COMPANY RESEARCH AND ANALYSIS REPORT

USEN-NEXT HOLDINGS Co., Ltd.

9418

Tokyo Stock Exchange Prime Market

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Summary

In FY8/22, both net sales and operating profit will set new record highs for the sixth consecutive period

USEN-NEXT HOLDINGS Co., Ltd. <9418> (hereafter, also "the Company") provides various equipment and solutions needed to operate stores and facilities and for DX, with music distribution as the main area, to commercial stores such as restaurants and retailers, and to facilities including hotels, hospitals, and offices. It also provides distribution services for individuals, such as for video and e-books. USEN Co., Ltd. and U-NEXT Co., Ltd. reintegrated in December 2017 and the Company was established as the holding company. The aim of the reintegration was to promote growth by circulating funds from the cash cow music distribution to the growth businesses, including the content distribution business, while another aim was to create synergies by cross-selling the mainstay products of the Group's companies by utilizing their strengths and sales channels. This strategic reintegration has been a success, and results in actual terms have set new record highs for the sixth consecutive period, with both net sales and operating profit setting new record highs in actual terms for the sixth consecutive period (for FY8/18, which was an eight-month fiscal period, net sales have been converted to a twelve-month fiscal period).

1. Strengths of the Group as a whole include a deep customer base and sales capabilities cultivated through music distribution and other services

The Company operates five businesses. The content distribution business distributes movies, e-books, and other digital content to individuals via the "U-NEXT" flat-rate distribution service. The store services business distributes music to commercial stores and retail facilities, manages music copyrights, and supplies all types of solution services related to store management, such as for store DX products and services. The communications business conducts sales and provides services for ICT for corporate customers and its own optical line service for commercial stores. The business systems business sells and maintains automated payment machines, front desk management systems, and other products and services to hotels and hospitals, among other users. The energy business sells electricity and gas as products supporting the store services business. Each respective business has its own strengths, while the strengths of the Group as a whole include its deep customer base and sales capabilities cultivated through music distribution.

2. Sales and profits increased in FY8/22 despite the transition in the with / after COVID-19 period and the weak yen

In the FY8/22 results, sales and profits increased by double digits, with net sales of ¥237,927mn (up 14.2% year-on-year (YoY)) and operating profit of ¥17,321mn (up 11.0%). Within the transition in the with / after COVID-19 period, economic activities recovered, but the business environment remains severe because, against the backdrop of the Ukraine situation and other factors, inflation is increasing due to the weak yen and the rising prices of raw materials. However, in the content distribution business, there was a recovery from the rebound of nesting (stay at home) demand and the number of paid subscribers increased, while store DX grew stably from capturing the strong needs due to inflation and the labor shortages. Therefore, although in the content distribution business operating profit did not reach the forecast because of the impact of the weak yen, in the businesses as a whole, sales and profits increased. In the consolidated results, net sales and every profit item achieved new record highs. The Company adopted "the Accounting Standard for Revenue Recognition, etc." from the start of FY8/22, but for the increase and decrease rates, the new accounting policy has not been retroactively applied.

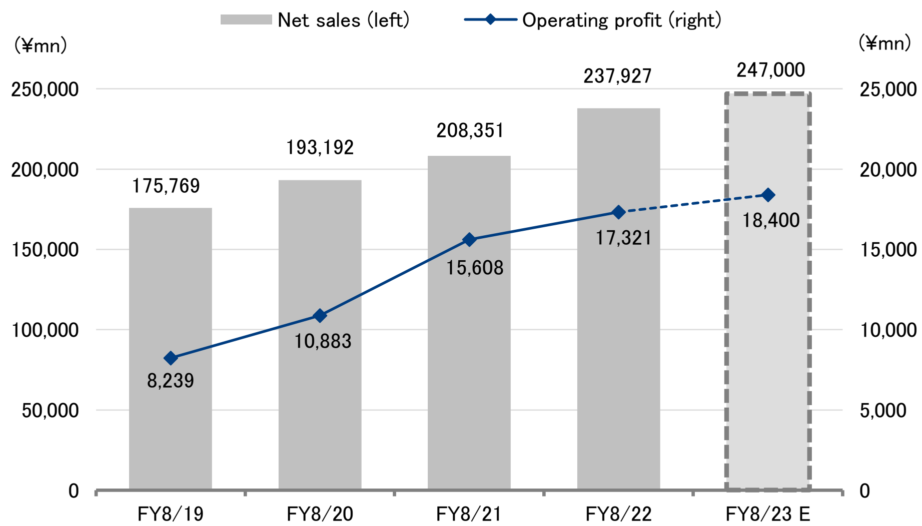
3. The weak yen is a risk, but inbound demand is expected and the FY8/23 forecasts are for higher sales and profits

For the FY8/23 results, the Company is forecasting net sales of ¥247,000mn (up 3.8% YoY) and operating profit of ¥18,400mn (up 6.2%). Going forward also, the Company's policy is to utilize to the greatest possible its strengths, such as its stable customer base, and to maximize Group synergies in order to respond to consumption behaviors and the social environment that are changing in the with / after COVID-19 period. Within this situation, on the one hand the Company will respond to the rapidly weakening yen, including by reviewing the procurement details of overseas content, while on the other hand it is considered that in relation to the lifting of restrictions on movement, it will capture domestic travel and inbound demand that are expected to increase, and that this will support results improvements at commercial stores, restaurants, hotels, and other establishments. For the medium-term management plan, there are risks in that the progress made by some businesses is slightly behind schedule, and also the weak yen, but overall, it seems that excellent progress is being made.

Key Points

- Against the backdrop of the strategic reintegration, in actual terms both net sales and operating profit set new record highs for the sixth consecutive period
- In FY8/22, sales and profits increased in all businesses despite the rebound from nesting demand, the weak yen, and rising raw material prices
- In FY8/23 as well, although the weak yen will continue to trend unstably, domestic travel and inbound demand are expected to grow

Results trends



Note: The Accounting Standard for Revenue Recognition, etc. has been applied from FY8/22.
Source: Prepared by FISCO from the Company's financial results

Company profile

A “social DX company” that makes the future closer

1. Company profile

Through the Group companies under its umbrella as the holding company, the Company provides devices, solutions and other products and services needed to operate stores and facilities and support for DX, centered on its founding business of music distribution, to restaurants, retailers and other commercial stores, and to various facilities including hotels, hospitals, and offices. It also provides a service that distributes movies, e-books, and other digital content to individuals under a flat-rate-fee system. The Company creates synergies through cross-sales of the Group companies’ mainstay products. This involves leveraging the respective strengths of each Group company, specifically a customer base consisting of close to 1mn commercial stores and other such enterprises, nearly 3mn paid subscribers of its video distribution services, expertise in supporting commercial stores, a network infrastructure, and sales capabilities such as a direct sales platform, telemarketing and a network of agencies. It is also progressing a dynamic growth strategy that actively incorporates next-generation technologies like IoT and AI. In this way, the Company is implementing its corporate slogan of “Brighten the future” as a “social DX company” that brings the future closer to the present by progressing store DX and lifestyle DX.

