COMPANY RESEARCH AND ANALYSIS REPORT

Wacom Co., Ltd.

6727

Tokyo Stock Exchange First Section

3-Dec.-2020

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Index

Summary

In 1H FY3/21, sales and profits increased significantly and were higher than expected. Is capturing the increase in demand for online education due to the coronavirus pandemic

Wacom Co., Ltd. <6727> (hereafter, also "the Company") is the global leading manufacturer aiming to create value for customers based on technologies in the field of digital pen and ink. It dominates in brand clout and market share supported by professional creators such as designers and animators who work in studios for movie production or industrial design studios. Its two business segments are the Branded Business, in which it sells its own-brand Displays (LCD pen tablets) and Pen Tablets and other products, and the Technology Solution Business, in which it supplies proprietary digital pen technology as a component to manufacturers of finished products, including smartphones and tablets.

1. 1H FY3/21 results

In the 1H FY3/21 consolidated results, net sales increased 17.9% year on year (YoY) to ¥55,326mn and operating profit rose 186.4% to ¥8,618mn. So sales and profits increased significantly and were higher than expected, hitting new record-high results (on a 1H basis). Alongside the global spread of the novel coronavirus pandemic (hereafter, the coronavirus pandemic), results were affected by factors such as self-restraint on sales-promotion events and restrictions on sales activities. However, demand rapidly increased, including for online education and teleworking, and as a result, results grew significantly in the Branded Business, mainly of Displays and Pen Tablets. In the Technology Solution Business also, results grew for manufacturers for which the Company is the OEM supplier. In other words, benefitting from the coronavirus pandemic, it can be evaluated that the Company captured both growth in new demand (a structural factor) and demand that has been pushed forward (a temporary factor), which led to results that were significantly higher than expected. In profit-loss, it realized a major increase in operating profit because factors including the effect of the higher sales, improvements to the product mix, and optimization of SG&A expenses absorbed the impact of factors like additional tariffs placed on China by the United States and the exchange rate (the strong yen).

2. FY3/21 results outlook

For the FY3/21 consolidated results outlook, based on factors including the 1H results, the Company has upwardly revised the initial forecasts (in a range format) and shifted to single values using baselines. The revised forecasts are for higher sales and profits for the full fiscal year as well, with net sales to increase 11.8% YoY to ¥99,000mn and operating profit to rise 61.7% to ¥9,000mn. To achieve the full fiscal year forecasts, net sales must be ¥43,674mn and operating profit ¥382mn in 2H. Reasoning for the conservative figures in the 2H results forecasts include uncertainly regarding economic activities due to the coronavirus pandemic and for the portion that results exceeded 1H forecasts, there may be a decrease in 2H as a rebound from demand that was pushed forward, so the Company appears cautious. It uses the term "baseline" for forecasts to express the portion that exceeds the numerical forecasts which is highly likely to achieve, and has stated at the financial results briefing that it actively targets opportunities (for results to exceed forecasts) that are difficult to quantify numerically at the current time through measures intended for the next fiscal period and onward.

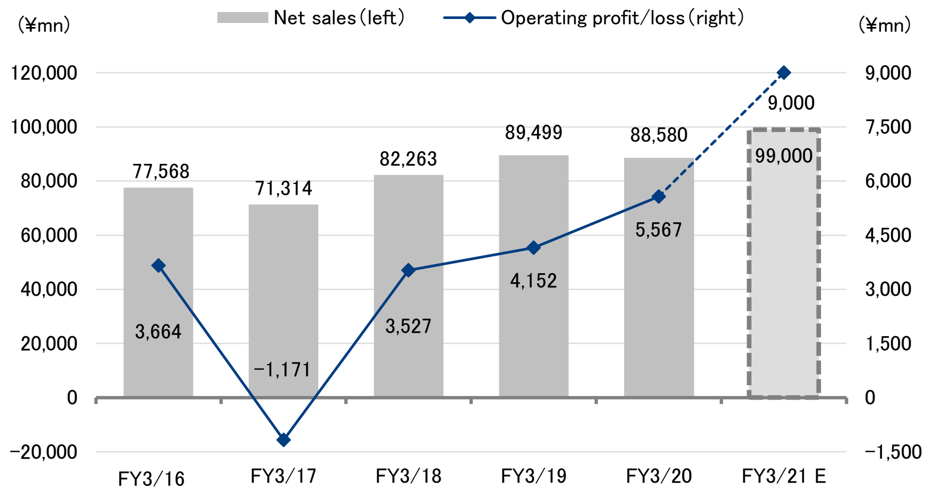
3. Growth strategy

The Company is progressing Wacom Chapter 2, its medium-term business plan for FY3/19–22. Looking toward the plan's third year, its aim is to achieve sustainable growth by returning to its roots as a Technology Leadership Company and creating customer-oriented value while constantly staying at the market forefront in pen and ink digital technology. To accomplish this, it is implementing three company-wide strategies set out in the plan: 1) Advancing technology leadership, 2) Close cooperation through island and ocean (island business = branded business; ocean business = technology business) and 3) Bold selection and concentration. The flow of digitization is clearly benefitting the Company, so we shall be focusing on the results of its activities with an eye to entering a new growth stage in the future.

