to increase 26.7% YoY. Is currently steadily progressing the medium-term management plan.
- Actively returns profits to shareholders. In FY3/22, plans to pay an annual dividend of ¥70. The total return ratio for the last eight years is 85.7%.

Results trends



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

Company outline

One of the largest facilities construction company in Japan. As a Mitsui-affiliate, it has a history of nearly 100 years

1. Company outline

Sanki Engineering is a facilities company that was established in 1925 as a spin-off of the machinery division of the former Mitsui & Co., Ltd. The first large projects for the Company were the Shiga manufacturing plant of Toyo Rayon (currently Toray Industries, Inc. <3402>), and a refrigerated warehouse for Aomori Seihyo. Initially, the Company engaged in heating, plumbing, steel frame construction and the supply of construction materials. It has subsequently branched out into electrical work, developing integrated plant construction planning, design and installation as its main operations.

After the war, the Company steadily grew on robust construction demand and surpassed ¥1bn in capital in 1958. In subsequent years, the Company participated in projects undertaken in preparation to host the Tokyo Olympic Games in 1964, and grew in tandem with the expansion of the Japanese economy. The Company diversified from the Facilities Construction Business, such as heating, ventilation, air-conditioning (HVAC), plumbing, and electrical systems into other types of facilities, such as transport equipment, conveyance systems, water treatment facilities and waste treatment facilities. Today, it is a leading domestic facilities company. The Company's shares were listed on the Tokyo Stock Exchange in 1950.

2. History

In April 2015, prior to the 90th anniversary of its establishment in FY3/16, the Company appointed Mr. Tsutomu Hasegawa as President and Representative Director. The Company subsequently announced the "Century 2025" long-term vision headed toward its 100th anniversary in 2025 in March 2016. It completed Phase 1 in FY3/19, the first step, reaching initial targets. Furthermore, since April 2020, it is promoting Phase 2 under Hirokazu Ishida as the new President.

History

1925	Sanki Engineering Co., Ltd. established as a spin-off of the machinery division of the former Mitsui & Co., Ltd.
1935	10th anniversary of its establishment. Had 5 branches, 6 sub-branch offices, 3 affiliated companies, and around 300 employees
1958	Capital exceeded ¥1,000mn
1963	Completed the Sagami Plant (currently, the Yamato Plant)
1964	Participated in projects relating to the Tokyo Olympic Games, including the Yoyogi National Gymnasium, and the NHK Broadcast Center
1982	Newly established Technical R&D Institute in Yamato City, Kanagawa Prefecture, equipped with facilities for basic research and for large-scale experiments
2000	Opened the Shonan Training Center (Yokosuka City, Kanagawa Prefecture) and strengthened human resource development
2011	Relocated its head office to the current location in the Tsukiji area of Tokyo
2016	90th anniversary of its establishment. Announced its long-term vision "Century 2025"
2018	Opened Sanki Techno Center, a comprehensive training and research facility (Yamato City, Kanagawa Prefecture)
2019	Opened the Yamato Product Center, and completed the STeP (Sanki Techno Park) project

Source: Prepared by FISCO from the Company's website, etc.

Business description

4 main segments, with a focus on the Facilities Construction Business

1. Outline of business by segment

The Company's main operations are divided into four business segments: three facility business segments of Facilities Construction, Machinery Systems, Environmental Systems, and Real Estate. An overview of each segment is set out below.

(1) Facilities Construction Business

The Facilities Construction Business engages in activities including planning, design, installation, maintenance, and repair of facilities including office buildings, schools, hospitals, shopping centers, factories, R&D centers, and other facilities. The scope of activities handled by this business is extensive and can be further divided into the following sub-segments.

a) HVAC and plumbing for buildings

The HVAC and plumbing for buildings business provide HVAC, water supply and wastewater systems, plumbing, area heating and cooling systems, kitchen systems, and disaster readiness systems for general buildings and facilities, such as office buildings, schools, hospitals, department stores, hotels, and warehouses.

b) Industrial HVAC

The industrial HVAC business provides HVAC for factories and research facilities of all industries, especially clean room systems for semiconductor plants and food processing plants, which are areas of strength for the Company, as well as special air-conditioning systems and appurtenances for manufacturers of medical systems, and the like; in addition to environmental control systems and so forth for automobile manufacturers.

c) Electrical systems

The electrical systems business provides electrical systems, communications-related systems, electrical civil works, and so forth.

d) Facility systems

The facility systems business offers project management and other services for the construction or relocation of the offices and dealing rooms of financial institutions and other industries. It also provides central monitoring and automatic control systems, Internet protocol (IP) solutions, network solutions, business continuity plan (BCP) solutions and other services for large-scale buildings.

(2) Machinery Systems Business

The Machinery Systems Business supplies materials handling systems, including various transportation equipment (conveyors, sorting systems, etc.), and conveyance systems for factories and automated warehouses.

(3) Environmental Systems Business

The Environmental Systems Business provides facilities such as water treatment facilities (including facilities to treat drinking water and dispose of sewage, facilities for the disposal of industrial wastewater, and facilities for the treatment or incineration of sludge), facilities for the treatment of waste (including waste incineration facilities, landfill wastewater treatment facilities), and others.

(4) Real Estate Business

The Real Estate Business utilizes vacant land, such as former factory sites, and manages real estate lease business and building management business.

Sanki Engineering's main business is the provision of the facilities and solutions as described above. The Company obtains about half of its orders directly from facility owner clients and half indirectly through general contractors.

Just as the size of the orders varies widely from a few million yen to a few billion yen, the order completion time varies from a few weeks to a few years for longer orders. The profitability of an order varies and may differ from the originally planned profitability depending on factors such as labor and material costs and the management construction schedule. Some orders end up more profitable than originally planned, and some are less profitable.