Has built a strong earnings foundation with high growth potential through strategic reintegration

2. History

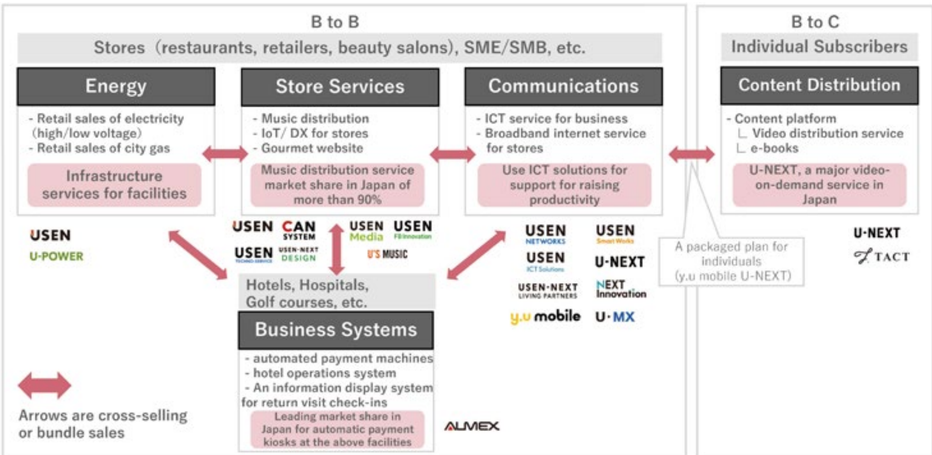
Mototada Uno founded USEN in 1961 as Osaka Yusen Broadcasting and subsequently built a wired broadcast network nationwide. When Yasuhide Uno took over as President in 1998, he promoted store assistance services and broadband services using the Company’s existing customer base and infrastructure, and pursued diversification and digitalization, including video distribution, and other content provision services. U’s Broad Communications (now, U-NEXT), a broadband service provider, took over the paid TV video distribution service and sales agent business for optical lines for individuals and other communication lines and spun off from USEN in December 2010. However, USEN and U-NEXT strategically reintegrated in December 2017 with the aim of leveraging respective customer bases and other management resources. The reintegration was an opportunity to concentrate shared Group functions while simultaneously expanding business through Group synergies. Currently, the Company is building a firm revenue base with high growth potential. In April 2022, the Company moved to the Prime Market, the new market segment of the Tokyo Stock Exchange.

Is developing content distribution for individuals stores and management support services for stores and facilities

3. Business overview

The five business segments are the content distribution business, the store services business, the communications business, the business systems business, and the energy business. The content distribution business involves the distribution of digital content, of movies and e-books, to individuals. The other four businesses mainly consist of providing management support services for SME's business establishments and various facilities, such as commercial stores operated by corporations and individual business owners. The store services business provides the cash cow music distribution services to commercial stores including restaurants and retail stores, and various other facilities. It also conducts sales and installations of peripheral sound equipment, manages music copyrights, and provides store management solution services, including for store DX products and services, which is a growth business. The communications business sells ICT products to corporations, which have stable growth, and its own optical line service and other products and services to commercial stores, which have high growth. The business systems business sells equipment, such as automated payment machines and front desk work management systems, to hotels, hospitals, and other customers, and also provides maintenance services. The energy business sells low-cost electricity and gas to the customers of the store services business and the communications business. The Company is not only pursuing synergies, such as through cross sales between these businesses, but it is also improving the earnings structure by shifting away from a model of one-time income at the time of a sale to a model of increasing stable and continuous recurring income obtained through monthly usage fees.

Segment overview



Source: The Company's results briefing materials

(1) Content distribution business

"U-NEXT" is a content distribution service for individuals of video, of movies and TV, and e-books and music, which for a monthly fee users can access via the Internet on many types of devices, including TVs, PCs, and smartphones. The video distribution market expanded rapidly due to the novel coronavirus pandemic (hereafter, COVID-19), but it has been noted that this growth is slowing down in the shift in with / after COVID-19 period. However, in Japan, the use of flat-rate-fee video distribution services has not progressed sufficiently compared to in the United States and other countries, so it seems that this market will grow in the medium to long term. In this way, Japan's video distribution market is growing and can be said to be a growth market, but on the other hand it can also be said to be a fiercely competitive market. The total market share of DAZN, Hulu, and other small and medium-sized operators is falling, but conversely, it can be said that share is becoming concentrated in the services of the big four companies of "U-NEXT," Netflix, Amazon Prime, and Disney Plus.

The overwhelming strength of the three major foreign companies is the contents they produce based on the enormous amounts that they spend on them. To compete with them, "U-NEXT" has a comprehensive lineup of content from Japan and overseas. In its "coverage strategy," it provides an all-you-can-watch service for a library of more than 240,000 titles, including movies, dramas, and anime. Users can also watch more than 30,000 rental titles, including the latest titles that have only just been released and broadcast, and the number of titles in its lineup is said to be industry leading. Moreover, its lineup covers niche fields, live music, live martial arts, and other areas, while it is also quick to distribute new titles. In addition, as it packages together more than 760,000 e-books, including manga and books, and music-distribution songs, with just one contract users can use multiple content services to "listen," "watch" and "read." The monthly usage fee for the Company services seems high at ¥2,189 (tax included), but every month users receive points worth ¥1,200 (points can be used to acquire coupons for live theater performances), so it is actually only ¥989 (tax included). Also, a single account can be viewed by up to four people, and when considering together all these benefits, its cost performance can be said to be high.

The Company also differentiates its services from others in terms of the contents it provides. Through its "ONLY ON strategy" of "only watchable on U-NEXT" and "enjoy all-you-can watch only on U-NEXT," it is working to strengthen exclusive distribution of new titles, topical titles, sports content and live music content. For this, it has entered into contracts for exclusive distribution rights with overseas content holders to enable it to compete against Netflix and Amazon Prime, while it is also progressing the development of live music distribution that utilizes the deep relationships it has built in the music distribution area. Moreover, it is the only major service provider to distribute adult content, and the fact that adult content is a major differentiation factor can be understood from the overwhelming victory of TSUTAYA Co., Ltd., over US-based major Blockbuster LLC during the growth years of video rental. In these ways, the Company is progressing strategies that clearly differentiate its service from those of the three major foreign companies, and it seems that many users choose "U-NEXT" when they use multiple video distribution services.

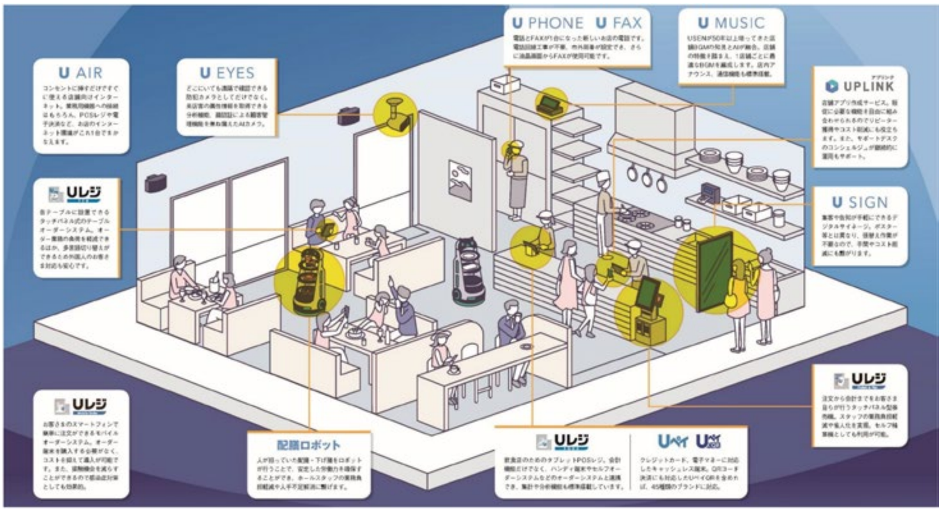
(2) Store services business

The store services business provides "USEN MUSIC," which is the cash cow music distribution service and the Company's founding business with a history of more than 60 years, and also a service to support store DX. It targets the approximately 3mn commercial stores and facilities nationwide, including restaurants, retail stores, beauty salons, medical facilities and offices, ranging widely from individually-run stores to community-based or nationwide chains. Of these, the Company provides a music distribution service to 700,000 stores and facilities throughout the country, (its estimated share of the music distribution market for stores is approximately 90%), broadcasting music and various information for stores and facilities ranging from specialty channels, such as for J-POP and Western music, through to request channels. In this service, it has a library of around 10mn songs and can use AI to create playlists suited to any type of industry or business format. It also provides as standard 1,000 types of in-store announcements for customers, employees, and others.

