COMPANY RESEARCH AND ANALYSIS REPORT

Fuyo General Lease Co., Ltd.

8424

Tokyo Stock Exchange Prime Market

14-Mar.-2023

FISCO Ltd. Analyst
Ikuo Shibata

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

Index

Summary

Set new record highs (on an H1 basis) again in H1 FY3/23, with balanced growth in each business. Also seeing a certain level of results based on various initiatives carried out in coordination with partner companies

Fuyo General Lease Co., Ltd. <8424> (hereinafter, "the Company") is a comprehensive leasing company established in 1969 by six Fuyo Group companies, including The Fuji Bank, Limited (currently Mizuho Bank, Ltd.) and Marubeni-Iida Co., Ltd. (currently Marubeni Corporation <8002>). Its strengths include real estate and energy & environment, and it has an annual newly executed contract volume of ¥1,384.4bn (FY3/22 result) and operating assets of ¥2,601.5bn (as of September 30, 2022). In addition to the steady increase in operating assets in business fields it has positioned as strategic fields, such as real estate, the Company is steadily expanding its earnings through expanding the functions of BPO services* from M&A. The Company started its new medium-term management plan Fuyo Shared Value 2026 (five years) from FY3/23, and is aiming for sustainable growth by simultaneously "resolving social issues" and delivering "economic value."

* Business Process Outsourcing: A service that contributes to operational improvements and increased efficiency by handling some of client companies' business processes.

1. Summary of H1 FY3/23 results

In the H1 FY3/23 results, operating profit increased 14.9% year-on-year (YoY) to ¥27.0bn, ordinary profit grew 13.2% to ¥31.1bn, and profit attributable to owners of parent rose 12.3% to ¥20.3bn, as all profit lines posted increases, with the Company marking a new record high in profit (on a H1 basis). Profit before interest expenses, which shows true business performance, grew steadily, increasing 10.6% to ¥53.3bn, due to growth in the growth drivers such as energy & environment, real estate and aircraft, as well as other factors including the fact that WorkVision Corporation (formerly Toshiba Solutions Sales Corporation), which the Company brought under its scope of consolidation in October 2021, contributed to profits from the start of the fiscal year. Looking at ordinary profit by business field, in addition to real estate and aircraft, profit also grew in mobility, energy & environment, and BPO/ICT, so it can be said that the Company achieved balanced growth in profits across fields. In terms of activities, the Company has been laying the groundwork for the future in all directions through efforts including coordination with highly-specialized partner companies (including overseas companies) and M&A.

2. FY3/23 results outlook

For the FY3/23 results, the Company is forecasting higher revenues and profits, unchanged from the initial forecast, with total revenues to increase 6.4% YoY to ¥700.0bn, operating profit to grow 11.9% to ¥51.5bn, ordinary profit to rise 6.2% to ¥56.0bn, and profit attributable to owners of parent to increase 6.2% to ¥36.0bn. It is also forecasting a higher dividend, which it has increased continuously since being listed. The accumulation of operating assets, centered on real estate and energy & environment that continue to perform well, recovery of aircraft, collaboration with WorkVision and the growth of BPO/ICT (an increase in non-asset earnings) are expected to contribute to the increase in profits. The Company plans to further improve ROA as well through asset control that prioritizes profitability and the growth of non-asset earnings.