2. Strengths, distinguishing traits, and competitors

(1) Broad business domain and one-stop shop solutions

It's no exaggeration to say that there are countless companies in Japan providing the same kind of construction and facilities as Sanki Engineering. The Company's strength lies in the wide range of its businesses, which includes HVAC for building, plumbing, industrial HVAC, electrical systems, facility systems, automated control systems for buildings, transportation systems, and water treatment facilities. The Company can provide services for many types of facilities and solutions covering all phases from planning and design, to installation, maintenance, repair, and replacement, depending on the life cycle of the building. This capability allows its customers to place one-stop shop orders to resolve their problems. By making use of "total engineering" and "life-cycle engineering," which combines a wide variety of businesses horizontally, the Company can provide optimal systems with high added value, and this comprises the Company's strength.

(2) Top-class technology and high-quality customer base

One of the Company's main strengths is the advanced technology it has accumulated since before World War II. Moreover, this top-class technology spans a wide range of fields. Furthermore, Sanki Engineering has earned a reputation for reliability over decades of business, which underpins its extensive, high-quality customer base. This can also be considered a strength of the Company. In addition to its prewar achievements, the Company's involvement in numerous post-war projects, including the construction of facilities for the Tokyo Olympic Games of 1964, have enabled it to obtain orders for recent large projects, such as the ABENO HARUKAS in Osaka and Tokyo Midtown Hibiya.

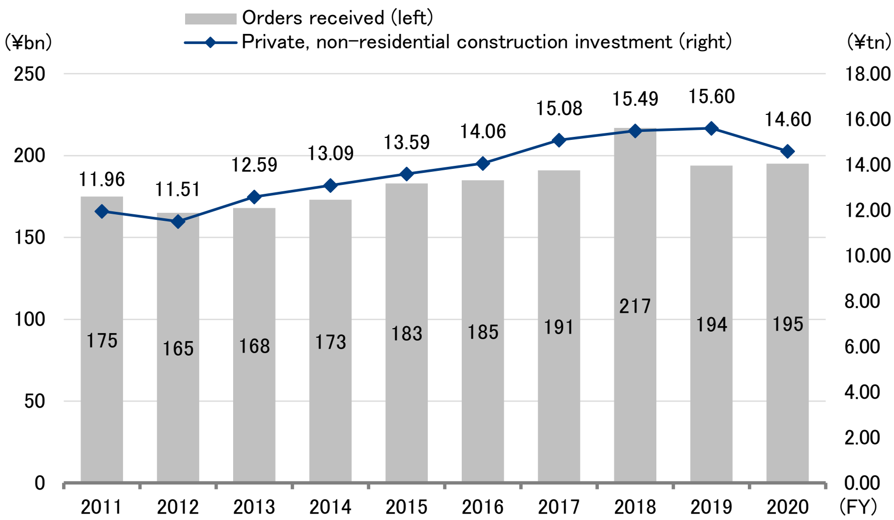
3. Main competitors

Sanki Engineering's competitors vary by project, but its main competitors among the comprehensive facility construction companies are other large companies such as Takasago Thermal Engineering Co., Ltd. <1969>, Shinryo Corporation (unlisted), Dai-Dan Co., Ltd. <1980>, and Taikisha Ltd. <1979>. Compared to these competitors, Sanki Engineering's strengths lie in its broad business domain and its superiority in industrial HVAC systems, such as clean rooms.

4. Trend in orders received and the economic environment

Given the nature of Sanki Engineering's businesses, orders received are the most important factor affecting the Company's performance. Annual orders received are greatly affected by the overall Japanese market, or the Japanese macro-economy. As the Company's main business is facilities construction, it is influenced by the macro indicator of private sector, non-residential construction investment. The correlation between orders received and private sector, non-residential construction investment is arguably very high.

Orders received versus Private, non-residential construction investment



Source: Prepared by FISCO from the Company's financial results and the "Integrated Statistics on Construction Work," Ministry of Land, Infrastructure, Transport and Tourism

Business trends

In FY3/21, although sales and profits decreased YoY, orders received increased 0.8% and the balance carried forward was maintained at the high level of ¥141,676mn

1. FY3/21 results overview

(1) Earnings

In the FY3/21 results, orders received were ¥195,580mn (up 0.8% YoY), balance carried forward was ¥141,676mn (up 4.0%), net sales were ¥190,067mn (down 8.5%), operating income was ¥7,498mn (down 29.7%), ordinary income was ¥8,196mn (down 27.0%), and profit attributable to owners of parent was ¥5,901mn (down 22.1%).

For net sales, sales were strong in electrical systems, for which a large-scale project was acquired in the previous period, but overall sales decreased as it was the quiet season for large-scale projects in the mainstay HVAC and plumbing for buildings, and also as orders declined for small-scale maintenance and repairs projects due to the impact of COVID-19. Orders decreased in the Machinery Systems Business, which was significantly impacted by COVID-19, but they were strong in HVAC and plumbing for buildings, industrial HVAC, and the Environmental Systems Business. Therefore, total orders received were ¥195,580mn (up 0.8% YoY). Due to a decline in sales and an increase in orders, the balance carried forward at the end of the period had maintained its high level at ¥141,676mn (up 4.0% on the end of the previous period).

In profits, the Company is continuing with measures including thoroughly managing costs and strengthening site-support systems, but sales declined and small-scale maintenance and repairs projects decreased. Therefore, the gross profit margin was 15.1% (down 0.4pp YoY), but it was still maintained at a high level (15% range).