Store DX has been conducting a business peripheral to the music distribution service. In recent years, needs for digital support aimed at personnel saving and labor saving have been rapidly increasing. It is a big challenge for SMEs to progress technology such as IoT and DX on their own, so the Company provides them with installation support as a one-stop service. Centered on the “USEN MUSIC” music distribution service, this is a store management service that integrates various products and services, including “USEN Regi,” which is a POS cash register, “USEN AIR,” which is business-use Wi-Fi, “USEN Camera,” which is an AI camera that can analyze the attributes of customers visiting stores, and catering service robots. This store infrastructure is called the “USEN IoT PLATFORM” that provides all the DX products and services required by new businesses. Against the backdrop of the enhancements to this service, the Company has developed “USEN Marutto Store DX,” which creates a package of store DX products and services, and it is progressing operations for new customers, including for new stores that have a high set contract completion rate. When adding music distribution, this business has a customer base on a scale of close to 1mn customers and can be said to be the Company’s greatest management resource.

The strengths of this business are this customer base and also a strong support network consisting of 140 Group bases nationwide, as well as a workforce of 1,200 direct sales and 900 installation and maintenance professionals. The approach for both music distribution and store DX is to provide support from a store opening through to its management, from installing equipment through to aftercare and also dealing with troublesome copyrights. The music distribution market is stable and the situation is that store closures (contract cancellations) are cancelled out by new stores (new contracts), so this business is a highly profitable cash cow. Therefore, it is a business that financially supports the growth strategy of the Group as a whole. On the other hand, for store DX, alongside the decline in the working population, needs for personnel saving and labor saving are rapidly increasing, and in particular among the Company’s existing customers, many individually-run stores and small- and medium-sized stores have not progressed digitalization, so there remains plenty of room for store DX installations and it can be said to be an extremely high growth business.

“USEN IoT PLATFORM”



Source: The Company’s homepage

(3) Communications business

The communications business conducts sales agency operations for broadband internet lines, proposes and sells the building of office ICT (Information and Communication Technology) environments, provides the "y.u mobile" MVNO service, and provides and sells broadband internet lines for individuals. For the building of ICT environments, it provides corporations with ICT products and solution services linked to SaaS, such as cloud services, mobile services and data center services from Google, Cybozu <4776>, and others. The strengths of the Company's corporate business, which has continued to stably grow despite the rapid changes in the ICT industry, include the wide breadth of its service lineup through a multi-vendor strategy and offering highly convenient direct sales through which it can respond to each customer's needs via a single customer desk.

Also, for broadband internet lines, the Company is progressing the switch of existing contracts from agencies to its own highly profitable optical line service, while also strengthening sales of up-sales products to commercial stores and of work environment improvement products combined with music distribution to offices. There are risks, such as competition intensifying, but within the transition in the with / after COVID-19 period, offices and commercial stores' needs are strengthening for digitalization, improved work efficiency, and security measures, so its momentum is increasing as a high-growth service. The strengths of this business include the synergies with the store services business and that sales promotions are conducted through a network of 250 agencies. Another strength is its network in the real estate industry, and it provides a one-stop communication line service for residents of major rental residential properties.

(4) Business systems business

The subsidiary ALMEX INC. is responsible for the business systems business. It sells equipment to meet customer needs for personnel saving and labor saving, such as automated payment machines and front desk work management systems, including to general hotels, leisure hotels, general hospitals and clinics, golf courses, as well as order terminals, operating systems, and other products to restaurants. It also provides other services that generate recurring revenue, including maintenance and software upgrade services. In terms of its track record of deliveries to all types of facilities within Japan, its market shares are high for all facilities except for clinics. Among them, according to the Company it has the top shares in each market for automated payment machines. The strengths of this business include that, as a fabless manufacturer, it itself conducts each stage from the development of equipment and systems through to sales and maintenance.

In terms of the market environment, the medical industry has started to improve convenience for patients, and during the with / after COVID-19 period, in the hotel industry, domestic travel is expected to recover due to the measures to support travel, while inbound demand is also expected to recover thanks to the easing of restrictions on entering the country, and the desire to invest in personnel saving and labor saving through DX is increasing even more. In adjacent markets as well such as golf courses, retailers, and pet clinics, demand is considered to be large from their affinity with the Company's devices and they are expected to achieve comparatively high growth in the medium to long term. In the short term, in addition to government subsidies, in April 2023 the Ministry of Health, Labour and Welfare will implement a policy that in principle will make it obligatory to introduce online qualification, so it seems that introductions of insurance certification systems and devices that use the My Number card are accelerating from general hospitals and also medium- and small-sized clinics. Within this situation, the "Sma-pa Myna Touch," which is a card reader with face authentication that is compatible with the Company's online qualification, is proving popular as it has proprietary functions that enable the reading of various card-based certifications like health insurance cards and medical certificates, in addition to contactless forms, and it has become an effective tool for opening-up markets, such for small- and medium-sized clinics.

(5) The energy business

The energy business, which was launched following the liberalization of energy sales in 2016, involves selling high-voltage and low-voltage electricity and city gas procured on a relative basis from Tokyo Electric Power Company Holdings, Inc. <9501> (hereinafter, TEPCO), with which the Company has a business alliance, to the Company's customers and others in areas other than TEPCO's areas through "USEN Energy." In addition, it sells products including LED, business-use air conditioners, and "USEN GAS," and it provides consulting and services, such as for energy saving. It is also focusing on them as products that will spur new customer acquisition in the store services business and cross-selling.

In contrast to "USEN Energy," which uses an agency model, in March 2022 the Company started the fully fledged provision of "U-POWER," which uses an own energy procurement model. Based on the increases in companies' and stores' awareness of compliance with SDGs and of environmental conservation, it is providing a menu that includes "Green Electricity with Non-fossil Fuel Energy Certificates." The reasons it has been able to fully launch this service are that its features include that, because it uses an own energy procurement model, it can transfer prices onto customers when power wholesale prices are rising so the risk of gross profit declining is low, and that it is highly profitable compared to the agency model. Currently, the Company is actively developing this business, including working to retain existing customers of "USEN Energy" whose intention to cancel their contract has strengthened alongside the intensification of competition with new power companies and existing regional power companies, and providing market-linked "high voltage green power" in collaboration with the power company switching service of ENECHANGE<4169>.

Financial results trends

Results were excellent in FY8/22, with sales and profits increasing and exceeding the initial forecasts

1. FY8/22 results

In the FY8/22 results, net sales were ¥237,927mn (up 14.2% YoY), operating profit was ¥17,321mn (up 11.0%), ordinary profit was ¥16,241mn (up 10.0%), and profit attributable to owners of parent was ¥8,687mn (up 8.0%), so every sale and profit item increased by double digits except for profit attributable to owners of parent. Each item also exceeded their initial forecast, net sales by ¥17,927mn, operating profit by ¥321mn, ordinary profit by ¥241mn, and profit attributable to owners of parent by ¥187mn. Therefore, based on the actual values when the FY8/18 eight-month fiscal period is converted into a twelve-month period, the results set new record highs for the sixth consecutive period. The Company adopted "the Accounting Standard for Revenue Recognition" etc., from the start of FY8/22, and as a result, there were decreases of net sales of ¥2,096mn, cost of sales of ¥1,519mn, SG&A expenses of ¥17mn, and operating profit, ordinary profit, and profit before income taxes of ¥559mn for each. The increase and decrease rates were calculated based on the consolidated results in the previous period before its adoption, and the new accounting policy has not been retroactively applied.