Key Points

- In 1H FY3/21, sales and profits increased significantly due to higher demand, including for online education
- By capturing new demand due to the coronavirus pandemic, sales of Displays and Pen Tablets grew greatly
- For the FY3/21 results outlook, has upwardly revised the initial forecasts (in a range format) and shifted to single values using baselines. Is forecasting a major increase in sales and profits for the full fiscal year as well
- As a Technology Leadership Company, is aiming for sustainable growth through customer-oriented value creation while taking the lead in the market through its pen and ink digital technologies

Results trends



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

Business overview

Global leader aiming to create value for customers based on technologies in the field of digital pen and ink

The Company is the world's leading company aiming to create value for customers based on technologies in the field of digital pen and ink. It sells products in more than 150 countries worldwide and dominates in brand clout and market share supported by professional creators such as designers and animators who work in studios for movie production or industrial design studios. Furthermore, as a Technology Leadership Company, it broadly supplies the latest digital pen technology to partner companies manufacturing smartphones, tablets, digital stationery, and other products and is fostering a business field that specializes in education with partners from the educational industry.

The Company is also striving to create new growth opportunities by rebuilding product lineups and further evolving the business model amid major changes in the market environment, including tougher competition in low- and mid-priced product categories and evolution of user needs and workflow accompanying advances in digital technologies (IoT, VR/MR, AI, and others) and the communications environment (mobile, cloud, 5G, and others). In particular, although at the current time the coronavirus pandemic is having both positive and negative effects, the Company is entering the next growth phase by capturing new demand from the new normal.

Its two business segments are the Branded Business, which sells the Company's own-brand Displays, Pen Tablets and other products, and the Technology Solution Business, which supplies proprietary digital pen technology as a component to manufacturers of finished products, including smartphones and tablets. Looking at results trends up to the previous period, while the Branded Business, the Company's core business since its founding, had slowed, the Technology Solution Business was growing at a healthy pace as the market expanded and had surpassed the Branded Business in sales mix*. However, at the present time, the Branded Business is also showing signs of a recovery.

* Breaking down sales by segment for 1H FY3/21, the Branded Business accounted for 47.1% and the Technology Solution Business accounted for 52.9%.

With the overseas sales ratio (overseas local entity sales ratio excluding the Technology Solution Business) at about 85%*, careful attention should be given to the impact of foreign exchange market fluctuations on earnings (in particular, fluctuations in the euro-yen rate have a major impact on operating profit).

* Asia-Oceania sales at about 30.8%, (of which China at 15.0%), European sales at about 25.0% and US sales at about 29.3%.

Additionally, while development sites are practically all concentrated in Japan, excluding developments of digital ink and security-related software (which are mainly in Europe), the Company consigns production to multiple overseas partners (almost entirely in China). It plans to increasingly diversify production sites to Southeast Asia and other nearby areas from the standpoint of alleviating supply-chain concentration risk.

Business and major product features

Promoting updates in the product portfolio that address changes in the business environment and de facto standardization of proprietary technologies

1. Branded Business

The Company has a broad lineup for target customers and product types. It sorts products into two categories: (1) Creative Solution and (2) Business Solution*.

* In order to conduct a more appropriate results briefing through reflecting changes in the business environment, the Company changed aspects such as category ranges and names of business segments from FY3/21. Specifically, the previous three product categories of the Creative Business, the Consumer Business, and Business Solution were reduced to two, and the Creative Business was renamed Creative Solution. It also integrated the Consumer Business with Mobiles within Creative Solution.

(1) Creative Solution

This is the core business since the Company's founding and possesses strong brand clout and market share with professional creators. Product types include Displays, Pen Tablets and Mobiles, and understanding their differences is important in assessing the competition environment and growth potential.

a) Displays

This category covers products that use an LCD panel as the tablet* and are similar to Mobiles, which are explained below, in terms of directly writing on an LCD screen with a digital pen. Meanwhile, they are also PC peripherals, similar to Pen Tablets as an input device that does not have an OS or storage feature. Prices for larger products range from around ¥200,000 to ¥400,000. Users are mainly professionals and advanced amateurs, and the Company holds an overwhelming share in this market. In response to market changes (such as expanded scope and demand shift from Pen Tablets), it released multiple new models including a 16-inch entry model with an actual sales price in the ¥60,000 to 70,000 range (tax exclusive; same below) in January 2019, a 22-inch model (actual sales price in the ¥100,000 to 110,000 range) in July 2019, and a 13-inch model for beginners (actual sales price in the ¥30,000 to 40,000 range) in January 2020. The Company is steadily expanding results even in the entry model segment where it faces tough price competition from other companies (Chinese manufacturers, etc.).

* Sometimes referred to as "LCD tablets" too.

b) Pen Tablets

The most basic device* consists of a digital pen and tablet (blackboard type) and has contributed to the Company's results as a mainstay product. It is a PC peripheral used over a connection to a PC, similar to a mouse or keyboard. The Company offers a broad lineup that ranges from professional to beginner products thanks to a simple configuration. While it is sustaining competitiveness in the professional high-end market, competition has intensified in the low- to mid-priced category where it is difficult to achieve differentiation. Furthermore, since the Company has strategically shifted management resources in response to a demand shift toward Displays with better operability and lower prices, sales have been steadily trending downward in the past few years.

* Sometimes referred to as "opaque tablets for drawing" too.

c) Mobiles, others.*1

The Mobiles category covers Displays for use as an input device that contain an OS and storage feature. From the standpoint of usability, they are the same as standard tablets with general pen entry support (many of these products utilize the Company's pen sensor system) and might even appear to have a competitive relationship (fostering competition with the Technology Solution Business in the Company's case). However, the difference is obvious to users who place emphasis on input performance, and it makes more sense for general users who do not have this focus to select standard tablets rather than the Company's Mobiles that function focusing on input devices. These products hence have clear segmentation in performance and functionality. Also, in products other than Mobiles, it sells a group of products that are used, for example, to create illustrations and notes on a digital device, such as the stylus pen for Windows tablets for general consumers, smart pads*2, and digital stationery.

*1 Integrated the Consumer Business into the former Mobiles category.
*2 This is a notebook-type device capable of converting handwritten memos written on paper with the provided pen to digital file formats.