Conversely, SG&A expenses were ¥21,255mn (down 0.8% YoY). Due to the impact of COVID-19, business-trip expenses and other expenses declined, but it decreased only slightly because of the YoY increases in expenses to prevent infections and personnel expenses. The reasons for the higher personnel expenses included the slight increase in the number of personnel, but the majority of this increase was to improve benefits to employees alongside the work-style reforms. As a result, operating income declined 29.7% YoY.

FY3/21 results

(¥mn)

	FY3/20		FY3/21		YoY	
	Result	Ratio	Result	Ratio	YoY change	Change %
Orders received	194,018	-	195,580	-	1,561	0.8%
Balance carried forward	136,163	-	141,676	-	5,513	4.0%
Net sales	207,684	100.0%	190,067	100.0%	-17,617	-8.5%
Gross profit	32,110	15.5%	28,754	15.1%	-3,356	-10.5%
SG&A expenses	21,436	10.3%	21,255	11.2%	-180	-0.8%
Operating income	10,674	5.1%	7,498	3.9%	-3,175	-29.7%
Ordinary income	11,224	5.4%	8,196	4.3%	-3,027	-27.0%
Profit attributable to owners of parent	7,576	3.6%	5,901	3.1%	-1,675	-22.1%

Source: Prepared by FISCO from the Company's financial results and Summary of Financial Results

(2) Earnings by segment

The Facilities Construction Business posted ¥155,501mn in net sales (down 9.3% YoY). In sub-segments, HVAC and plumbing for buildings posted ¥55,293mn (down 21.9%) in sales. From the beginning, sales were forecast to decline because it is the quiet season for large-scale projects. But in addition to this, due to the impact of COVID-19, sales decreased of small-scale maintenance and repairs projects, including for hotels and department stores. In industrial HVAC, sales declined slightly YoY to ¥64,152mn (down 5.3%), but were still maintained at a comparatively high level. In electrical systems, sales were strong at ¥24,941mn (up 13.9%), including from the acquisition of a large-scale order in the previous year. In facility systems, sales were maintained at the same level as in the previous year, at ¥11,113mn (down 0.0%).

Total net sales in the Plant & Machinery Systems Business were ¥32,533mn (down 5.5% YoY). In the Machinery Systems Business, sales were ¥8,973mn (down 19.7%), mainly because the Company was unable to acquire sales of conveyor-related projects and other projects due to the self-restraint on sales activities. The Environmental Systems Business posted ¥23,560mn (up 1.3%) in sales mainly on progress in a major DBO* project booked as an order previously. Besides these facility business segments, the Real Estate Business recorded ¥2,375mn in net sales (up 7.5%), including the boost from starting rental of a portion of the former Yamato Plant site to Nippon Life Insurance Company, and Others posted ¥815mn in net sales (down 12.5%).

* DBO (Design Build Operate) is a method for publicly-built, privately-operated projects with a collective order made to private companies (such as the Company) for design, building, and operations and maintenance management.

The Company discloses gross profit and ordinary income as segment profit values from FY3/20. Our report uses gross profits. In FY3/21, whereas gross profit in the Facilities Construction Business decreased to ¥23,253mn (down 9.8% YoY for a decrease of ¥2,527mn). In the sub-segments, gross profit was ¥21,038mn (down 10.9%) in HVAC and plumbing for buildings, industrial HVAC, and electrical systems, and was ¥2,215mn (up 2.1%) in the facility systems. Gross profit in the Plant & Machinery Systems Business was ¥4,732mn (down 16.0% for a decrease of ¥898mn), which consists of ¥1,556mn (down 32.8%) in the Machinery Systems Business and ¥3,176mn (down 4.2%) in the Environmental Systems Business. In the Real Estate Business and Others, gross profits were ¥866mn (up 28.6%) and ¥101mn (down 49.7%), respectively.

Net sales and gross profit by segment

(¥mn)

	FY3/20		FY3/21		YoY	
	Result	Ratio	Result	Ratio	YoY change	Change %
Net sales	207,684	100.0%	190,067	100.0%	-17,617	-8.5%
Facilities Construction Business	171,501	82.6%	155,501	81.8%	-15,999	-9.3%
HVAC and plumbing for buildings	70,756	34.1%	55,293	29.1%	-15,462	-21.9%
Industrial HVAC	67,736	32.6%	64,152	33.8%	-3,584	-5.3%
Electrical systems	21,889	10.5%	24,941	13.1%	3,052	13.9%
Facility systems	11,119	5.4%	11,113	5.8%	-5	-0.0%
Machinery Systems Business	11,169	5.4%	8,973	4.7%	-2,196	-19.7%
Environmental Systems Business	23,261	11.2%	23,560	12.4%	298	1.3%
Real Estate Business	2,210	1.1%	2,375	1.2%	165	7.5%
Others	931	0.4%	815	0.4%	-116	-12.5%
Adjustments	-1,389	-	-1,158	-	230	-
Gross profit	32,110	15.5%	28,754	15.1%	-3,356	-10.5%
Facilities Construction Business	25,781	15.0%	23,253	15.0%	-2,527	-9.8%
Building HVAC, industrial HVAC, and electrical systems	23,610	14.7%	21,038	14.6%	-2,572	-10.9%
Facility systems	2,170	19.5%	2,215	19.9%	44	2.1%
Machinery Systems Business	2,316	20.7%	1,556	17.3%	-760	-32.8%
Environmental Systems Business	3,314	14.2%	3,176	13.5%	-138	-4.2%
Real Estate Business	673	30.5%	866	36.5%	192	28.6%
Others	200	-	101	-	-99	-49.7%
Adjustments	-176	-	-199	-	-23	-

Note: Segment profits are shown as gross profit from FY3/20
Source: Prepared by FISCO from the Company's Summary of Financial Results

(3) Orders received by segment

In the Facilities Construction Business as a whole, orders received were maintained at basically the same level YoY, at ¥156,768mn (down 0.6% YoY). In an environment impacted by COVID-19, including the self-restraint on sales activities, this can be said to be a good effort. By segment, in HVAC and plumbing for buildings, orders received were ¥65,371mn (up 5.3%) and orders are steadily growing. In industrial HVAC, due to the strong orders for semiconductor-related, 5G-related, and R&D-related, orders received increased YoY to ¥59,234mn (up 1.4%). In electrical systems, orders received were ¥21,472mn (down 14.1%), but it seems that most of this decrease rate was due to the high level in the previous period, so it is not a result to cause concern and they are still being maintained at above ¥20bn. In facility systems as well, there was a large-scale project in the previous period, so orders received were ¥10,690mn (down 12.2%), but this is the same level as in FY3/19 and is not a bad result.