FY8/22 results

(¥mn)

	FY8/21		FY8/22		YoY
	Results	% of net sales	Results	% of net sales	
Net sales	208,351	100.0%	237,927	100.0%	14.2%
Gross profit	81,579	39.2%	84,500	35.5%	3.6%
SG&A expenses	65,971	31.7%	67,178	28.2%	1.8%
Operating profit	15,608	7.5%	17,321	7.3%	11.0%
Ordinary profit	14,768	7.1%	16,241	6.8%	10.0%
Profit attributable to owners of parent	8,044	3.9%	8,687	3.7%	8.0%

Note: The Accounting Standard for Revenue Recognition, etc., was adopted at the start of FY8/22, and the YoY values were calculated based on the consolidated results in the same period in the previous fiscal year before it was adopted.
Source: Prepared by FISCO from the Company's financial results

Even during COVID-19, in the second half of FY8/22 there were no restrictions on behavior, such as a declaration of a state of emergency, and the Japanese economic environment has normalized during the with / after COVID-19 period. However, due to the impact of the global spike in the prices of raw materials and also the rapidly weakening yen, inflationary pressures are further strengthening. Therefore, the situation is that many companies and commercial stores are having to revise the prices of their products and services, and there are concerns that customers will lose their motivation to purchase and will stop using products and services. Moreover, for subscription services, which have rapidly grown due to COVID-19, the sense of uncertainty about the business environment surrounding commercial stores and the Company has increased, such as consumers selecting only some services due to having "subscription fatigue." Under these sorts of conditions, in accordance with the medium-term management plan "Road to 2025," the Company has been providing integrated, one-stop products and services that eliminate the various problems facing customers.

As a result, sales and profits increased in the Company's business as a whole, and in the consolidated results, net sales and every profit item achieved new record highs. Compared to the initial forecasts, in the content distribution business, in which member numbers steadily grew even after nesting demand, operating profit was less than forecast because payments denominated in foreign currencies for overseas content increased due to the weak yen and also because of the active investment in sales promotions. In the business systems business as well, net sales were less than forecast, mainly because of weak initial device sales for medical institutions, centered on "Myna Touch." But in all other businesses, net sales and operating profit were higher than forecast, while the consolidated results were also higher than forecast. In FY8/22 Q4, operating profit declined by around ¥900mn compared to Q3, but the factors in the background to this were the increase in procurement costs in the content business due to the weak yen, the strengthening of sale promotions, the increase in depreciation costs for grouped depreciating assets in the store services business, and a decrease as rebound to the busy period for commercial store agencies in the communications business, and rather it can be said that these corporate activities include the Company's spare capacity. The extraordinary profit that was recorded in FY8/21 was not recorded in this period, and therefore the YoY growth of profit attributable to owners of parent was low.

Sales and profits increased in every segment

2. FY8/22 results by segment

In the FY8/22 results by segment, in the content distribution business, net sales were ¥71,432mn (up 19.1% YoY) and operating profit was ¥6,294mn (up 9.8%); in the store services business, net sales were ¥58,172mn (up 3.7%) and operating profit was ¥9,048mn (up 5.3%); in the communications business, net sales were ¥50,764mn (up 5.4%) and operating profit was ¥5,367mn (up 18.4%); in the business systems business, net sales were ¥19,151mn (up 1.2%), and operating profit was ¥3,277mn (up 13.1%); and in the energy business, net sales were ¥41,626mn (up 49.1%) and operating profit was ¥512mn (up 44.7%), so sales and profits increased in every segment. It is considered that in the background to this performance was that, even during COVID-19, the Company continued to actively invest, mainly in the content distribution business and the store services business, and that it achieved synergies and business portfolio effects through Group management.

FY8/22 results by segment (before adjustment)

(¥mn)

Net sales before adjustment	FY8/21		FY8/22		YoY
	Results	% of net sales	Results	% of net sales	
Content distribution business	59,956	28.4%	71,432	29.6%	19.1%
Store services business	56,112	26.6%	58,172	24.1%	3.7%
Communications business	48,179	22.8%	50,764	21.1%	5.4%
Business systems business	18,925	9.0%	19,151	7.9%	1.2%
Energy business	27,926	13.2%	41,626	17.3%	49.1%

Operating profit before adjustment	FY8/21		FY8/22		YoY
	Results	Profit ratio	Results	Profit ratio	
Content distribution business	5,731	9.6%	6,294	8.8%	9.8%
Store services business	8,590	15.3%	9,048	15.6%	5.3%
Communications business	4,534	9.4%	5,367	10.6%	18.4%
Business systems business	2,898	15.3%	3,277	17.1%	13.1%
Energy business	354	1.3%	512	1.2%	44.7%

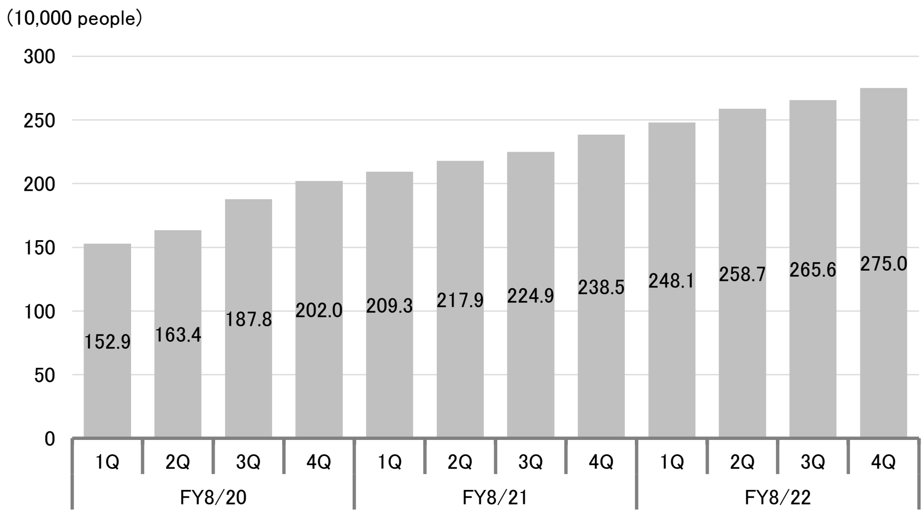
Note: The Accounting Standard for Revenue Recognition, etc., was adopted from the start of FY8/22, and the increase and decrease rates were calculated based on the consolidated results in the same period in the previous fiscal year before the adoption.
Source: Prepared by FISCO from the Company's financial results

(1) Content distribution business

Amid the shift in the with / after COVID-19 period, the content distribution market environment can be broadly divided into three phases. Initially, in the context of the COVID-19 nesting demand, there occurred sorting and selection of the video distribution service providers that had become haphazard, but the Company's "coverage strategy" was highly evaluated and it established a position of being the leader among the domestic players. Soon after, the attacks strengthened of services provided by global companies like Netflix and Amazon Prime, but while those companies stand out because of their private brands, the Company's strengths include its rich lineup of anime and older titles and the speed that it launches new titles, so there occurred a state of co-existence and co-prosperity with these global companies with which it had complementary relationships. Then in the with / after COVID-19 period, the growth of the content distribution market has slowed down, including due to the rebound of nesting demand and reviews of subscription services, and both global companies and other domestic companies have entered a phase of reviewing their strategies toward downsizing. In particular, the global companies have been forced to change their various strategies, including on their private brands, prices, and focus areas. In this rapidly changing environment, the Company, whose strengths include its rich lineup, has conversely been strengthening its sales promotions and has been able to increase its share.

In other words, on the one hand the Company's reputation as a contents service provider is improving, including by progressing its "coverage strategy" and "ONLY ON strategy," while on the other hand, contrary to the developments in the industry, the various customer-attraction measures it is implementing are proving successful. Specifically, aiming for co-existence and co-prosperity with movie theaters, which should be its rival, through mutually sending customers to each other, it has increased the movie theaters where purchases can be made with "U-NEXT Points" and has started a collaborative campaign with TOHO Cinemas. Also, by having television manufacturers install the "U-NEXT Button" on the remotes of newly sold TVs, it is also progressing efforts to strengthen customer attraction for "U-NEXT." Aiming to improve the quality of the stable distribution environment, it has adopted "Media CDN," which is the newly launched CDN (content / delivery / network) service provided by Google of the United States. In the background to this strategy is the recovery of nesting demand from its rebound, and the number of "U-NEXT" paid subscribers is showing high growth and it set to rise by more than 360,000 on the end of the previous period to 2.75mn at the end of FY8/23, which will lead to the strong sales performance. The main reasons why profit growth is not as strong as sales growth are the increase in procurement costs for overseas content due to the rapid weakening of the yen and the active spending on advertising and promotions costs. Both factors will lead to sales in the future, but for procurement prices, the intention is to cover the increase from the bargaining power from having close to 3mn paid subscribers and improvements to the content mix.