(2) Business Solution

The Company sells business-use products that are capable of direct drawing and character entry on an LCD screen. Usage is increasing in digital signature (hotel check-in, credit card payments, etc.) and medical (electronic medical records, etc.) areas.

2. Technology Solution Business

This business is divided into two segments, AES Technology Solution and EMR Technology Solution, based on digital pen technologies*. It supplies pen sensor systems to smartphone and tablet and notebook PC manufacturers. In particular, the Company is expanding sales to Samsung Electronics <KRX: 005930> (Galaxy Note series) in smartphone-related use, a growing market. Tablet and notebook PC manufacturers highly rate the Company's technology, and it deals with major manufacturers and the number of projects is steadily growing. The Company aims to expand business scale through promotion of its proprietary digital pen technology as a de facto standard, while expanding the scope of users.

* The Company's technologies consist of Active ES (proprietary electrostatic coupling, battery required for pen) format technology and EMR (electro-magnetic resonance) rapid, high-precision positioning sensors (battery not required).

Financial highlights

In 1H FY3/21, sales and profits increased significantly and were higher than expected. Results, including for online education, grew greatly due to the coronavirus pandemic

1. 1H FY3/21 results

In the 1H FY3/21 consolidated results, net sales increased 17.9% YoY to ¥55,326mn, operating profit rose 186.4% to ¥8,618mn, ordinary profit climbed 232.4% to ¥8,469mn, and profit attributable to owners of parent grew 184.5% to ¥6,282mn. So sales and profits increased significantly and were higher than expected, hitting new record-high results (on a 1H basis).

For sales, alongside the global spread of the coronavirus pandemic, demand rapidly increased, including for online education and for teleworking. As a result, sales increased greatly in the Branded Business, mainly of Displays and Pen Tablets. In the Technology Solution Business as well, sales in the EMR Technology Solution segment steadily grew to manufacturers to which the Company is an OEM supplier.

In profit-loss, gross profit greatly increased, mainly due to the effects of the higher sales and improvements to the product mix (particularly the growth of Pen Tablets, which have a high profit margin). As a result, this absorbed impacts like additional tariffs placed on China by the United States and the exchange rate (the strong yen mainly against Asian currencies). So operating profit greatly increased, and the operating profit margin also rose significantly to 15.6% (from 6.4% in the same period in the previous fiscal year). For SG&A expenses, personnel expenses increased, mainly for the provision for bonuses and related to the results-linked remuneration system. However, the SG&A expenses ratio still improved to 21.8% (from 26.0% in the same period in the previous fiscal year), mainly due to efforts to optimize various costs and the restrictions on sales activities due to the coronavirus pandemic (reductions in advertising and sales promotion expenses).

In the financial condition, capital increased 19.0% on the end of the previous period to ¥32,999mn due to the accumulation of retained profit. Total assets also increased 37.3% to ¥70,244mn, reflecting seasonal factors by which trade receivables and inventories increased due to the higher sales alongside the securing of liquidity on hand (cash and deposits.) Therefore the equity ratio declined to 47.0% (from 54.2% at the end of the previous period).

1H FY3/21 financial results

(¥mn)

	1H FY3/20		1H FY3/21		Change	
	Results	% of sales	Results	% of sales	Amount	%
Net sales	46,932		55,326		8,393	17.9%
Branded Business	19,329	41.2%	26,053	47.1%	6,723	34.8%
Technology Solution Business	27,602	58.8%	29,273	52.9%	1,670	6.1%
Cost of sales	31,726	67.6%	34,631	62.6%	2,904	9.2%
SG&A expenses	12,195	26.0%	12,076	21.8%	-119	-1.0%
Operating profit	3,009	6.4%	8,618	15.6%	5,608	186.4%
Branded Business	-170	-0.9%	4,276	16.4%	4,446	-
Technology Solution Business	5,105	18.5%	6,481	22.1%	1,376	27.0%
Adjustment	-1,925	-	-2,139	-	-214	11.1%
Ordinary profit	2,548	5.4%	8,469	15.3%	5,921	232.4%
Profit attributable to owners of parent	2,207	4.7%	6,282	11.4%	4,074	184.5%

	Results at end of March 2020	Results at end of September 2020	Change	
			Amount	%
Total assets	51,155	70,244	19,088	37.3%
Shareholders' equity	27,734	32,999	5,264	19.0%
Equity ratio	54.2%	47.0%	-7.2pt	-

Note: Figures in the financial results have been rounding to the nearest million yen.
Source: Prepared by FISCO from the Company's financial results

Breakdown of SG&A expenses

(¥mn)

	1H FY3/20 results	1H FY3/21 results	Change	
			Amount	%
Personnel expenses	4,586	5,350	764	16.6%
R&D expenses	2,065	1,978	-87	-4.2%
Sales promotion and advertising expenses	1,235	826	-409	-33.1%
Outsourcing expenses	658	602	-56	-8.5%
Depreciation	492	330	-162	33.0%
Other	3,161	2,993	-168	-5.3%
Total	12,196	12,077	-119	-1.0%

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

2. Results overview by segment

(1) Branded Business

Net sales increased 34.8% YoY to ¥26,053mn and segment profit was ¥4,276mn (compared to a loss of ¥170mn in the same period in the previous fiscal year), and both increased significantly and were higher than expected. Net sales by product are shown below.