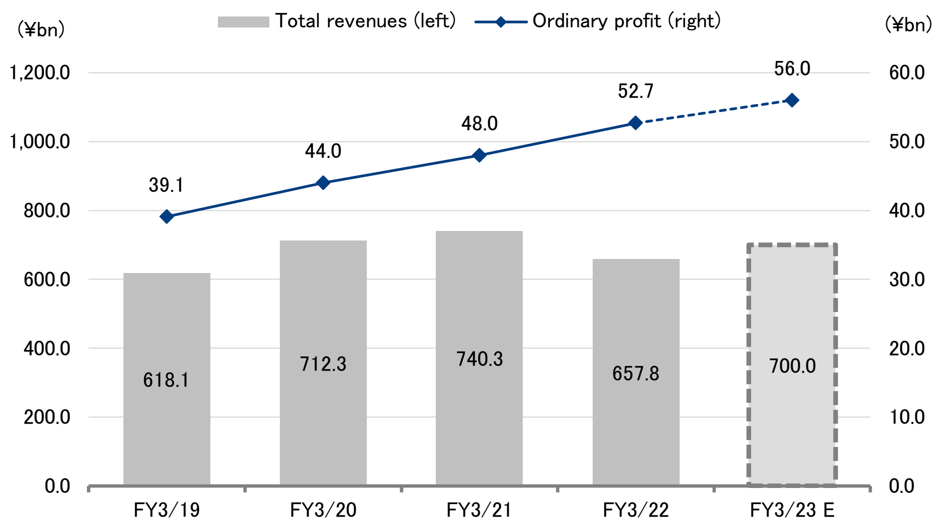
3. Medium-term management plan

Fuyo Shared Value 2026 (five years), the Company's medium-term management plan that started from FY3/23, is based on a strategy of achieving sustainable growth by realizing enterprise value and social value simultaneously, and it sets both financial and non-financial items for its management targets. Growth will be driven by: 1) the Rising Transformation ("RT") field (mobility and circular economy) that is aiming for strategic growth enabled by capturing tectonic social changes; 2) the Accelerating Transformation "AT" field (energy & environment, BPO/ICT, and medical/social welfare) that aims for accelerating growth based on an understanding of market trends, and; 3) the Growing Performance "GP" field (real estate and aircraft) that is aiming for stable growth of the core fields. Then, the strategy is to improve earnings through concentrated investment of management resources into the RT and AT fields where market expansion and creation are expected and also through differentiation in the GP field. The financial targets are ordinary profit of ¥75.0bn, ROA of 2.5%, an equity ratio of 13% to 15%, and ROE of at least 10%, while the Company has also set non-financial targets for all items to be addressed, centered on the environment (a decarbonized society and a recycling-based society), society and people, and human resources investment.

Key Points

- Set new record high profits (on a H1 basis) again in H1 FY3/23, with balanced growth in each business
- In terms of activities, laying the groundwork for the future in all directions through efforts including coordination partner companies
- The Company left its initial forecasts for FY3/23 unchanged, and expects continued increases in sales and profits, as well as consecutive dividend increases since its shares were listed
- Started the new five-year medium-term management plan. The direction it is aiming for is achieving sustainable growth by "resolving social issues" through human growth and dialogue while at the same time delivering economic value

Trends in total revenues and ordinary profit



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

Company profile

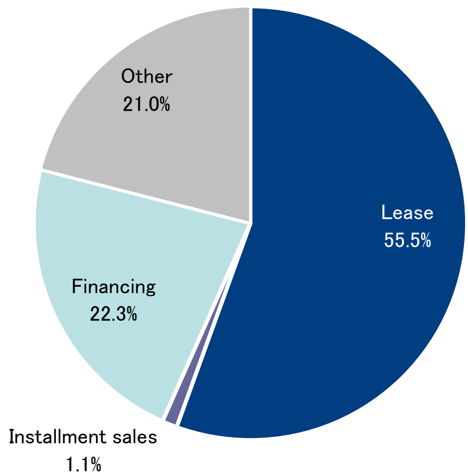
Comprehensive leasing company with strengths in real estate, energy & environment, and other areas. Also working to strengthen new domains, such as BPO/ ICT and the mobility

1. Business overview

The Company has three business segments - lease and installment sales, financing, and other – but discloses "lease" and "installment sales" separately. The mainstay lease business accounts for 63.3% of operating assets and 55.5% of profit before interest expenses* (H1 FY3/23 results). As future growth drivers, the Company plans to proactively invest management resources in business fields including mobility, energy & environment, BPO/ICT, medical/social welfare, real estate and aircraft, and over the medium to long term its policy is to move away from "nontraditional leasing" and "non-financial services."

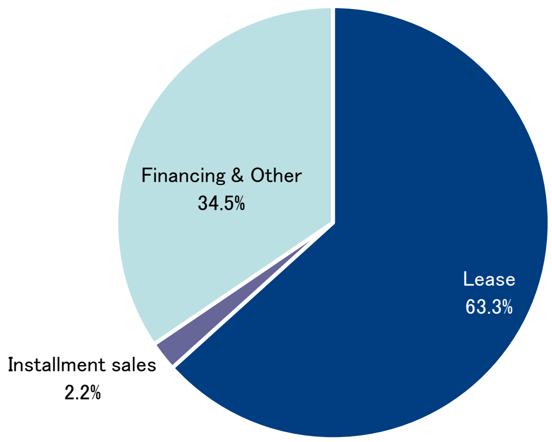
* Gross profit before deducting interest expenses.

Composition of profit before interest expenses by segment (H1 FY3/23)



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

Ratio of operating assets by segment (H1 FY3/23)



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

Below, we review the Company's business segments.

(1) Lease and installment sales

This segment handles leases of information and communications equipment, office equipment, industrial machine tools, and other equipment and installment sales of commercial facilities, production facilities, hospital facilities, and other facilities. In the lease business, the leasing company purchases and leases machinery, equipment, or other facilities selected by customers for a certain leasing fee over a relatively long period. In other words, leases constitute a funding method (financial transaction) that focuses on facility deployment. Benefits to customers, versus outright purchase (and ownership) of facilities, include efficient utilization of capital, reduction of administrative burden, avoidance of risk from outdated facilities, and cost control. Leasing companies, meanwhile, face less collection risk than ordinary loan transactions, because they possess ownership rights to the leased equipment. The Company conducts installment sales for equipment that does not qualify as leasing for tax purposes and cases in which the customer wants direct ownership.