Trends in paid subscribers in the content distribution business



Note: included monthly points services, etc., through business alliance partners
Source: Prepared by FISCO from the Company's results briefing materials

(2) Store services business

Economic activities are recovering in with / after COVID-19 period, and in this situation, the business environments of commercial stores and restaurants that are the Company's customers are improving, including that congestion can be seen in some transportation facilities and at some tourist destinations due to the increased movements of people. Also, there is policy-related support toward the fully fledged recovery of inbound demand, including the easing of restrictions on entering the country, and inbound demand has started to recover and customers' mindsets are also improving. However, due to the price hike rush of raw materials, fuel, and daily necessities, the situation is that customers are being forced to review their product prices, and there are concerns about their customers' motivation to purchase declining and that they will stop using products and services. Conversely, the labor shortages are becoming even more severe and it seems that in some stores there is occurring discord in terms of management itself.

The Company's role is to eliminate these concerns and problems, and it has strengthened its support through cross-sales products*, such as store DX products and services, centered on the mainstay POS cash registers. As a result, at the end of FY8/22, the number of contracting stores was 957,000 (up 4.9% on the end of the previous period) and was drawing close to the 1mn level, while for cross-sales products as well, the number of contracts has more than doubled in three years. In this situation, as measures for the labor shortage, the Company has been able to provide in a timely manner digital signage and catering service robots that use digital technologies and for which needs have quickly strengthened. With regards to home delivery established as a new sales channel during COVID-19, in September 2022 Virtual Restaurant Co., Ltd. was made a Group company, and it started providing registration agency services and consulting, such as Uber Eats and Demaecan, for customer restaurants, and it also started providing products with short processing times. As a result of these efforts, net sales grew steadily for both initial earnings and recurring earnings, and operating profit grew more than net sales because the impact of recording grouped depreciating assets was absorbed.

* Cross-sales products: devices and services other than music distribution for stores.

Store services business -Number of contracts

Note: Other services to stores: The total of communication lines, POS cash register services, Wi-Fi services, IP camera services, app creation services, and gourmet food website services. In the event of one customer having contracts for multiple services, each service counts as one.
Source: The Company's results briefing materials

(3) Communications business

In the with / after COVID-19 period, remote working and online conferences have become firmly established, and due to the labor shortages and other factors, needs have strengthened to introduce tools to improve work efficiency and for labor saving. But as conditions are different in each company, such as the ratio of office workers to remote workers, the Company has worked on providing work environment improvement proposals tailored to each company. It has also provided services, including various cloud services (SaaS services) that support employees' workstyles, and BGM services, such as "Sound Design for OFFICE" so that employees can work comfortably at the office. In addition, it has started handling "Virtual Private Gate," a new product and service that can speed up the transition to on the Cloud, etc., and introductions of network functions, and "USEN Hikari 01," an optical line service for individuals that is compatible with remote working. As a result, the number of newly acquired communication line, network, and security services customers continued to grow steadily, particularly among small- and medium-sized businesses, thus securing an increase in sales. In profits, in addition to the higher sales, it has made progress in shifting from one-shot fees to recurring earnings alongside the increase in the Company's own optical lines for commercial stores, and the extent of the rise in profit increased YoY. The reasons why profit declined in 4Q included an increase in ICT costs for corporations due to the weak yen, a decline as a rebound from the busy period for line agencies, and the increase in agency fees.

(4) Business systems business

Against the backdrop of the lifting of restrictions on movement and the easing of restrictions on inbound visitors entering the country, movements of people increased in tourist sites and downtown areas, and positive signs could be seen for industries such as travel, tourism and entertainment. Conversely, to respond to the labor shortages, needs for DX for labor saving and other purposes are rising. In response to this situation, the Company has started introductions of "Cyphy-inn," which is a face authentication check service for hotels. Also, for entertainment facilities where it has become difficult for staff to provide "hospitality," it is proposing devices for personnel saving and labor saving, such as automated payment machines. In particular, for self-check-in at golf courses, the Company has progressed system coordination with the "Rakuten Check-in Service" provided by the "Rakuten GORA" golf course reservation service. Elsewhere, for the issues facing hospitals and clinics such as labor shortages, workstyle reforms, and contactless reception desks, it has started to provide "APS-NEXT," which is a new automated re-visit reception machine. In April 2023, the Ministry of Health, Labour and Welfare will implement a policy that in principle will make it obligatory to introduce online qualification. Toward this deadline, the Company is actively selling "Sma-pa Myna Touch," a card reader with a proprietary face authentication function not provided by other companies, which will enable confirmation of online qualifications using either a My Number card or a health insurance card. In 4Q, sales and profits declined as a rebound to the batch delivery of "Sma-pa Myna Touch" in the previous period, but for the full fiscal year, sales and profits increased because in addition to the recoveries of the tourism and entertainment industries, initial sales, particularly of automated payment machines for leisure hotels, performed well.

(5) Energy business

The Company sells high and low voltage electricity and gas in order to create high added value for store services. But the situation is that in the negotiations affected by the recent rises in fuel prices, to a certain extent there have occurred "USEN Energy (high voltage)" contract cancellations in the agency model. However, the Company has developed a sales policy to switch to "U-POWER," its own energy procurement model, for customers intending to cancel their contracts, and in addition, it is compensating for these cancellations by increasing sales prices and accumulating low voltage contracts from which many other companies are withdrawing, and therefore it secured increases in sales and profits. In "U-POWER," which is a service to support stores' SDGs that was launched in March 2022 with three plans with different green energy ratios, the Company has been proposing a high-voltage green menu to the many companies that have stopped accepting high voltage in the context of the soaring fuel prices.

Procured corporate bonds of ¥10bn and expanded fund raising methods

3. Financial strategy

The strategic reintegration of USEN and U-NEXT in December 2017 had the major advantage of building a high-growth, strong earnings foundation by simultaneously realizing improved efficiency and an expanded business scope through Group synergies. However, initially after the reintegration, it had the disadvantage of worsening the financial condition, such as raising the debt ratio. But the debt has contracted alongside the profit growth, and the equity ratio has improved from a single digit at the time of the reintegration to 26.3% at the end of FY8/22, and this disadvantage, of worsening the financial condition, is being eliminated. Therefore, the Company has become able to raise its financial strategy to a higher stage, of shifting from only focusing on debt reduction to focusing on funding as well.

In September 2022, the Company raised funds of ¥10bn from the market through domestic, unsecured straight corporate bonds. From its funds, it plans to allocate more than ¥40bn to business investment and other purposes, scheduled for the 4th period of the medium-term management plan. In particular, for semiconductors, for which there is a global shortage, it is considered it will procure them in advance for the required parts for DX products in the store services business. It seems that it will also be able to fully invest in content and sales promotions that were planned from previously. Other than these uses, it plans growth investment of more than ¥16bn in the 4th period of the medium-term management plan. The main investment scope is expected to be large-scale M&A and also content, IP (Intellectual Property), and original anime titles that are adjacent to its current business. By securing the funds through the current fund raising, it can be said that the feasibility of realizing profit growth in the medium term from FY8/23 onwards has increased. The Company is expected to grow, so it seems that it has been able to attract plenty of buyers for its corporate bonds in the markets.