Earnings breakdown in the Branded Business

(¥mn)

	1H FY3/20 results	1H FY3/21 results	Change	
			Amount	%
Creative Solution	17,375	24,425	7,050	40.6%
Displays	8,212	10,759	2,547	31.0%
Pen Tablets	8,090	12,580	4,490	55.5%
Mobiles, others	1,073	1,086	13	1.2%
Business Solution	1,954	1,628	-326	-16.7%

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

a) Creative Solution sales

Net sales increased greatly, rising 40.6% YoY to ¥24,425mn. They were partially affected by factors such as self-restraint on sales promotion events and restrictions on sales activities due to the coronavirus pandemic. However, because of the increase in demand, including for online education, sales grew rapidly of entry models in the mainstay Displays and low-to mid-priced models in Pen Tablets. In particular, in Displays, sales of entry models such as the 22-inch size announced in July 2019 and the 13-inch size announced in January 2020 grew significantly. Also, sales of low-to mid-priced models in Pen Tablets, which had been contracting due to intensifying competition, changed direction and increased significantly. Alongside this, the Company was able to secure an increase in sales for the professional models as well, even while being impacted by the restrictions on sales activities. Therefore, benefitting from factors such as the spread of online education and teleworking due to the coronavirus pandemic, it can be evaluated that results grew significantly from the Company capturing both the growth in new demand (a structural factor) and the existing demand for creatives that has been pushed forward (a temporary factor). On the other hand, for Mobiles, others., although sales of Mobiles increased greatly from the updating of the product lineup in the previous period, overall sales grew only slightly because of the decline in sales of stylus pens in products other than Mobiles.

b) Business Solution sales

Sales decreased 16.7% YoY to ¥1,628mn. In addition to the impacts of market trends and changes to the competitive environment, results were affected by restrictions on sales activities. Therefore, sales of liquid crystal sign tablets for financial institutions, mainly in Europe, decreased significantly.

On the other hand, profit-loss in the Branded Business was affected by the strong yen (negative impact of approximately ¥100mn) and directly affected by additional tariffs placed on China by the United States (negative impact of around ¥300mn). But the Company still realized a major increase in profits, mainly from the effects of the higher sales and improvements to the product mix. The segment profit margin also rose greatly to 16.4%, and it is considered that the recovery of Pen Tablets, which have an especially high profit margin, contributed significantly.

(2) Technology Solution Business

Net sales increased 6.1% YoY to ¥29,273mn and segment profit rose 27.0% to ¥6,481mn, resulting in major increases in sales and profits. Net sales by solution (technology) are described below.

Earnings breakdown in the Technology Solution Business

(¥mn)

	1H FY3/20 results	1H FY3/21 results	Change	
			Amount	%
Technology Solution	27,603	29,273	1,670	6.1%
AES technology	9,433	8,987	-446	-4.7%
EMR Solution, others	18,170	20,286	2,116	11.6%

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

a) AES Technology Solution sales

Net sales decreased 4.7% YoY to ¥8,987mn. They were affected by factors including production and supply-side restrictions due to the coronavirus pandemic.

b) EMR Technology Solution, others sales

Net sales grew steadily, up 11.6% YoY to ¥20,286mn. Sales rose greatly due to an increase in demand from manufacturers for which the Company is an OEM supplier.

3. Key takeaways of 1H FY3/21 results

Comprehensively assessing the 1H FY3/21 results from the above, although there are factors adversely affecting some of the results, including restrictions on sales activities due to the coronavirus pandemic, the results can be evaluated positively as being significantly higher than expected from the Company capturing new demand. In particular, for online education, the measures it has conducted up to the present time for this growth field can be viewed as bearing fruit, and going forward, it seems we can expect results to grow sustainably. On the other hand, for nesting-type demand generated due to the coronavirus pandemic, it is undeniable that part of this demand has been pushed forward from the end-of-year shopping season in a typical year, so it will be necessary to pay close attention to this point.

Outlook

Has upwardly revised results forecasts for the full fiscal year and shifted to single values using baselines. The outlook for the full fiscal year is for new record-high results from major increases in sales and profits

For the FY3/21 consolidated results outlook, based on factors including the 1H results, the Company has upwardly revised the initial forecasts (in a range format) and shifted to single values using baselines. The revised forecasts are for higher sales and profits and new record-high results for the full fiscal year as well, with net sales to increase 11.8% YoY to ¥99,000mn, operating profit to rise 61.7% to ¥9,000mn, ordinary profit to climb 69.4% to ¥8,800mn, and profit attributable to owners of parent to grow 60.8% to ¥6,300mn.

Sales are expected to grow in both the Branded Business and Technology Solution Business. In profit-loss also, even while the Company continues to actively invest in R&D for the future, a major increase in profits is forecast from the effects of the higher sales, improvements to the product mix, and optimization of SG&A expenses.

To achieve the forecasts for the full fiscal year, net sales of ¥43,674mn and operating profit of ¥382mn in 2H will be sufficient. The reason for the conservative figures in the 2H results forecasts, despite the fact that 1H results largely exceeded forecasts, is that the level is the required minimum that must be achieved after considering the main factors behind the anticipated downturn. That is to say, the Company appears to be cautiously looking at the possibility that there may be a decrease in 2H as a rebound from the demand that was pushed forward, in addition to the uncertainty of economic activities in conjunction with the coronavirus pandemic. Its intention in using "baselines" is to show the portions that exceed the minimum levels that must be achieved, and actively target opportunities (for results to exceed forecasts) that are difficult to quantify numerically at the current time and through measures intended for the next fiscal period onwards as well.