Looking at the volume of newly executed lease contract volume by type of equipment, substantial growth has been experienced in buildings, etc. (real estate leases) and transportation equipment in the past few years. Key drivers in real estate leases are commercial properties (such as large shopping centers), an area of expertise, as well as diversification of properties including hotels, nursing care and residential, leisure, services, and logistics, following the expansion in alliance partners. The Company leverages its experience of over 30 years and an extensive network in this business given the need for expertise and knowhow with tough legal hurdles and complex rights relationships. Also, the growth of transportation equipment up until recently was due to aircraft leases. However, the Company's strengths include its track record and expertise accumulated over many years. In addition, it is aiming to strengthen the mobility business, which is expected to grow in the future, through making YAMATO LEASE CO., LTD.* a consolidated subsidiary (in April 2020).

* Started making a consolidated subsidiary of YAMATO LEASE, which was a subsidiary of YAMATO HOLDINGS CO., LTD <9064> in April 2020. The Company's shareholding ratio became 60% and YAMATO HOLDINGS became 40%.

(2) Financing

This segment covers capital investment funding and other business loans, real estate financing, and securities-related management tasks. Its operating assets include corporate operating loans (such as syndicate loans) and retail funding through consolidated subsidiary Sharp Finance Corporation (hereafter, "SFC"). The Company added a factoring business* by making Accretive Co., Ltd. a consolidated subsidiary (in January 2017).

> * This business mainly handles FPS (early payments service for accounts receivable) for small- and medium-sized companies, and FPS Medical (early payment service for medical and care fee credits) for medical institutions.

(3) Other

This segment includes large-scale solar power operations (renewable energy business) handled directly by the Company, silent partnership originations for aircraft leases and other businesses, and the life insurance agency business. Also, the Company has built a structure to respond to various BPO needs with the addition of an integrated billing service* provided by INVOICE INC., which was made into a consolidated subsidiary in October 2018, and wide-ranging back-office services (including accounting, human resources and salary, general affairs and sales administration) provided by NOC Outsourcing & Consulting, Inc. (hereinafter, "NOC") which was made into a consolidated subsidiary in August 2019. In October 2021, the Company expanded its service functions even further with the consolidation of WorkVision, which provides IT solutions centered on cloud packages (DX support, etc.).

> * A service that handles making burdensome monthly payments to telecom carriers and other utilities on behalf of customers.

2. History

The Company was established in 1969 with six companies from the Fuyo Group as shareholders led by Fuji Bank (now Mizuho Bank) and Marubeni-Iida Co., Ltd. (now, Marubeni).

It steadily broadened business scope thereafter and created a local entity in the US in 1988. It established a local entity in Ireland (Dublin), a major center for aircraft leases, in 1999. The Company was relatively early in its entry to aircraft business, which has recently attracted attention from many companies, and accumulated a track record and know-how with leveraged leases (aircraft leases with investor subscriptions) and other formats.

The Company has also teamed up with other companies to establish joint ventures, such as Yokogawa Rental & Lease Corporation (holds a large share in measuring instruments) with Yokogawa Electric Corporation <6841> in 1987 and Nihon Credit Lease Co., Ltd.* (holds a large share in medical equipment and welfare equipment) with NICHIIGAKKAN CO., LTD. in 1999.

> * In January 2022, the Company carried out an absorption-type merger of Nihon Credit Lease with the Company as the surviving company.

Major turning points were listing shares on the First Section of the Tokyo Stock Exchange in December 2004 and acquisition of SFC as a consolidated subsidiary (buying a 65% stake) in April 2008. SFC controls a strong share in the retail (vendor lease) area and contributed substantially to broadening business scope and increasing scale.

In July 2014, the Company acquired ALM 2010 Limited (it changed the name to Fuyo Aviation Capital Europe Limited; hereinafter ALM), a UK-based aircraft-related services company, as a consolidated subsidiary (buying all shares) and thereby strengthened its ability to expand aircraft business.

In January 2017, it acquired Accretive, a subsidiary of Don Quijote Holdings Co., Ltd. (Pan Pacific International Holdings Corporation <7532>) that operates a factoring business (purchase of accounts receivable) mainly for small and medium-sized companies, as a consolidated subsidiary. In addition to pursuing synergies through cross-selling with each company in the Group, the Company is also progressing other measures, including strengthening measures for the new domains. In October 2018, the Company made INVOICE, an integrated billing service provider, a consolidated subsidiary and then in August 2019, it made NOC, a back-office service provider with a wide range of operations, a consolidated subsidiary in an effort to strengthen the BPO services business. In April 2020, it made a consolidated subsidiary of YAMATO LEASE, a subsidiary of YAMATO HOLDINGS, establishing footholds toward the development of the mobility business, which is considered to have growth potential, and for the logistics industry.

Financial results

Profit before interest expenses, which shows true business performance, is trending upward, including through the accumulation of operating assets and the growth of non-asset earnings

1. Key points for assessing results

The Company's total revenues consist of lease fee revenue (over 80% of overall sales), revenue from installment sales, interest income on financing, and non-asset earnings (such as fee income). Since total revenues (excluding non-asset earnings) fundamentally fluctuate with operating assets, the Company needs to increase newly executed contract volume and accumulate more operating assets in order to expand total revenues. However, it should be noted that accounting of mainstay lease fee revenue reflects the purchase transaction and includes the price of the leased item. Consequently, profit before interest expenses excluding the acquisition cost of leased equipment from total revenues is the suitable indicator for assessing actual income growth as a financing business.