The forecasts, although conservative, are to once again achieve peak profits

4. FY8/23 outlook

For the FY8/23 results outlook, the Company is forecasting net sales of ¥247,000mn (up 3.8% YoY), operating profit of ¥18,400mn (up 6.2%), ordinary profit of ¥17,300mn (up 6.5%), and profit attributable to owners of parent of ¥9,200mn (up 5.9%). Going forward also, it will utilize to the greatest possible extent its management resources, including its stable customer base, video content, music content, various IoT products, and network infrastructure. Its policy is to maintain its strong direct sales platform and to maximize Group synergies by utilizing its sales channels, including telemarketing, online marketing, and its agency network, and during the with / after COVID-19 period, to respond to the rapidly and greatly changing consumption behaviors and corporate activities, technologies, and societal environment. Through this, it will achieve sustainable profit growth and increase shareholder value and enterprise value.

In FY8/23, which is the second period in the medium-term management plan “Road to 2025,” major changes are expected, of the rapid weakening of the yen and the lifting of restrictions on movement. In relation to the weak yen, there are concerns about the rise in prices of procuring overseas content, but alongside the increase in stock revenue, the stability of profits is also increasing. Therefore, the Company’s policy is to cover for this by improving the ratio of domestic content to overseas content, negotiating conditions, and other measures. In relation to the lifting of restrictions on movement, both domestic and inbound movements are forecast to rapidly increase, which is expected to raise-up the results of commercial stores, restaurants, hotels, and other establishments. When considering this situation, the Company’s FY8/23 forecasts appear slightly conservative.

FY8/23 outlook

(¥mn)

	FY8/22		FY8/23		YoY
	Results	% of net sales	Forecast	% of net sales	
Net sales	237,927	100.0%	247,000	100.0%	3.8%
Operating profit	17,321	7.3%	18,400	7.4%	6.2%
Ordinary profit	16,241	6.8%	17,300	7.0%	6.5%
Profit attributable to owners of parent	8,687	3.7%	9,200	3.7%	5.9%

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

For the FY8/23 results outlook by segment, in the content distribution business, it is forecasting net sales of ¥74,000mn (up 3.6% YoY) and operating profit of ¥7,300mn (up 16.0%); in the store services business, net sales of ¥61,000mn (up 4.9%) and operating profit of ¥8,700mn (down 3.8%); in the communications business, net sales of ¥53,000mn (up 4.4%) and operating profit of ¥5,700mn (up 6.2%); in the business systems business, net sales of ¥21,000mn (up 9.7%) and operating profit of ¥3,400mn (up 3.8%); and in the energy business, net sales of ¥42,000mn (up 0.9%) and operating profit of ¥700mn (up 36.7%).

Segment outlook for FY8/23 (before adjustment)

(¥mn)

Net sales before adjustment	FY8/22		FY8/23		YoY
	Results	% of net sales	Forecast	% of net sales	
Content distribution business	71,432	29.6%	74,000	29.5%	3.6%
Store services business	58,172	24.1%	61,000	24.3%	4.9%
Communications business	50,764	21.1%	53,000	21.1%	4.4%
Business systems business	19,151	7.9%	21,000	8.4%	9.7%
Energy business	41,626	17.3%	42,000	16.7%	0.9%

Operating profit before adjustment	FY8/22		FY8/23		YoY
	Results	Profit ratio	Forecast	Profit ratio	
Content distribution business	6,294	8.8%	7,300	9.9%	16.0%
Store services business	9,048	15.6%	8,700	14.3%	-3.8%
Communications business	5,367	10.6%	5,700	10.8%	6.2%
Business systems business	3,277	17.1%	3,400	16.2%	3.8%
Energy business	512	1.2%	700	1.7%	36.7%

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

In the content distribution business, although in the industry there is a sense that a temporary lull will occur after the nesting demand, the Company is forecasting that the excellent results will continue, with sales to increase and profits to rise by double digits. When considering that following the reopening, the wallet share and time share of video distribution will be shifted to other products and services, the forecasts are for the net increase in the number of paid subscribers to be around 200,000 in one year and for net sales growth in the low single digits in the first half of the year. In profits, it seems the cost of procuring overseas content will increase due to the weak yen, but the Company is expanding its domestic procurement and reviewing transaction conditions, and it expects the operating profit margin to improve, including by reducing costs to acquire users. It can be said that the hurdle to achieve the forecasts has become a little higher as currently the yen is weakening at a rapid rate, but conversely, the net increase in the number of paid subscribers was 360,000 in the previous fiscal year, which seems fairly conservative. There are some concerns about NETFLIX's introduction of a low-cost tier with ads, and the impact that it may have on the Company, but at FISCO, we think that it will be difficult to obtain user consensus for paid-for content distribution in which distribution without ads is standard.

In the store services business, the music distribution is maintaining its customer base, so it is assumed that the number of contracts will be unchanged YoY. With customer needs for labor saving in the background, the forecast is for the number of contracts for POS cash registers, catering service robots, and store DX products such as digital signage to steadily increase. Conversely, profits are expected to decline including due to the increase in depreciation costs for DX devices, the increase in personnel costs following the strengthening of the service structure, and the decline in the number of contracts for music distribution for individuals. In the communications business, the Company is aiming to increase sales and profits, mainly by shifting from stock-type revenue to recurring-type revenue. In ICT for corporations, the forecasts are for the sales-increase trend to be maintained, but for operating profit to be unchanged YoY because of the increase in costs due to the weakening of the yen and the strengthening of personnel. For the Company's own optical cables for commercial stores, the forecasts are for sales and profits to increase from the steady rise in the number of contracts, but for sales and profits to increase only slightly for agency lines. In services for individuals, sales are expected to continue to trend downward, but operating profit is forecast to be unchanged YoY from MVNO becoming profitable.

In the business systems business, the forecasts are for sales and profits to increase from the expected recoveries of business conditions for travel, accommodation, and entertainment that will spread during the with / after COVID-19 period. Among them, actual demand for business hotels is expected to increase from the travel support measures, but it is anticipated that there will be a decrease as a rebound to the special demand created by the Japan Tourism Agency's subsidies in FY8/22. For hospitals and clinics, sales and profits are forecast to increase, including from the growth in sales of the new-type re-visit reception machines and strengthened cross sales for clinics. In particular, the number of applications in the market as a whole for “Sma-pa Myna Touch” is rapidly increasing in conjunction with it becoming obligatory to introduce the My Number insurance system in April 2023. Already 14,000 units have been sold, but due to the limited number of units produced by other companies with the same business, ALMEX is expected to newly received additional orders for around 15,000 units in FY8/23. However, it is assumed that it will not contribute to profits, including due to the sharp rises in purchasing prices, but at FISCO we think this is conservative assumption. In the energy business, even in the context of the many uncertain elements such as the rise in the prices of raw materials, the forecasts are for sales to increase slightly and profits to increase significantly through the Group actively implementing measures. Sales of “USEN Energy” are decreasing alongside the decline in the number of customers due to them stopping accepting new high voltage contracts, but operating profit is still expected to increase slightly because of the improved profitability from price increases and the decline in sales agency fees following the reduction in proposals. “U-POWER” will surpass the profit-loss breakeven point by steadily increasing the number of contracts, and profitability is forecast to improve significantly, including because of the popularity of green energy.

Medium-term management plan

Targeting consolidated operating profit of ¥22bn to ¥25bn in FY8/25

1. The medium-term management plan, "Road to 2025"

The Company is aiming to progress store and facility DX and lifestyle DX by utilizing the management resources it has cultivated in music distribution, such as its customer base, and by further increasing the sophistication of its value creation process. Conversely, it is aiming to increase enterprise value by strengthening the profitability and growth potential of the existing businesses, achieving non-continuous growth by utilizing M&A and other methods, progressing a flexible financial strategy that maintains discipline and achieving stable and continuous shareholder returns. The Company's purpose is to evolve to become a "social DX company" that makes the future closer, and toward achieving this, in February 2022 it formulated the medium-term management plan "Road to 2025."