In the Plant & Machinery Systems Business, orders received in the Machinery Systems Business were ¥7,858mn (down 24.1% YoY), but this was mainly due to the impact of COVID-19. Conversely, orders trended strongly in the Environmental Systems Business, centered on large-scale projects, and orders received was ¥28,710mn (up 18.4%). As a result, orders received in the Plant & Machinery Systems Business totaled ¥36,569mn (up 5.7%), and together with the Facilities Construction Business, orders received for the facilities work segments overall reached ¥193,338mn (up 0.6%).

In areas other than facilities work segments, orders received in the Real Estate Business totaled ¥2,375mn (up 7.5%), and in Others totaled ¥609mn (down 33.6%). Total orders received in FY3/21 (including adjusted amounts) was ¥195,580mn (up 0.8%). Balance carried forward at the end of FY3/21 hence worked out to ¥141,676mn (up 4.0%). By industry, orders were strong (increasing YoY) for electrical systems, medical, finance and insurance, and government ministries and agencies.

Orders for large-scale projects (orders exceeding ¥1,000mn) totaled ¥48,483mn with 27 projects. The average amount per order declined compared to the previous period to ¥1,796mn (¥2,457mn in the previous period). But the number of orders and the order amount are both increasing.

Orders received by segment

(¥mn)

	FY3/20		FY3/21		YoY	
	Result	Ratio	Result	Ratio	YoY change	Change %
Orders received	194,018	100.0%	195,580	100.0%	1,561	0.8%
Facilities Construction Business	157,659	81.3%	156,768	80.2%	-890	-0.6%
HVAC and plumbing for buildings	62,095	32.0%	65,371	33.4%	3,276	5.3%
Industrial HVAC	58,391	30.1%	59,234	30.3%	843	1.4%
Electrical systems	25,000	12.9%	21,472	11.0%	-3,528	-14.1%
Facility systems	12,171	6.3%	10,690	5.5%	-1,481	-12.2%
Machinery Systems Business	10,351	5.3%	7,858	4.0%	-2,492	-24.1%
Environmental Systems Business	24,247	12.5%	28,710	14.7%	4,462	18.4%
Real Estate Business	2,210	1.1%	2,375	1.2%	165	7.5%
Others	917	0.5%	609	0.3%	-308	-33.6%
Adjustments	-1,367	-	-742	-	-	-

Source: Prepared by FISCO from the Company's Summary of Financial Results

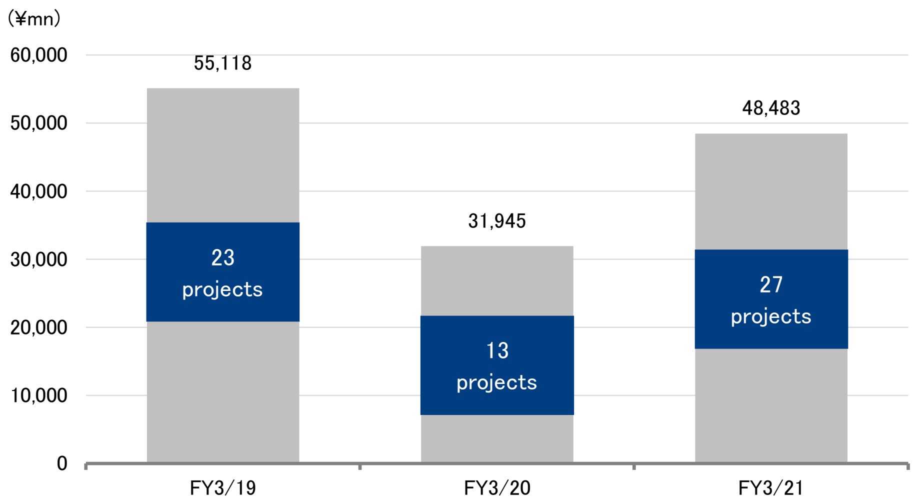
Breakdown of large-scale projects with orders exceeding ¥1,000mn

(projects)

	FY3/19	FY3/20	FY3/21
Office	2	1	4
Multi-purpose buildings	1	-	-
Hotel	1	-	-
Factory	10	3	6
Logistics Center	1	-	-
Residential complexes	1	-	-
Hospital and Clinics	1	1	3
Research institute	1	2	3
General government buildings	1	1	-
Gymnasiums	1	-	-
Other building interiors	1	2	3
Railway, Airport	1	-	1
Power plants and substations	-	1	-
School buildings and auditoriums	-	-	1
Waste processing facility	1	1	1
Water treatment plants and sewage plants	-	1	5
Total (projects)	23	13	27
Total (¥mn)	55,118	31,945	48,483

Source: Prepared by FISCO from the Company's Summary of Financial Results

Breakdown of large-scale projects with orders exceeding ¥1,000mn



Source: Prepared by FISCO from the Company's Summary of Financial Results

2. Financial condition

Looking at financial conditions at the end of FY3/21, current assets totaled ¥116,054mn (down ¥14,710mn YoY). This was mainly due to decreases of ¥8,859mn in cash and deposits and ¥6,141mn in notes and accounts receivable on completed construction contracts and other. Noncurrent assets were ¥55,258mn (up ¥5,218mn), which was primarily because of an increase in investments and other assets of ¥4,945mn. As a result, total assets at the end of FY3/21 were ¥171,313mn (down ¥9,492mn).