Meanwhile, to ascertain the profitability of the Company's main business, the most rational approach is thought to be monitoring trends in ordinary profit, in which expenses such as interest expenses (fund-raising costs), personnel and equipment expenses, and costs related to bad debts (including reversals)*, are deducted from profit before interest expenses. Ordinary profit is obtained by multiplying operating assets by ROA (ratio of ordinary profit to operating assets), so it is affected by movements in both. Also, most recently, the Company has been working to grow non-asset earnings, so it is also necessary to pay attention to the Other segment.

* This is the net value of provision of allowance for doubtful accounts (SG&A expenses) and reversal of allowance for doubtful accounts (non-operating income).

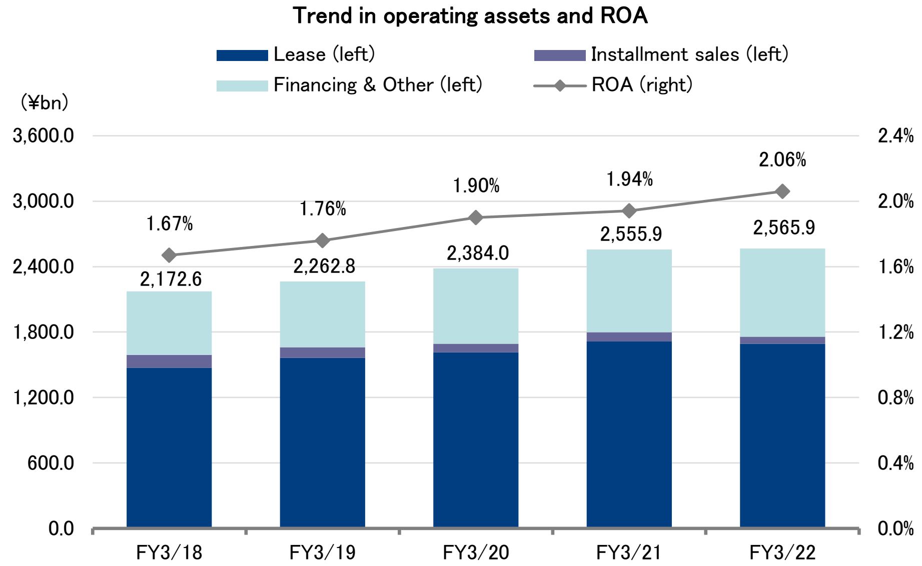
2. Past results trends

Looking back on past results trends, total revenues have trended upward alongside the accumulation of operating assets. Ordinary profit has also continued to increase from both the accumulation of operating assets and the improvement of ROA. The improvement of ROA has been particularly due to the growth of real estate leases and aircraft leases, which have comparatively high yields, while most recently, the growth of new-domain businesses (non-asset earnings), mainly BPO services, has also been contributing.

From a cost perspective, meanwhile, Interest expenses have been largely flat. This trend, despite growth in total funding value, is driven by a decline in interest on funding due to the impact of market rates. Additionally, the Company keeps personnel and equipment expenses at a certain level and has a low bad debts-related costs, demonstrating the company's strength in low-cost operations. As a result, ordinary profit for FY3/22 reached all-time highs.

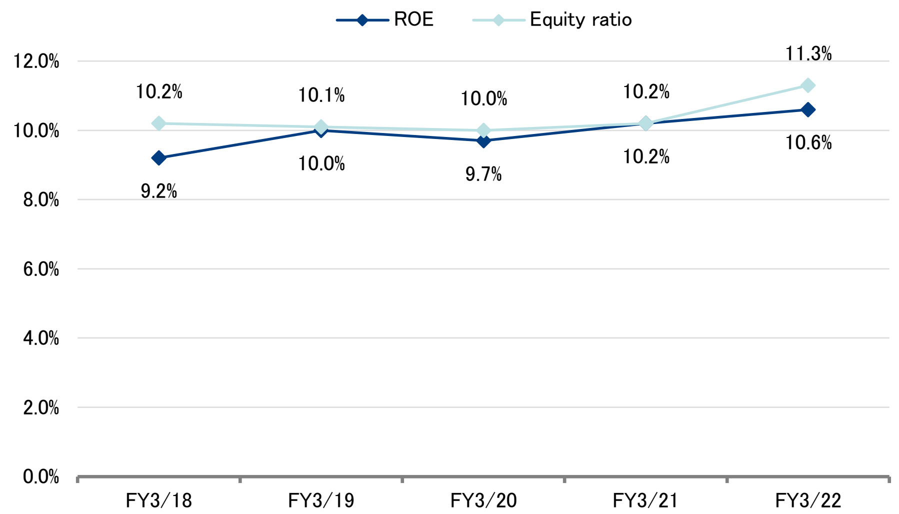
Interest-bearing debt has been growing due to the accumulation of operating assets, but the equity ratio remains steady at about 10%. The 10% range does not compare unfavorably to other companies in the leasing industry, which possesses large amounts of highly liquid operating assets, and should not spark concerns about stability of the Company's financial base.