In the medium-term management plan "Road to 2025," in consideration of the changes in the external environment due to incidents such as COVID-19 and the Ukraine situation, the targets are divided into two scenarios, which are a base case of lower-limit targets and an upside case of achievement targets. In both scenarios, the Company is aiming for operating profit to grow by double digits (four-year compound annual growth rate (CAGR), 9.0% to 12.5%) and plans to achieve consolidated operating profit of ¥22bn to ¥25bn in FY8/25. In the case of the Company, the market characteristics and growth potential are different for each segment, so a key point is that it has a strategy for each segment, but basically, they are upgraded strategies from the previous versions.

Numerical targets in the medium-term management plan

(¥bn)

	FY8/21 Results	FY8/25 targets (base case)		FY8/25 targets (upside case)	
		Target	Four-year growth rate	Target	Four-year growth rate
Net sales	208.4	274.0	31.5%	286.0	37.2%
Operating profit	15.6	22.0	41.0%	25.0	60.3%
Operating profit margin	7.5%	8.5%	0.5%	8.7%	1.2%
Profit attributable to owners of parent	8.0	12.0	50.0%	13.5	68.8%
EBITDA	24.4	33.0	35.2%	36.0	47.5%
EBITDA-CAPEX (includes investing and financing, and prepaid contents)	13.8	16.5	19.6%	19.5	41.3%

Source: Prepared by FISCO from the Company's medium-term management plan materials

For operating cash flow, the Company has raised the target from ¥15.7bn at the time the plan was formulated to ¥21bn to ¥24bn in the plan's final fiscal year, which is to be achieved through steady profit growth and a precise financial strategy. As the fourth period total, it will create operating cash flow of more than ¥80bn, while it plans to invest more than ¥40bn of this in business investment, more than ¥15bn in repaying borrowing, and more than ¥4bn in paying dividends, and it intends to use the remaining amount of more than ¥16bn for growth investment (excluding buffers). The anticipated uses are considered to be for large-scale M&A and for uses appropriate as a "social DX company" in new business development. The development targets are thought to be store, facility, and lifestyle DX, the backup of Japan's productivity improvements, and in related businesses, such as digitalization in the entertainment field, while its policy for M&A is to limit proposals to those peripheral to its existing businesses and not to handle different industries or fields.

As its financial targets, the Company will continue efficient management that utilizes leverage and is targeting improving the equity ratio to 30% to 40% while maintaining ROE at about 20%. In addition, it will continue to reduce the leverage ratio and the D/E ratio and secure sufficient funding capacity at all times. Through this, it should be able to respond flexibly for even greater growth investment. The Company prioritizes sustainability as a "social DX company" and intends to progress measures to resolve environmental issues and social issues. Among them, it has set four themes as those it will work on as the priority issues: "Contribute to reduction in environmental burden and the creation of a recycling-oriented society" (environment), "Ensure mutual prosperity involving all stakeholders via the creation of a working environment in which everyone can E work with enjoyment" (society), "Pursue sound and highly transparent management by constantly updating our approach" (governance), and "Make people happier, help their communities flourish, and strive for a better society via the use of technology" (business), and its policy is to realize sustainable corporate growth and a sustainable society.

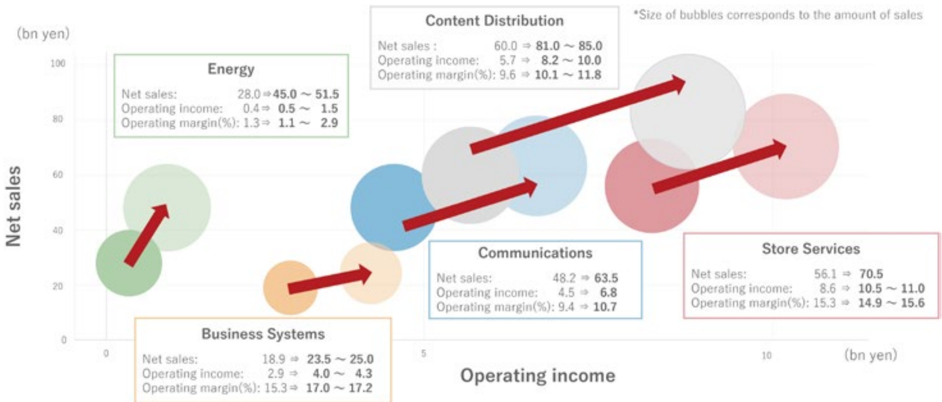
The content distribution business and store DX are driving growth

2. Growth strategy by segment

The Company conducts business portfolio management on classifying businesses into the cash cow business, stable-growth businesses, and high-growth businesses, and it has not changed its previous policy of redistributing growth funds from the cash cow business to the high-growth businesses. It classifies the cash cow business as music distribution in the store services business, the stable-growth businesses as the business systems business and the communications business (within which, ICT for corporations), and the high-growth businesses as the content distribution business and store DX (in the store services business, POS cash registers and Wi-Fi, and in the communications business, the Group's own optical lines for commercial stores, etc.)

For the FY8/25 operating profit targets by segment, in the content distribution business, the target is ¥8.2bn to ¥10bn; in the store services business, ¥10.5bn to ¥11bn; in the communications business, ¥6.8bn; in the business systems business, ¥4bn to ¥4.3bn, and in the energy business, ¥0.5bn to ¥1.5bn. It seems the targets for each business have been divided into a base case and an upside case. For Company-wide costs, the profits from the upside case, of the profits exceeding the base case, will be used as the source, and it seems that it will additionally allocate funds to investment to strengthen the Group's growth potential and ability to adapt to its environment, including for human resources development, education, and re-skilling training, and also for corporate branding and to enhance welfare.

Growth image by segments



Source: The Company's medium-term management plan materials

(1) Content distribution business

The video distribution market is a growth market in which competition is fierce, so the Company will further strengthen its "coverage strategy" and "ONLY ON strategy" that are the sources of its competitive advantages. In conjunction with this, in music distribution services, it will start its own fully fledged distribution of non-video content, such as deeply related live music and music content, and it will monetize content including by creating videos of popular IP in original e-books, such as manga and novels. For these highly competitive Company contents, which include videos, books, music, and live performances, its policy is to enhance all-in-one entertainment by enabling them to be enjoyed on a single app. As a result, in FY8/25 it is aiming for the number of paid subscribers to reach 3.1mn to 3.5mn (four-year CAGR of 7% to 10%), recurring sales alone of ¥72.3bn to ¥76.7bn (four-year CAGR of around 6%), and operating profit of ¥8.2bn to ¥10bn. It seems that the reason why the difference between the operating profit base case and upside case is larger than that of other businesses is that it is difficult to forecast consumption trends in the with / after COVID-19 period and also the pace of expansion of growth markets. Incidentally, the base case assumes that growth will temporarily slow down as a rebound to the nesting demand, but it is growing steadily at the current time and when considering that Japan's content distribution market still has plenty of room to grow compared to Europe and the United States, at FISCO we think that it is probably already unnecessary to assume the base case.

(2) Store services business

The Company is working on a strategy centered on store DX for which high growth is expected, and it is assumed that music distribution will trend from unchanged YoY to a slight decrease. In terms of what it is focusing on the most, its policy is to continue to provide stores with total work support, from their front work through to their back office work, by building a communications environment, such as Wi-Fi, and installing smart devices, including POS cash registers, It is also promoting up-sales through a one-stop service by the Group, from sales through to maintenance. Further, by building a partner network of 10,000 companies, it obtains 100,000 items of new business information per year, and it is strengthening highly responsive direct sales for newly opened stores that have a high contract completion rate. For already opened stores, for both existing customers and unacquired customers, it utilizes non-direct sales channels, including agencies and telemarketing, from the viewpoint of sales efficiency. By implementing these measures, the Company intends to increase the number of contracts from 912,000 at the end of FY8/21 to 1.052mn by the end of FY8/25. It also plans to increase the number of billings by POS cash registers, which is a typical smart device, from 21,000 cases to 41,000 cases.