Forecasts for FY3/21

(¥mn)

	1H FY3/20		1H FY3/21			Change	
	Results	% of sales	Initial forecasts	Revised forecasts	% of sales	Amount	%
Net sales	88,580		89,000~91,500	99,000		10,420	11.8%
Branded Business	42,587	48.1%	42,500~43,500	51,000	51.5%	8,413	19.8%
Technology Solution Business	45,993	51.9%	46,500~48,000	48,000	48.5%	2,007	4.4%
Operating profit	5,567	6.3%	5,600~6,500	9,000	9.1%	3,433	61.7%
Branded Business	1,706	4.0%	2,800~3,200	5,700	11.2%	3,994	234.0%
Technology Solution Business	7,650	16.6%	7,000~7,500	7,800	16.3%	150	2.0%
Adjustment	-3,789	-	-	-4,500	-	-710	18.7%
Ordinary profit	5,194	5.9%	5,600~6,500	8,800	8.9%	3,606	69.4%
Profit attributable to owners of parent	3,917	4.4%	4,000~4,600	6,300	6.4%	2,383	60.8%

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

Below we review results outlooks by business area.

(1) Branded Business

Sales and profits are forecast to increase significantly, with net sales rising 19.8% YoY to ¥51,000mn and segment profit growing 234.0% to ¥5,700mn. The Company intends to grow sales mainly for entry models of Pen Tablets and Displays by capturing demand, such as for online education for which the market continues to expand. In profit-loss, the outlook is that it will realize a major increase in profits from the effects of the higher sales, improvements to the product mix, and optimization of SG&A expenses, and for the segment profit margin to improve greatly to 11.2% (from 4.0% in the previous period).

(2) Technology Solution Business

The forecasts are for higher sales and profits, with net sales to increase 4.4% YoY to ¥48,000mn and segment profit to grow 2.0% to ¥7,800mn. While cautiously considering the impact of the coronavirus pandemic, the Company intends to maintain and develop strong relationships with its main customers, and at the same time, to acquire earnings by generating new business opportunities, including for education. In profit-loss as well, the outlook is that it will secure an increase in profits through the effects of the higher sales, even while actively investing in R&D for the future, and that it will maintain the segment profit margin at the high level of 16.3% (16.6% in the previous period).

FISCO's analysts consider that, although it is necessary to keep in mind the risk factors of the impact of the coronavirus pandemic and the possibility of a rebound decrease from demand being pushed forward, if based on the growth of new demand, including for online education, it is fully possible that the Company will achieve its results forecasts based on the baselines, and the key point will rather be by how much results will exceed them. For example, if the market's structural changes become clear despite demand temporarily falls in 2H, this is likely to be important information for determining growth potential in the future. In particular, we shall be focusing on the recovery of Pen Tablets, whose sales had been contracting up to the present time, and the changes in profitability alongside this.

Results trends in past years

Technology Solution Business driving growth over the past few years

Looking at how sales trended up to the previous period, the large slump in FY3/17 occurred because of the combined impacts of yen appreciation (especially against euro), product cycle movement, product recalls by Samsung Electronics, and other factors. Since then, however, sales recovered with growth in the Technology Solution Business and reached an all-time high in FY3/19. Nevertheless, Branded Business sales have been trending lower with the structure of positive growth in the Technology Solution Business continuing to offset its decline.

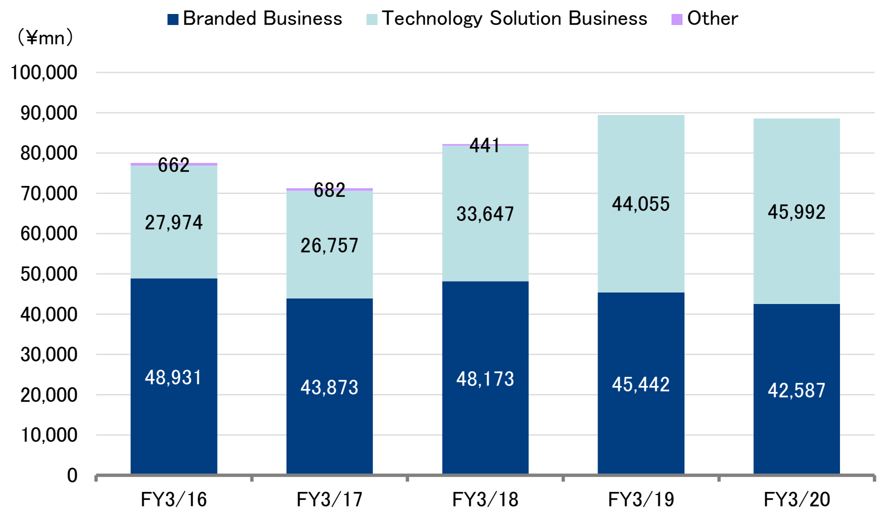
The main reason for downturn in Branded Business sales has been the need for time to respond to changes in the market environment in mainstay Pen Tablets as strategic demand shifts to Displays, amid growing competition in low- to mid-priced products in Pen Tablets, has not generated a sufficient offset in sales yet. However, Displays is steadily developing a new market and ramping up sales with entry models with high profit margins, and it is important to recognize change in the sales mix (ratios).

Growth in the Technology Solution Business over the past few years, meanwhile, reflects expansion of the market for pen sensor systems for tablets and notebook PCs and strong performance in pen sensor systems for smartphones (particularly with Samsung Electronics' Galaxy Note series) aided by enhanced functionality.

In profit-loss, the operating profit margin stayed in the 4% range (other than in FY3/17 when the Company incurred an operating loss) due to aggressive R&D activities and new product development. However, the Company successfully raised its profit margin in FY3/20, while sustaining the R&D investment level, mainly by optimizing SG&A expenses and other measures.