Current liabilities were ¥67,882mn (down ¥11,822mn from the end of the previous period). This was mainly due to decreases of ¥3,100mn in notes payable and ¥6,925mn in accounts payable on construction contracts. Noncurrent liabilities were ¥11,731mn (down ¥2,004mn), with the main factors including a decrease of ¥390mn in long-term loans payable and a decrease of ¥1,755mn in liability for retirement benefits. As a result, total liabilities at the end of FY3/21 were ¥79,614mn (down ¥13,826mn). Total net assets totaled ¥91,699mn (up ¥4,334mn), mainly due to a ¥997mn decrease in retained earnings from payment of dividends, a ¥328mn decrease in retirement of treasury stock, and a ¥3,579mn increase in unrealized gains on available-for-sale securities.

Cash and deposits and accounts payable decreased greatly YoY, but this was mainly due to the change to payment entirely by cash due to the change in payment terms to partner companies (with capital of less than ¥40mn).

Condensed balance sheet

(¥mn)

	FY3/20	FY3/21	YoY change
Cash and deposits	44,946	36,087	-8,859
Notes and accounts receivable on completed construction contracts and other	71,739	65,598	-6,141
Current assets	130,765	116,054	-14,710
Tangible noncurrent assets	13,957	13,972	15
Intangible noncurrent assets	679	937	258
Investments and other assets	35,403	40,348	4,945
Noncurrent assets	50,040	55,258	5,218
Total assets	180,805	171,313	-9,492
Notes and accounts payable on construction contracts and other	52,489	41,709	-10,780
Short-term loans payable	6,869	7,135	266
Advances received on uncompleted construction contract	7,493	8,580	1,087
Current liabilities	79,705	67,882	-11,822
Long-term loans payable	3,850	3,460	-390
Liability for retirement benefits	3,465	1,710	-1,755
Noncurrent liabilities	13,735	11,731	-2,004
Total liabilities	93,440	79,614	-13,826
Total net assets	87,364	91,699	4,334

Source: Prepared by FISCO from the Company's financial results and Summary of Financial Results

3. Cash flow conditions

In FY3/21, net cash used in operating activities was ¥483mn. The main inflows were the recording of profit before income taxes of ¥7,797mn, depreciation and amortization of ¥1,700mn, and a decrease of ¥4,770mn of notes and accounts receivable. The main outflows included decreases of ¥10,777mn in notes and accounts payable, ¥1,525mn in the allowance for bad debt, ¥1,594mn in liability for retirement benefits (contributions to benefit trust assets), and ¥1,706mn in other current liabilities. Net cash used in investment activities was ¥1,423mn. The main outflow was ¥1,494mn in purchase of property, plant and equipment. Net cash used in financing activities was ¥6,974mn. The main outflows were ¥1,171mn in acquisition of treasury stock and ¥5,474mn in cash dividends paid.

Cash and cash equivalents hence decreased ¥8,859mn in FY3/21 to a period-end balance of ¥37,087mn.

Compared to the previous period, cash flows from operating activities decreased significantly (a change from net cash provided of ¥11,940mn to net cash used of ¥483mn). But the main reason for this was the change to entirely cash payments for the payment terms for partner companies (with capital of less than ¥40mn).

Condensed statement of cash flows

(¥mn)

	FY3/20	FY3/21
Cash flows from operating activities	11,940	-483
Profit before income taxes	11,114	7,797
Change in notes and accounts receivable on completed construction contracts and other (- indicates increase)	15,321	4,770
Change in notes and accounts payable on construction contracts and other (- indicates decrease)	-16,009	-10,777
Cash flows from investment activities	-303	-1,423
Purchase of property, plant and equipment	-1,839	-1,494
Cash flows from financing activities	-8,955	-6,974
Change in short- and long-term loans payable (- indicates decrease)	-1,376	-125
Cash dividends paid	-4,469	-5,474
Change in cash and cash equivalents (- indicates decrease)	2,636	-8,859
Cash and cash equivalents at end of period	45,946	37,087

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

Outlook

In FY3/22, operating income is forecast to increase 26.7% YoY

The future remains unclear in terms of the impact of COVID-19, so for FY3/22 the Company is currently forecasting orders received of ¥200,000mn (up 2.3% YoY), net sales of ¥200,000mn (up 5.2%), operating income of ¥9,500mn (up 26.7%), ordinary income of ¥10,000mn (up 22.0%), and profit attributable to owners of parent of ¥7,000mn (up 18.6%). These forecasts are calculated based on the current orders received, etc., and these forecast values are also the targets for the third year (final year) of the medium-term management plan "Century 2025" Phase 2.

Breaking down net sales, the Facilities Construction Business is expected to provide ¥161,000mn (down 3.5%). By sub-segment, in HVAC and plumbing for buildings sales are expected to increase by 19.4% YOY to ¥66,000mn. In industrial HVAC they are expected to decrease by 9.6% to ¥58,000mn. In electrical systems they are expected to increase by 0.2% to ¥25,000mn. In facility systems they are expected to increase by 8.0% to ¥12,000mn. In the Plant & Machinery Systems Business, the forecasts are for net sales to increase 11.4% to ¥10,000mn in the Machinery Systems Business, and to increase 14.6% to ¥27,000mn in the Environmental Systems Business.