In addition, ROE (Return on Equity), which shows capital efficiency, has been increasing alongside the rise in the profit level, and it has exceeded 10% since FY3/21.



Note: ROA is calculated as ordinary profit (annualized) ÷ operating assets (average balance)
Source: Prepared by FISCO from the Company's financial results

Trend in equity ratio and ROE



Note: FY3/19 and FY3/20 reflect the values determined through accounting treatment for business combination in FY3/20
Source: Prepared by FISCO from the Company's financial results

3. Summary of H1 FY3/23 results

In the H1 FY3/23 results, operating profit increased 14.9% YoY to ¥27.0bn, ordinary profit rose 13.2% to ¥31.1bn, and profit attributable to owners of parent grew 12.3% to ¥20.3bn, and every profit item increased and set new record highs* (on an H1 basis).

* Ordinary profit marked a new record high for the sixth consecutive period, while profit marked a new record high for the eighth consecutive period.

Profit before interest expenses (gross profit before deducting interest expenses), which shows true business performance, grew steadily, increasing 10.6% YoY to ¥53.3bn, due to increases in the growth drivers such as energy & environment, real estate and aircraft, as well as other factors including the fact that WorkVision Corporation (BPO/ICT), which the Company brought under its scope of consolidation in October 2021, contributed to profits from the start of the fiscal year.

Ordinary profit also increased 13.2% due to factors including the growth in profit before interest expenses and the increase in earnings from equity-method investments*. Looking at ordinary profit by business field, in addition to real estate and aircraft, profit also grew in mobility, energy & environment, and BPO/ICT, so it can be said that the Company achieved balanced growth in profits across each field.

* Notably, there was a strong performance by an equity method affiliate in Canada (leasing and rental of pickup trucks) and by Yokogawa Rental & Lease Corporation (rental of PC and measuring instruments), which is a joint venture with Yokogawa Electric Corporation.

Meanwhile, looking at expenses, interest expenses were roughly flat. Going forward, while there is concern about an increase in fund-raising costs accompanying the rise in overseas market interest rates, the impact is expected to be limited due to the fact that foreign currency-denominated interest-bearing debt does not account for a significant percentage of the Company's overall fundraising. Additionally, personnel expenses increased due to factors including the consolidation of WorkVision, but OHR was maintained at a favorable level. The default risk of credits held by the Company was also kept at a low level.

Newly executed contract volume increased 9.0% YoY to ¥701.6bn. In energy & environment, there was a large increase in equity investment (participation in renewable energy business), while there was also a big increase in real estate financing. Meanwhile, in leases, executed contract volume struggled to grow in mobility due to the impact of the prolongation in delivery times for new cars in mobility, but for the full fiscal year it seems that the Company is forecasting the executed contract volume to be on par with the previous year. The Company was able to grow operating assets by 1.4% versus the end of the previous fiscal year to ¥2,601.5bn, as the growth in energy & environment and real estate covered the exits from a large project in real estate.

As a result, ROA* improved sharply to 2.41% (2.15% in the year-earlier period). ROA is steadily improving with advances in converting the portfolio to highly profitable asses and expansion of business domains.

* Ordinary profit (annualized) ÷ operating assets (average balance)

For the financial condition, total assets increased 1.4% on the end of the previous period to ¥2,991.3bn and were basically unchanged YoY, while core capital increased 7.4% to ¥357.4bn due to the accumulation of internal reserves, and as a result the equity ratio improved to 11.9% (11.3% at the end of the previous period). Also, interest-bearing debt (excluding lease obligations) increased slightly by 1.1% versus the end of the previous period to ¥2,391.1bn*1, but the long-term interest-bearing debt ratio*2 was basically flat at 43.1% (43.2% at the end of the previous period).

*1 In particular, the Company is proactively advancing ESG finance initiatives, and became the first leasing company to procure funds through syndicated Positive Impact Finance.
*2 The long-term debt ratio of interest-bearing debt represents the ratio of long-term interest-bearing debt (corporate bonds + long-term borrowings + long-term payables under securitization of lease receivables) to interest bearing debt.

Summary of H1 FY3/23 results

(¥bn)