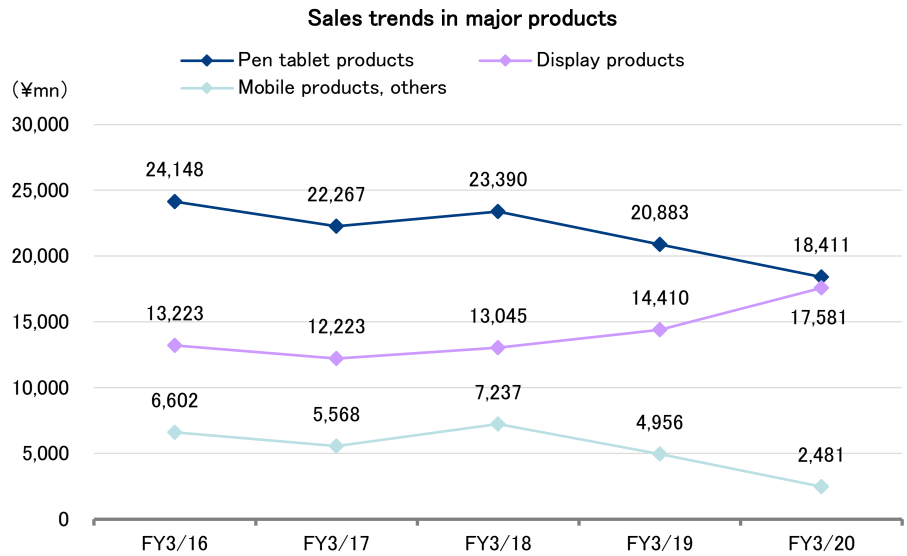
In financial standing, while the capital ratio temporarily slipped in FY3/17 on a hefty net loss due to recording impairment losses, it has steadily improved since then with buildup of retained profits and has moved close to 60%, the near-term goal for financial soundness. ROE, which reflects capital efficiency, has also been at about 15% in the past two fiscal years, and we think the Company has a well-balanced financial position.

Trends in net sales by business

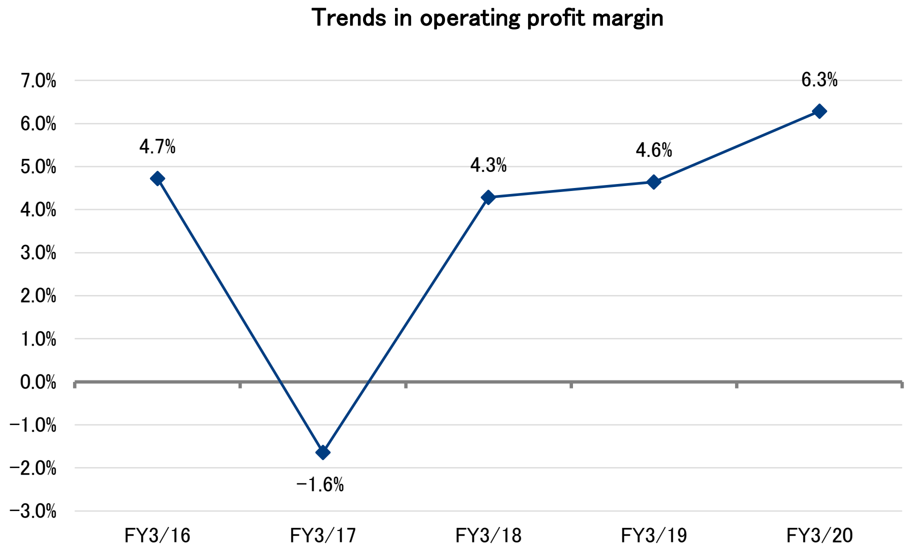


Source: Prepared by FISCO from the Company's financial results

Results trends in past years

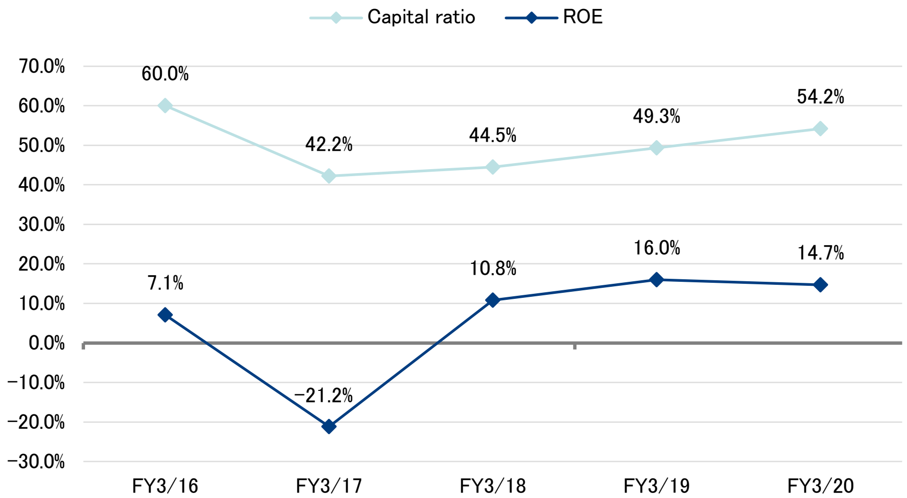


Source: Prepared by FISCO from the Company's financial results



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

Trends in capital ratio and ROE



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

Growth strategy

Is progressing the medium-term business plan, with FY3/22 as its final fiscal year. Has in sight achieving the targets, both numerical and strategies

1. Medium-term business plan

The Company announced Wacom Chapter 2, a new medium-term business plan (covering FY3/19–22), in May 2018 after Nobutaka Ide became President & CEO in April 2018, and the plan's third year is approaching. Besides full-fledged expansion of the pen input device market and the accompanying tougher competition, there has been a significant evolution of user needs and workflow related to advances in digital technology (IoT, VR/MR, AI, etc.) and the communications environment (mobile, cloud, 5G, etc.) including the professional-use segment where the Company holds advantages. In response to these changes in the business environment, the Company aims to achieve sustainable growth by returning to its roots as a Technology Leadership Company and creating value needed by customers while constantly staying at the market forefront in pen and ink digital technology. To accomplish this, it is implementing three company-wide strategies set out in the plan: 1) Advancing technology leadership, 2) Close cooperation through island and ocean and 3) Bold selection and concentration. Plan goals are ¥100,000mn in net sales, ¥10,000mn in operating profit (10% profit margin), ¥6,948mn in profit attributable to owners of parent, 15–20% ROE, and a roughly 60% capital ratio in FY3/22. Although the Company is being impacted by factors such as the US tariff hike on imports from China and the spread of the coronavirus pandemic, it is making steady progress for the strategies, including making progress toward the numerical targets, and it does not need to majorly revise the direction. We think it is important for management to positively utilize changes to the market environment and present a path from a long-term perspective on how it intends to boost potential in the last year of the plan period ahead of the next plan (Chapter 3).