In the mainstay Facilities Construction Business, orders received are forecast to increase slightly to ¥161,000mn (up 2.7% YoY). By sub-segment, in HVAC and plumbing for buildings orders are expected to increase by 5.6% YOY to ¥69,000mn. In industrial HVAC they are expected to decrease by 3.8% to ¥57,000mn. In electrical systems they are expected to increase by 7.1% to ¥23,000mn. In facility systems they are expected to increase by 12.3% to ¥12,000mn. With respect to the Plant & Machinery Systems Business, orders for the Machinery Systems Business are expected to increase by 52.7% to ¥12,000mn, while orders for the Environmental Systems Business are expected to decrease by 12.9% to ¥25,000mn. As a result, overall orders received including the Real Estate Business and Others are forecast to be ¥200,000mn (up 2.3%).

The gross profit margin was at a comparatively high level in FY3/21 (15.1%) as well, but the Company is targeting 16.0% by continuing to implement measures to improve profits. Specific measures include establishing and strengthening various site-support systems, particularly strengthening negotiating capabilities for materials procurement by the procurement head office, and continuing to support purchasing operations at sites. This seems a high target, but on considering that it is maintaining a gross profit margin at a level above 15% even during the COVID-19 pandemic, it does not seem to be an impossible one. The forecasts are for gross profit of ¥32,000mn and operating income of ¥9,500mn.

FY3/22 forecast

(¥mn)

	FY3/21		FY3/22		YoY	
	Result	Ratio	Forecast	Ratio	YoY change	Change %
Orders received	195,580	100.0%	200,000	100.0%	4,420	2.3%
HVAC and plumbing for buildings	65,371	33.4%	69,000	34.5%	3,629	5.6%
Industrial HVAC	59,234	30.3%	57,000	28.5%	-2,234	-3.8%
Electrical systems	21,472	11.0%	23,000	11.5%	1,528	7.1%
Facility systems	10,690	5.5%	12,000	6.0%	1,310	12.3%
Facilities Construction Business	156,768	80.2%	161,000	80.5%	4,232	2.7%
Machinery Systems Business	7,858	4.0%	12,000	6.0%	4,142	52.7%
Environmental Systems Business	28,710	14.7%	25,000	12.5%	-3,710	-12.9%
Real Estate Business	2,375	1.2%	2,000	1.0%	-375	-15.8%
Others	609	0.3%	500	0.3%	-109	-17.9%
Net sales	190,067	100.0%	200,000	100.0%	9,933	5.2%
HVAC and plumbing for buildings	55,293	29.1%	66,000	33.0%	10,707	19.4%
Industrial HVAC	64,152	33.8%	58,000	29.0%	-6,152	-9.6%
Electrical systems	24,941	13.1%	25,000	12.5%	59	0.2%
Facility systems	11,113	5.8%	12,000	6.0%	887	8.0%
Facilities Construction Business	155,501	81.8%	161,000	80.5%	5,499	3.5%
Machinery Systems Business	8,973	4.7%	10,000	5.0%	1,027	11.4%
Environmental Systems Business	23,560	12.4%	27,000	13.5%	3,440	14.6%
Real Estate Business	2,375	1.2%	2,000	1.0%	-375	-15.8%
Others	815	0.4%	500	0.3%	-315	-38.7%
Adjustments	-1,158	-	-500	-	658	-
Gross profit	28,754	15.1%	32,000	16.0%	3,246	11.3%
Operating income	7,498	3.9%	9,500	4.8%	2,002	26.7%
Ordinary income	8,196	4.3%	10,000	5.0%	1,804	22.0%
Profit attributable to owners of parent	5,901	3.1%	7,000	3.5%	1,099	18.6%

Note: The amounts listed as “adjustments” serve to eliminate inter-segment transactions included in each segment.
Source: Prepared by FISCO from the Company’s Summary of Financial Results

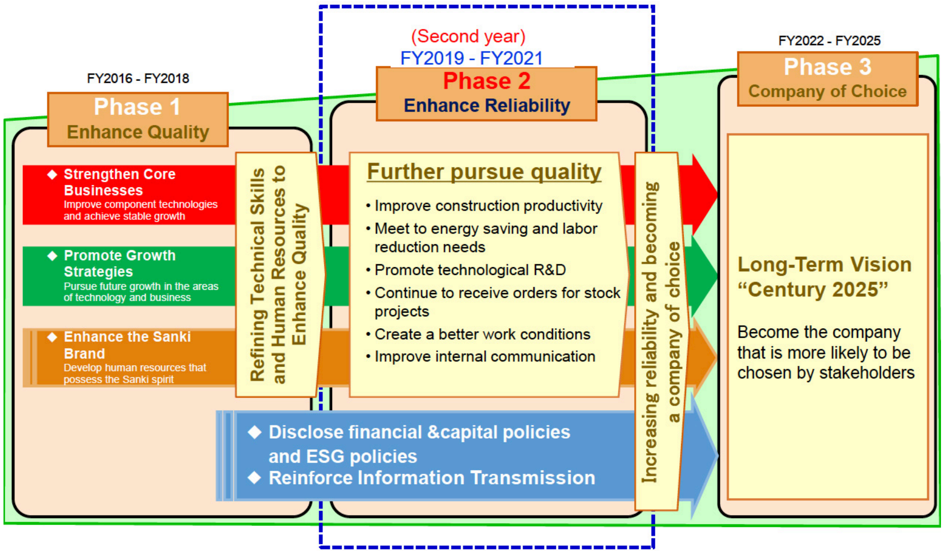
Medium-term management plan

Promoting “Century 2025” Phase2

1. What is the “Century 2025” long-term vision?

The Company has announced a 10-year long-term vision “Century 2025” that covers from FY3/17 to FY3/26, the 100th anniversary of its establishment. The ultimate goal of this long-term vision is to be “The Company of Choice.” The Company has divided the 10 years into three phases described below in order to achieve this goal and the Company’s policy is to implement business strategies promoted in each phase of medium-term management plan.