	H1 FY3/22		H1 FY3/23		YoY change	
	Results	%	Results	%	Amount	%
Total revenues	285.4		356.0		70.6	24.7%
Lease	238.8	83.7%	303.3	85.2%	64.5	27.0%
Installment sales	16.8	5.9%	15.7	4.4%	-1.1	-6.3%
Financing	11.6	4.1%	12.1	3.4%	0.5	4.4%
Other	18.2	6.4%	25.0	7.0%	6.7	36.9%
Profit before interest expenses	48.1	16.9%	53.3	15.0%	5.1	10.6%
Lease	26.9	11.3%	29.6	9.8%	2.6	9.7%
Installment sales	0.8	4.8%	0.6	3.8%	-0.1	-17.6%
Financing	11.4	98.3%	11.9	98.3%	0.5	4.1%
Other	9.0	49.5%	11.2	44.8%	2.2	23.9%
Interest expenses	4.7	1.6%	4.8	1.3%	0.1	2.1%
Gross profit	43.4	15.2%	48.4	13.6%	5.0	11.5%
SG&A expenses	19.9	7.0%	21.4	6.0%	1.5	7.5%
Operating profit	23.5	8.2%	27.0	7.6%	3.5	14.9%
Ordinary profit	27.4	9.6%	31.1	8.7%	3.6	13.2%
Profit attributable to owners of parent	18.0	6.3%	20.3	5.7%	2.2	12.3%
By business field (ordinary profit)	27.5		31.1		3.6	
Mobility	2.2		2.6		0.3	
Energy & environment	1.4		1.8		0.4	
BPO/ICT	1.7		1.9		0.3	
Social welfare	1.1		1.0		-0.1	
Real estate	9.2		10.8		1.6	
Aircraft	0.4		2.4		2.0	
General leasing and financing	11.6		10.7		-0.9	
Newly executed contract volume	643.8		701.6		57.8	9.0%
Financing & Lease	124.1	19.3%	112.8	16.1%	-11.2	-9.1%
Operating & Lease	103.0	16.0%	80.5	11.5%	-22.4	-21.8%
Installment sales	11.2	1.7%	11.7	1.7%	0.5	4.8%
Financing & Other	405.4	63.0%	496.4	70.7%	91.0	22.5%

	As of March 31, 2022 Results	As of September 30, 2022 Results	Amount	%
Operating assets	2,565.9	2,601.5	35.6	1.4%
Financing & Lease	1,019.7	898.0	-121.6	-11.9%
Operating & Lease	671.8	748.0	76.2	11.3%
Installment sales	66.0	58.6	-7.3	-11.2%
Financing & Other	808.2	896.7	88.4	10.9%

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

4. Business performance and activities by business field

(1) Mobility (RT field)

As of the end of September 2022, operating assets were slightly lower than at the end of FY3/22, having declined ¥3.3bn to ¥160.8bn. On the other hand, ROA improved to 3.1% (2.6% in the year-earlier period), leading to ordinary profit of ¥2.6bn (up ¥0.3bn YoY). Although the Company struggled to accumulate operating assets due to the prolongation of delivery times for new cars against the backdrop of the global shortage of semiconductors, the soaring used car market and strong rental income of overseas affiliates contributed to the increase in profit. In terms of activities, the Company approached new business domains, including participating in a proof-of-concept test targeting the implementation of autonomous vehicles*1 and the building of GREEN FORK*2, a forklift lease package that utilizes a reused battery.

*1 As a joint project with partner companies, the Company participated in a proof-of-concept test for local public agencies, etc. utilizing an autonomous vehicle owned by the Company. This can be viewed as an initiative aimed at resolving social issues, including ensuring freedom of mobility, reducing traffic accidents, improving productivity, revitalizing local communities, and reducing environmental load.

*2 An initiative in partnership with IGUAZU Corporation, which holds patent technology for reused batteries. Utilizing reused batteries can significantly reduce battery costs and CO_2 emissions.

(2) Energy & environment (AT field)

The balance of operating assets as of the end of September 2022 increased ¥16.4bn from the end of FY3/22 to ¥106.8bn, while ordinary profit grew ¥0.4bn YoY to ¥1.8bn due to the fact that ROA improved to 3.6% (3.0% in year-earlier period). The renewable energy business grew in Japan and overseas, while the renewable energy power generation capacity (a non-financial target) grew steadily, increasing 56MW compared to the end of FY3/22 to 374MW (medium-term management plan target is 1,000MW)*1. In terms of activities, the Company began actively investing in Europe in collaboration with global players. This included investing in a U.K. offshore wind power generation project*2 and investing in a renewable energy fund (solar PV, wind power, hydropower, etc.)*3 in the European Economic Area. In addition, aiming to expand the storage battery-related business, the Company is focusing on realizing co-creation projects with a wide range of partners including energy companies.

*1 562MW including projects under development (up 115MW versus end-March 2022)

*2 Through an investment in an investment fund managed by U.K.-based Equitix Investment Management Ltd., which has assets under management of approximately 8.5 billion pounds. This is the Company's first investment in an offshore wind project, but the project covers an offshore wind power facility that is already in operation, so there is no development risk.

*3 Through an investment in a renewable energy fund of Germany-based Aquila Capital Holding GmbH, which as an overall group operates and manages approximately 13.2 billion euros in assets (as of June 30, 2022).

(3) BPO/ICT (AT field)

The balance of operating assets as of the end of September 2022 decreased slightly by ¥1.5bn from the end of FY3/22 to ¥47.0bn, but ROA improved to 2.6% (2.1% in year-earlier period) while ordinary profit grew ¥0.3bn YoY to ¥1.9bn. The business expanded steadily in both BPO and ICT as a result of meeting growing BPO needs and through the partnership with WorkVision which was consolidated in October 2021. In terms of the non-financial target of work hours saved by customers, compared to FY3/22 there were 0.12 million hours saved (the target in the medium-term management plan is 1 million hours) so this got off to an excellent start. In terms of activities, the Company executed M&A in order to bolster BPO service functions*1, and was also able to achieve successful outcomes in expanding approach targets though collaboration with partners*2.