2. Growth strategies and progress

(1) Advancing technology leadership

The Company plans to lead the market by continually improving the experience through aggressive investments in alliances with partner companies and technology innovation. Technology innovation from a user-first perspective is a particularly important strategic theme. For example, collaboration with software is vital in addressing new user needs and workflow evolution, such as joint work with multiple and remote creators and new creation experiences freely utilizing 2D and 3D, and it is also working on new approaches, such as progressing collaborations with users from the development stage. The Company has arranged alliances with partner companies, focusing on virtual reality (VR), mixed reality (MR), and other next-generation technologies, digital stationery, display monitors and cutting-edge technological fields such as 5G. On entering this fiscal period, it has continued to achieve various results, including announcing the Hi-uni DIGITAL for Wacom, a digital pencil in collaboration with Mitsubishi Pencil Co., Ltd. <7976> (August 2020), and entering into a comprehensive business alliance agreement with Zoshinkai Holdings Inc. (Z-KAI Group) for the use of Handwriting x Digital in the education field (October 2020).

(2) Close cooperation through island and ocean

The Company is moving in a direction of accelerating growth by combining different characteristics through collaboration of island and ocean businesses, namely the branded businesses and technology businesses. While the Branded Business pursues technology innovation through provision of new user-first experiences as explained above, the Technology Solution Business seeks expanded scale through promotion of proprietary technologies as a de facto standard, while expanding the scope of users. Manufacturers have reacted favorably to the Company's pursuit of a de facto standard for digital pen technology (EMR and active ES formats) that transcends OS boundaries, and the number of projects for next-generation products is steadily increasing.

(3) Bold selection and concentration

Key measures of the Company's strategy are steady updates to the product portfolio in response to market changes and profitability enhancement by optimizing SG&A expenses. The Company has successfully ramped up an entry model Display originally released in January 2019 and recruited a user segment between professionals and general users (freelancers, students studying design, and others). Moreover, at the current time, benefiting from the coronavirus pandemic, demand is rapidly increasing for online education, and results are starting to appear toward acquiring this new demand. In optimization of SG&A expenses, the Company is conducting prioritized capital allocation sustaining R&D expenses at a high level aimed at achieving sustainable growth, while trying to improve the efficiency of other expenses as much as possible.

3. Future direction (headed toward Chapter 3)

Evolution of digital technology and the communications environment is accelerating, and these trends are creating major possibilities in digital pen and ink potential. The Company intends to proceed with activities that envision digital innovation in education (such as individual optimized education using AI), new work styles (remote and online collaboration), expanded content demand (expansion in apps and devices), creative workflow evolution (3D creation, cloud-based creation), and new pen experiences (foldables*, large screens, smart homes, etc. relating to the spread of objects drawn with a digital pen). It also wants to redefine value proposition from "tool" to "drawing and writing experience" and engage in business that combines hardware and services. The Company has advocated the following two strategy approaches for the future.

* Refers to smartphones that can be folded.

(1) Branded Business strategy

Mainly in Displays, the Company will revamp its product portfolio to extend from users who are beginners with strong creative interest to professionals. Additionally, it will promote development of XR drawing* as a new creation experience and offer a new subscription (service fee) business model via community development and enhanced support. It also intends to develop the corporate market for signature authentication solutions too.

* The X in XR (X Reality) indicates a variable. This is a general term covering VR (virtual reality), MR (mixed reality), and other technologies.

(2) Technology Solution Business strategy

The Company will strengthen new solution development in the increasingly digitized education market by working with partners. In particular, it wants to develop business models that combine parts and services and recruit value-added deals in foldables, large digital white boards, digital notes, and other areas. The Company will seek to strengthen its technology position as a de facto standard by building the Wacom Standard Pen Community and promoting other efforts.

FISCO's analysts consider that the numerical targets in the medium-term business plan are fully achievable taking into account the expansion of new demand and growth in results at the present time. Rather, what we should be focusing on is the direction and speed of the market changes from a medium- to long-term perspective and the progress made for the Company's strategies. In particular, the key points appear to be how the Company is leading changes in the market through its proprietary technological innovations and partner strategy, and its independent initiatives as a Technology Leadership Company. One part of this would seem to be what can be understood through the latest demonstrations and lectures with each partner at Connected Ink*, which is the open event held in Tokyo in the fall of each year. The flow of digitization is clearly benefitting the Company, and we shall be focusing on the results of its activities with an eye to entering a new growth stage in the future.

* This year it was held on November 18, 2020, the fifth time it has been held. The content of the event was partners in different industries and cultures, including art, technology, stationary, and education; the joint creation of "creative chaos" with "digital ink" as the keyword; and asking what is created from this. (Due to the coronavirus pandemic, the event was held in a hybrid format of online and at a Shinjuku venue, in a format of disseminating information for 24 hours while relaying between global bases).