Long-term vision “Century 2025”



Source: Company’s Status of Business Progress in the Medium-Term Management Plan

2. Summary of FY3/21

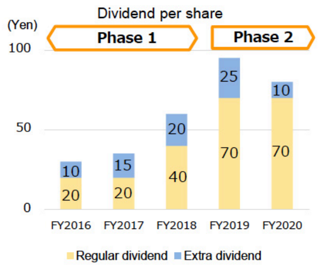
(1) “Century 2025” Phase 2 results targets and results

FY3/22 will be the final year of the “Century 2025” Phase 2 medium-term management plan, while in FY3/21, net sales, the gross margin, and ordinary income did not achieve their targets due to the impact of COVID-19. The final targets for Phase 2 in FY3/22 are an ordinary income margin of at least 5.0%, an annual dividend of at least ¥60, to acquire around 5 million treasury stocks (in the three years from FY3/20), a total return ratio of at least 70%, and ROE of at least 8.0%. It is unclear how long the impact of COVID-19 will extend into the future, but the Company’s policy at the current time is to leave the targets unchanged and continue to work toward achieving them. It has stated that “The future impact of COVID-19 is unclear and it may affect results, but we are resolutely progressing the “Century 2025” Phase 2 plan toward achieving the targets.”

"Century 2025" Phase 2 FY3/21 results and numerical targets

	Phase 2 (FY2019 to FY2021) targets					
	FY2019 targets	FY2019 results	FY2020 Targets	FY2020 Mid-term forecast	FY2020 results	FY2021 targets
Sales	200.0 billion yen	207.6 billion yen	200.0 billion yen	192.0 billion yen	190.0 billion yen	200.0 billion yen
Gross profit (margin)	30.0 billion yen (15%)	32.1 billion yen (15.5%)	31.0 billion yen (15.5%)	29.5 billion yen (15.4%)	28.7 billion yen (15.1%)	32.0 billion yen (16.0%)
Ordinary income (%)	9.00 billion yen (4.5%)	11.2 billion yen (5.4%)	9.5 billion yen (4.8%)	8.5 billion yen (4.4%)	8.1 billion yen (4.3%)	10.0 billion yen (5.0%)

	Phase 2 (FY2019 to FY2021) operating targets	FY2020 results
Operating profit ratio	5.0% or more (final fiscal year)	4.3%
Dividend	Annual dividend per share: 60 yen or more	Annual dividend: 80 yen
Acquisition of treasury stock	Approx. 5 million shares	1 million shares (total: 2,958 thousand shares)
Total return ratio	70% or more	97.3%
ROE	8.0% or more (final fiscal year)	6.6%



Source: Company's Status of Business Progress in the Medium-Term Management Plan

(2) Initiatives to improve "quality" and "trust"

"Century 2025" Phase 2 is a phase to pursue even further the "trust" placed in the Company and "quality."

To improve quality, the Company is promoting technological developments and addressing needs for energy saving and labor saving. Specifically, towards acquiring projects in the Facilities Construction Business, it has developed autonomous airflow measurement robots and is promoting measures to save energy and save labor by utilizing robots at construction sites. Moreover, it has developed an AI system to estimate moisture content of dewatered sludge, with the aim of saving energy throughout sludge processing facilities. In the energy saving and laborsaving area, the Company's supercharged fluidized bed furnance with a binary power generation system capable of generating power has been adopted for the Kitatama Water Reclamation Center No.1 Sludge Incineration Systems Reconstruction Project (Tokyo).

To improve the "trust" placed in it, the Company is working on three initiatives: 1) returning profits to shareholders (paying dividends and acquiring and retiring treasury stock), 2) reviewing the payment terms to partner companies, and 3) work-style reforms, improvements to internal communication, social contribution, and information dissemination.

1) Returning profits to shareholders (paying dividends and acquiring and retiring treasury stock)

As part of its efforts to return profits to shareholders, the Company actively acquires treasury stock on the stock market and retires them. From FY3/14 to FY3/21, the total amount the Company used to acquire treasury stock and for dividends was ¥34,919mn. The ratio in relation to the total profit attributable to owners of parent during this period of ¥40,678mn, or in other words, the total return ratio (weighted average), was 85.7%. This can be said to be an extremely high level even among the many listed companies. In FY3/22, which is the final fiscal year of "Century 2025" Phase 2, the Company is aiming to acquire around 5 million treasury stocks (it has already acquired 2,958,000 shares), for a total return ratio when combined with the dividend of at least 70%.

2) Reviewing the payment terms to partner companies

The Company is also actively responding to stakeholders other than shareholders. Specifically, it has reviewed the payment terms to partner companies and pays entirely in cash to those partner companies with capital of less than ¥40mn. Also in preparation for changes to social conditions in the future, including due to the impact of COVID-19, it has concluded a commitment line contract in order to secure capital to support partner companies and to prepare for temporary demand.

3) Work-style reforms, improvements to internal communication, social contribution, and information dissemination

For work-style reforms, the Company has launched the "Smile Project" led by the President, and it is striving to establish a pleasant working environment in every Group company, including by reviewing the work-leave system and reducing workloads at project sites. For internal communication, during the COVID-19 pandemic in which there tends to be a lack of communication, it is holding online opinion exchanges between the President and employees and between executives, while it also attempting to secure and train human resources. For social contribution, it has established the SANKI YOU Eco Contribution Points system and is subsidizing environmental conservation activities. In the event that the proposal and adoption of energy-saving equipment leads to CO_2 reductions at customers, it converts the amount reduced into Eco Contribution Points (1 point equals ¥100) to support tree-planting activities. FY3/21 was the 10th anniversary of the system's launch. For information dissemination, the Company is developing activities including posting Aurora Vision digital signage at every regional branch office and store for the new commercial and posters of "Kaiteki o katachi ni" (making your comfort a reality).