*1 In October 2022, the Company made Human CentriX Co., Ltd. a consolidated subsidiary. Human CentriX has a top-level track record in Japan in the video production/distribution business for BtoB companies. While the impact on business performance was minor, the aim was to acquire new business efficiency improving solutions that support customers' DX.

*2 The Company concluded a business alliance with Yasuda Logistics Corporation <9324> in the BPO service business area as well as a business alliance with OKI Crosstech Co., Ltd. of OKI Electric Industry Group in the area of outsourcing for IT operations. Also, the Company is partnering with The Michinoku Bank on an integrated billing service, and working with TEPCO Energy Partner, Inc. on TEPCO Billing Collection Service.

(4) Social welfare (AT field)

The balance of operating assets as of the end of September 2022 was ¥89.2bn (¥0.1bn less than at the end of FY3/22), and ROA was flat at 2.2% (2.2% in year-earlier period), with ordinary profit declining slightly by ¥0.1bn YoY to ¥1.0bn. The accumulation of medical and care fee credits factoring showed sluggish growth as a result of satisfaction of financing needs due to financial support from the government and other entities. In terms of non-financial targets, the number of nursing care facilities for the elderly (number of new rooms provided) was 110 rooms (the target in the medium-term management plan is 1,000 rooms), while financing that provides management support to customers in the medical and social welfare markets*1 was ¥19.5bn (medium-term management plan target of ¥56.0bn). In terms of activities, the Company worked to build a business model for medical/nursing care BPO*2 and strengthen solutions*3 for business operators with revitalization and business succession needs.

*1 FPS Medical, operating assets related to business succession, etc.

*2 Concluded a capital and business agreement with JSH Co., Ltd., which offers an employment support service for people with disabilities and a home medical care service specialized in psychiatry, and started collaboration aiming to build a business model for medical/nursing care BPO.

*3 Acquire business succession projects for healthcare corporations in collaboration with partners (expecting to execute in H2) and advancing the establishment of a healthcare fund specializing in medical/nursing care.

(5) Real estate (GP field)

The balance of operating assets as of the end of September 2022 was ¥967.4bn (¥32.5bn increase versus the end of FY3/22), and ROA was 2.3% (2.2% in year-earlier period), leading to ordinary profit increasing ¥1.6bn YoY to ¥10.8bn. Although there was an impact from the exit from a large real estate lease project, the accumulation of assets in the overall business resulted in a significant increase in profit. The Company plans to continue to conduct business operations with attention to risk-return in light of rising real estate prices due to continued active investments by real estate investors in Japan and overseas, as well as soaring construction costs associated with supply chain disruptions and other factors.

(6) Aircraft (GP field)

The balance of operating assets as of the end of September 2022 was ¥219.6bn (¥24.2bn increase versus the end of FY3/22), and ROA improved significantly to 2.3% (0.4% in year-earlier period), leading to ordinary profit increasing ¥2.0bn YoY to ¥2.4bn. The large increase in profit was due to factors such as the decline in bad debt-related expenses following progress on collections of overdue lease fees from some airlines resulting from the COVID-19 pandemic as well as the sale of aircraft. The number of self-owned aircraft was 45, while other aircraft (aircraft under management, etc.) totaled 57, both of which were basically flat, but the Company is expecting an increase in the number of self-owned aircraft throughout H2. In terms of activities, the Company achieved some results with respect to expanding transactions with U.S.-based airlines which are seeing a recovery in passenger demand mainly for domestic routes, and contributing* to the promotion of decarbonization in the airline industry.

* Concluded a Japanese Operating Lease contract with sustainability linked loan (SLL) linked to the decarbonization target for the A350, a large passenger aircraft to be introduced by France-based Compagnie Nationale Air France (Air France).

5. Summary of H1 FY3/23

To summarize H1 FY3/23 from the above, the Company achieved steady growth in the business areas it is focusing on, and realized balanced profit growth. In terms of activities, the Company is laying the groundwork in all directions towards achieving the medium-term management plan, and we can evaluate the Company as having gotten off to a good start, in both the quantitative and qualitative sense. In particular, based on collaboration with partner companies both in Japan and overseas, new developments have accelerated in growth fields including mobility, energy & environment, and BPO/ICT. These can be said to be points to focus on as the Company works to move away from "nontraditional leasing" and "non-financial services."

Business outlook

For FY3/23, the Company expects profits to continue to increase, unchanged from initial forecast

1. FY3/23 results outlook

For the results in FY3/23, the Company has not changed its initial forecast and expects total revenues to increase 6.4% YoY to ¥700.0bn, and profits are expected to increase with operating profit to increase 11.9% to ¥51.5bn, ordinary profit to rise 6.2% to ¥56.0bn, and profit attributable to owners of parent to grow 6.2% to ¥36.0bn.