Initiatives for society

Supporting a sustainable society through provision of "lifelong ink"

The Company places emphasis on initiatives that contributes to ESG improvements and a sustainable society. It posts information on the "Social Initiatives" section of the Company website and discloses its fundamental views and specific activities. We think the Company's use of a concept of "lifelong ink" (technology that richly communicates the gradations of life covering from happiness to sadness for children to adults) to describe its technology stands out. This reflects awareness of the origins of its significance and value creation in support for a sustainable society by facilitating "writing and drawing" experiences that accumulate throughout a person's life and communicating them to future generations. This strategy harnesses the pursuit of wide-ranging "lifelong ink" possibilities*1 from creative to business and education in people's lives to the Company's own sustainable growth as well. The Company also strongly put values on interactions of individual employees with society and promotes operations and product development that takes into account the environment. It intends to continue making proposals for the future image of society together with the community, such as Ars Electronica*2 rather than just as a single company.

*1 For example, in the education field, it is developing AI Ink for Education, which provides a learning environment tailored to individuals by clarifying the learning characteristics of individual students from line-of-sight data and pen movements made during learning.
*2 Ars Electronica, a global creative entity, has been continuously proposing "new creativity and future societal concepts facilitated by cutting-edge technologies" over 40 years from its location in Austria.

Also, the Company considers responding to climate change to be an important issue in environmental management and is working to reduce greenhouse gases, while it is also conducting business activities based on risks and opportunities in the business environment relating to climate change. In particular, it is progressing BCP to respond to the risk of a restriction to corporate activities due to floods and other natural disasters, which are increasing year by year. It also recognizes that developing environmentally friendly products is an opportunity and is working on strengthening the structure for this. In addition, as an action that will lead to a reduction in CO_2 emissions in the value chain as a whole, it requires that its suppliers support and implement the Wacom Supplier Code of Conduct.

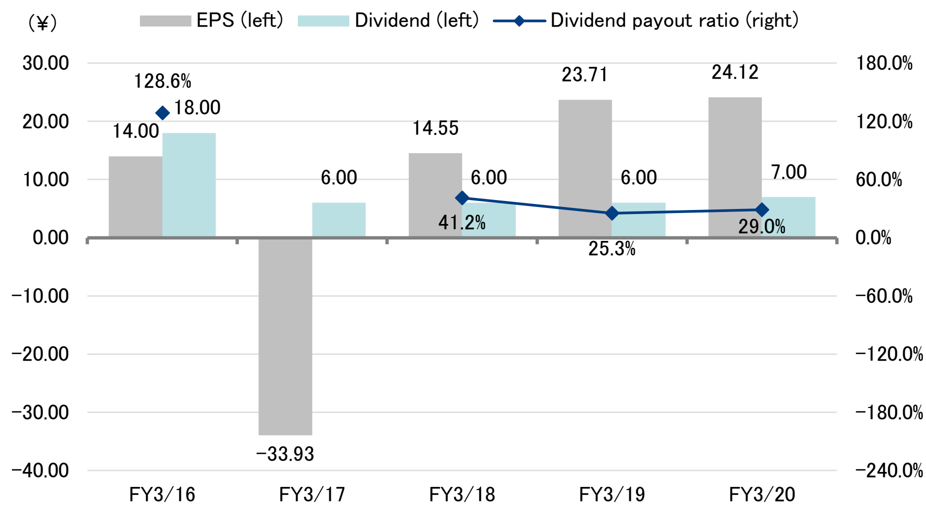
Returns to shareholders

Targeting a ¥0.5 hike to ¥7.5/share in FY3/21. Is highly likely to further increase the dividend, if it achieves the results forecasts

The Company's basic policy towards shareholder returns is to pay steady dividends on its profits after considering the amount of funds to be retained for future business development and a sound financial base. The Company had previously set a dividend payout ratio of around 40% as the standard for the dividend level, but from FY3/18, it lowered it to around 30%. This was in order to solidify the foundations for growth in the future and was necessary to increase its financial soundness, while in the background is the fact that it has set a target to aim for at the present time of around 60% for the equity ratio (it was 54.2 % at the end of FY3/20). Also, the Company only pays dividends once at the end of the fiscal period in consideration of keeping down administrative costs.

The Company is targeting a ¥0.5 hike to a ¥7.5/share dividend in FY3/21, and at the current time it has left the initial forecast unchanged. However, while closely observing the progress made in results, in the event that an environment is in place in which it can revise (increase) the dividend forecast, it has indicated that it will quickly disclose the revised amount. Therefore, it is considered highly likely that it will further increase the dividend if it achieves the (revised) results forecasts.

Trends in EPS, dividend, and dividend payout ratio



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

Company profile

Established in 1983, the Company has grown steadily with technology and now leads the global market of pen tablets for creators

The Company was established in 1983 in Ageo City, Saitama Prefecture. Its name derived from "world" and "computer," while "wa" includes the meaning of "harmony between people and computers" ("wa" being the Japanese word for harmony, a part of the new Reiwa era). In 1984, it announced the world's first cordless pen tablet. In 1987, it launched the SD Series of graphic pen tablets for professionals, which were used by the Walt Disney Company in the United States for film production. Subsequently, it constantly enhanced its products, and in the creative pen tablet market for creators, it has consistently kept a leading position on a global basis since the 2000s.

In 1991, it entered into the pen sensor components field (currently, the Technology Solution Business). The Company conducts OEM supply of digital pens, control ICs, touch pads, and other parts and modules to finished product manufacturers. It has been achieving rapid growth amid expansion of tablet, notebook PC, and smartphone markets.

In the securities market, after listing on the Japan Securities Dealers Association's JASDAQ market in April 2003, the Company became listed on the Tokyo Stock Exchange's First Section in December 2005, where it remains today.

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