(3) Topics in each segment

Below, the topics for the initiatives for "Century 2025" Phase 2 in FY3/21 are summarized.

1) Facilities Construction Business

Sales from new orders stagnated for small-scale projects such as repairs due to the impact of the COVID-19 pandemic. However, the Company secured orders in excess of FY3/20 by catering to strong demand for semiconductors and 5G products, etc.

a. On-site introduction of new labor-saving construction technology (development and on-site introduction of autonomous airflow measurement robots)
b. Reduction of accidents and construction issues and complaints by utilizing Sanki Techno Center

2) Facility Systems Business

Office work-style consulting increased to prevent the spread of COVID-19

a. Establishment of the Consulting Promotion Department and provision of new consulting services
b. Strong orders received and sales of the Company's next-generation central monitoring system (SIer)

3) Machinery Systems Business

The need for labor-saving and automation through the use of robots has increased as orders received and sales to the manufacturing industry have stagnated due to the impact of the COVID-19 pandemic

a. Strong orders received and sales of hybrid systems that combine robotics and transport equipment

4) Environmental Systems Business

Orders received greatly increased as a result of increased need for national resilience

a. Order received for a large-scale project utilizing its first supercharged fluidized bed furnace with binary generation system
b. Development of AI system to estimate moisture content of dewatered sludge

3. Initiatives for ESG

The Company is also actively working on ESG activities.

The Company's ESG activities

Item	Content
E Environment	・Actively promoted energy conservation and energy generation (Received order for Kitatama Water Reclamation Center No. 1 Sludge Incineration Systems Construction Project) ・Newly created Kansha-no-Mori and conducted tree planting activities to commemorate the 10th anniversary of SANKI YOU Eco Contribution Points ・Dispatched employees to the National Institute of Polar Research Japanese Antarctic Research Expedition 
S Society	・Introduced a flextime system for all employees to promote work styles that leverage diversity ・Shortened required work hours in the interest of work-life balance ・Commenced Smile Plans at the four groups, in order to further promote work-style reforms ・Reviewed payment conditions to reform financing of partner companies ・Established the Sanki Group Procurement Policy with an awareness of CSR procurement
G Governance	・Selected external director as chairman of the Board of Directors ・Conducted interviews through a third-party institution in order to evaluate the effectiveness of the Board of Directors ・Advisory Committee on Nomination and Remuneration comprised of only external directors ・Ensured independence of legal affairs section as organization reporting directly to the president 

Source: Company's Status of Business Progress in the Medium-Term Management Plan

Shareholder return policy

Proactive stance toward shareholder return with dividend hikes and acquisition and retirement of treasury stock

The Company actively returns profits to shareholders. While its basic annual dividend was ¥15 through FY3/14, a change in profit structure prompted a dividend increase beginning in FY3/15. Due to strong results in FY3/19, the Company implemented an extra year-end dividend of ¥20 in addition to the regular ¥40 dividend, for a total annual dividend of ¥60 (a dividend payout ratio of 40.0%). In FY3/20, the Company had an initial annual dividend target of at least ¥60 and raised the dividend to ¥95 (¥35 interim, ¥60 year-end) including a ¥25 extra dividend to reflect robust earnings. In FY3/21, it paid an annual dividend of ¥80, comprised of a regular dividend of ¥70 and an extra dividend of ¥10. In FY3/22, it currently plans to sustain the regular dividend at ¥70.

The Company actively acquires its own shares in the market and retires them as part of the shareholder return policy. It acquired 1,958,000 shares and retired 2,000,000 treasury stocks during FY3/20. Meanwhile, thus far in FY3/21 the Company has already retired 1,000,000 shares and has acquired another 1,000,000 treasury stocks. The total return ratio (weighted average) from FY3/14 to FY3/21 was 85.7%, which is an extremely high ratio. Going forward also, during the period of the "Century 2025" Phase 2 medium-term management plan, it is aiming to acquire around 5 million treasury stocks in the three years from FY3/20, for a total return ratio when combined with the dividend of at least 70%. So going forward, we shall be focusing on its dividend policy and acquisitions of treasury stock.

Also, as previously stated, the Company actively responds to stakeholders other than shareholders. For the payment terms for partner companies, it has changed to entirely cash payments for partner companies with capital of less than ¥40mn. Looking to the future, it is preparing for uncertain social conditions due to COVID-19 by securing capital to support partner companies and to prepare for temporary demand.

We think the Company should be favorably assessed for its positive stance in shareholder return and relationships with various stakeholders.

Shareholder returns

	Acquisition of treasury stock		Dividend amount (B)	Amount of shareholder returns (C) = (A) + (B)	Profit attributable to owners of parent
	Number of shares	Amount (¥mn) (A)			
FY3/21	1,000,000	1,171	4,568	5,739	5,901
FY3/20	1,958,000	2,899	5,543	8,442	7,576
FY3/19	1,000,000	1,191	3,595	4,786	9,046
FY3/18	3,000,000	3,679	2,136	5,815	3,906
FY3/17	0	0	1,906	1,906	4,698
FY3/16	0	0	1,906	1,906	5,327
FY3/15	2,000,000	1,604	1,270	2,874	2,461
FY3/14	4,000,000	2,408	983	3,391	1,763
Total:				34,859	40,678
Total return ratio (weighted average):					85.7%

Source: Prepared by FISCO from the Company's financial results and Summary of Financial Results

Disclaimer

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