(3) Communications business

In ICT/SaaS for corporations, the Company is focusing on cross sales, including support for security measures that have become more complex and maintenance and operations outsourcing for cloud and data centers as a BCP measure. In digital infrastructure, it is expanding its lineup, while in office environment improvements, it is responding by developing new services. In sales, on the one hand it is creating new potential customers by strengthening digital marketing, while on the other hand it is establishing new sales methods tailored to the times, such as online sales negotiations and inside sales. In optical lines for commercial stores, it is further progressing switching from agency lines to its own highly profitable lines, while at the same time, it is accelerating up-sales of IoT/DX products. Through these efforts, for the FY8/25 results, it is aiming for net sales of ¥25.9bn (four-year CAGR, 9%) and operating profit of ¥4.2bn (7%) for ICT/SaaS for corporations, and net sales of ¥11.7bn (18%) and operating profit of ¥600mn (stably achieve profits) for the Group's own optical lines for commercial stores.

(4) Business systems business

For its existing customers of hotels and general hospitals, the Company will strengthen DX support based on their needs for non-face-to-face and contactless operations, and for labor saving and improved efficiency. Also, by leveraging facility DX solutions, from a position of simply selling and maintaining automated payment machines, it is aiming to have a presence one stage higher as a visionary partner for its customers. In particular, for hotels, the Company expects a return to Japan's growth strategy of becoming a leading healthcare and tourist destination country through the recovery of inbound demand. For small clinics, dentists, dispensing pharmacies, and other establishments, from “Myna Touch” as the starting point, it will dig deeply to develop markets, including by enhancing cross-sale products and services. Conversely, for adjacent markets, including golf courses, retailers, restaurants, pet clinics, and tourist facilities, it will progress developments of products that incorporate the latest technologies, such as AI, biometric authentication (face authentication), and cashless and post-payment payments. Through these efforts, in FY8/25 it is targeting net sales of ¥13.1bn for hotels (four-year CAGR of 3%), ¥7.5bn for general hospitals (10%), and ¥4.4bn for adjacent markets (19%).

(5) Energy business

In the “USEN Energy” agency model, for commercial stores the Company is proposing measures including cost reductions and cross sales after cost reductions, while for offices, using set services, which including environmental BGM, as the entry point, it is building a system that is able to provide comprehensive proposals. It intends to further strengthen “U-POWER,” which is the Company's own highly profitable energy procurement model launched in March 2022. In this situation, it intends for highly competitive green energy that is compatible with the SDGs to drive the growth of “U-POWER.” Through these efforts, the numbers of “USEN ENERGY” customers in FY8/25 are forecast to increase to 50,000 customers (four-year CAGR, 22%) for low voltage, but to hardly increase (basically unchanged) for high voltage, at 7,000 to 8,000 customers. It is aiming for the number of “U-POWER” customers to increase significantly by from 41,000 to 62,000 customers (from zero in FY8/21).

Progress made for the medium-term management plan is for the upside case

3. Progress of the medium-term management plan

In the medium-term management plan, which has only just started, performance overall has been excellent, centered on content distribution and store DX, and if excluding the impact of the weak yen, from among the two results scenarios it seems progress is being made in accordance with the upside case. However, a risk is the rapidly weakening yen, and the content distribution business has taken a direct hit for purchases of overseas content denominated in foreign currencies. But as previously stated, in the short term the Company plans to improve the operating profit margin including by increasing the domestic procurement ratio, leveraging its strength of having close to 3mn paid subscribers to review transaction conditions, and reducing user acquisition costs, and it seems it will be able to absorb this risk in the medium term. More than the above, it is considered that the current situation, which is characterized by an increase in the movements of people following the lifting of movement restrictions, the recovery of inbound demand, and the labor shortages, will have a major positive impact on its businesses, particularly on the store services business and the business systems business. Therefore, currently progress is being made for the upside case and it seems that this will continue in the future also.

Shareholder return policy

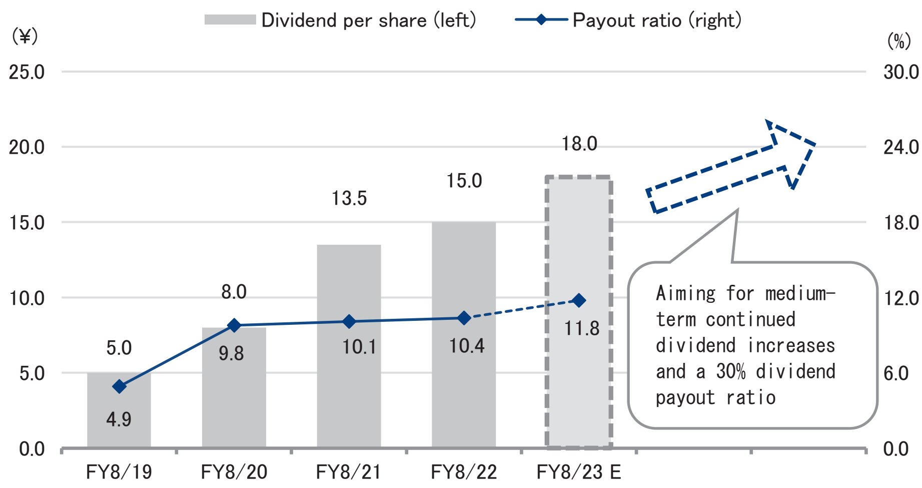
Policy is to continuously increase the dividend, targeting a dividend payout ratio 30%

1. Dividend policy

With regard to dividends, the Company has a fundamental policy of allocating surplus funds once a year at period-end based on results assessed comprehensively in terms of the financial position, profit situation, new investment plans, and other factors, and the general meeting of shareholders is the decision-making body for the payment of dividends from retained earnings. The Company views return of earnings to shareholders as a key corporate policy and paid a year-end dividend of ¥15.0 per share in FY8/22 as the result of an overall assessment of results and other factors in accordance with the fundamental policy. It plans to pay an annual dividend* of ¥18.0 per share in FY8/23. Although it is currently in an investment phase, the Company is aiming for a 30% dividend payout ratio in the medium-term and its policy is to continue increasing the dividend.

* From FY8/23, its basic policy is to pay dividends twice a year, an interim dividend and a period-end dividend.

Trends in dividend per share and payout ratio



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

Will end the “Premium Benefit Club,” but “U-NEXT” content distribution service will continue

2. Shareholder benefit program

The Company offers a shareholder benefit program to show appreciation to shareholders for their support, deepen shareholders’ understanding of business content by using Group services, and enhance the investment appeal of its shares and encourage long-term ownership. Specifically, for the “U-NEXT” content distribution service, shareholders with holdings of 100 shares to 999 shares receive 90 days of free service use along with ¥1,000 worth of points, and shareholders whose holdings amount to 1,000 shares or more receive one year of free service use and ¥1,800 worth of points each month. The Company plans to end the provision of the “Premium Benefit Club,” which is one of its shareholder benefits programs, on the last day of February 2023, and in the future it intends to reward shareholders mainly by increasing dividends. It will continue the “U-NEXT” shareholder benefits program as it is considered to be highly rational as a benefit for individual investors.

Information security

Reducing security risk for the Group as a whole

The Company is strengthening personal information protection capabilities and continues to implement educational programs. However, it cannot give a guarantee of complete protection and there is always risk of personal information leaks due to improper access from an external source, system trouble, insider crime, human mistakes, and management mistakes at outsourcing and service provision partners. Given these challenges, the Company manages the information system at a data center, employs a firewall, and continually assesses vulnerability in web applications as a more proactive information security effort. The Company allocates notebook PCs and smartphones to individuals as part of work-style reforms. It uses notebook PCs installed with a security chip (TPM), while its smartphones use mobile device management (MDM). Moreover, in order to provide services that can be used safely and securely, the Group as a whole is reducing security risk by establishing “Usirt,” centered on the Company, and implementing external audits in a planned manner.

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