The accumulation of operating assets, centered on the real estate and energy & environment fields that continue to perform well, recovery in aircraft, and the growth of BPO/ICT, including the effects of the collaboration with WorkVision (an increase in non-asset earnings) are expected to contribute to the increase in profits. The Company plans to further improve ROA as well through asset control that prioritizes profitability and the growth of non-asset earnings.

FY3/23 outlook

(¥bn)

	FY3/22		FY3/23			
	Results	% of revenues	Forecasts	% of revenues	Amount	YoY change
Total revenue	657.8	-	700.0	-	42.1	6.4%
Operating profit	46.0	7.0%	51.5	7.4%	5.4	11.9%
Ordinary profit	52.7	8.0%	56.0	8.0%	3.2	6.2%
Profit attributable to owners of parent	33.9	5.2%	36.0	5.1%	2.1	6.2%

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

2. Primary focus of FISCO's analysts

At FISCO, we consider it fully possible that the Company will achieve its results forecast based on the fact that H1 results made progress at a fast pace and because the Company is accumulating highly-profitable assets. Of course, attention must be paid to the external environment, with uncertainty regarding the future, including the impacts of the global semiconductor shortage, advancing inflation, and rising interest rates, but for the Company, which is realizing balanced profit growth in multiple growth fields, we can expect an appropriate amount of diversification effect and thus we feel downside risk can be viewed as being limited. Points to focus attention on will be the initiatives taken and the progress towards achieving the financial targets and non-financial targets laid out in the medium-term management plan. In particular, over both the short term as well as the medium to long term, we will closely follow the Company's initiatives aimed at resolving social issues, as well as watch how the Company advances personnel investment and its DX strategy to link these to its own sustainable value creation.

Growth strategy

Aims at achieving sustainable growth by "resolving social issues" while at the same time delivering "economic value"

1. Direction of the medium-term management plan

The Company started a new five-year medium-term management plan in FY3/23. Under the vision of "Fuyo Shared Value 2026," the direction the Company is aiming for is achieving sustainable growth by "resolving social issues" through human growth and dialog while at the same time delivering "economic value." It sets both financial and non-financial items for the management targets.

(1) Growth drivers

As the axes for the strategic fields (and new domains) up to the present time, the growth drivers have been categorized into three types; 1) the RT field that is aiming for strategic growth enabled by capturing tectonic social changes, 2) the AT field that is aiming for accelerating growth based on an understanding of market trends, and 3) the GP field that is aiming for the stable growth of the core fields. Then, the strategy is to improve profitability through concentrated investment of management resources into the RT and AT fields where market expansion and creation are expected and also through differentiation in the GP field. It has positioned mobility and circular economy in the RT field; energy & environment, BPO/ICT, and medical social welfare in the AT field; and real estate and aircraft in the GP field.

(2) Image of the allocation of resources and the earnings portfolio

The Company is concentrating investment of approximately ¥1tn (five-year cumulative total) into the RT and AT fields, which are growth areas, and it will improve ROA at the same time as accumulating operating assets. Also, in the GP field, which is a core field, its policy is to improve profitability that will lead to the improvement of ROA as a whole. In the next five years, operating assets are forecast to be around the ¥3tn level (an increase of around ¥0.5tn compared to FY3/22). Within this amount, operating assets in the RT and AT fields are expected to double, from ¥400.0bn to ¥800.0bn, alongside the replacements of assets. It is also targeting ordinary profit of ¥75.0bn in five years' time, and looking at the percentages for this, the percentage from the RT field will increase from 6% to 9% and from the AT field will increase greatly from 13% to 24%, while the GP field will be basically unchanged, from 41% to 40%. Conversely, the conventional general leasing and financing field will decline greatly, from 40% to 27%, and clearly there is a trend in progress of escaping from "nontraditional leasing" and "non-financial services."

(3) Management targets

As the business strategy's results targets through the three growth drivers, the Company has set both financial targets and non-financial targets and is aiming to simultaneously realize "corporate value" and "social value." The 4 financial targets are ordinary profit of ¥75.0bn, ROA of 2.5%, an equity ratio of 13% to 15%, and ROE of at least 10%. So, it will further improve profitability while maintaining a balance with a certain level of financial discipline and capital efficiency. Conversely, it has set the non-financial targets to be tackled from three perspectives – 1) the environment, 2) society and people, and 3) human resources investment – and its policy is for the Company itself to sustainably improve its enterprise value through "resolving social issues," such as by realizing a decarbonized society and a recycling-based society. Also, for measures to address climate change, it continues to work on achieving carbon neutrality and RE 100* toward the 2030 targets.

* An international consortium of companies that aim to procure 100% of the energy used in their operations from renewable energy.

Financial targets

(¥bn)

	FY3/22 Results		FY3/27 Target		Change	
		% of revenues		% of revenues		CAGR
Ordinary profit (¥bn)	52.7		75.0		22.3	7.3%
RT and AT	10.0	19.0%	25.0	33.3%	15.0	20.1%
GT	21.7	41.2%	30.0	40.0%	8.3	6.7%
General lease & financing	21.0	39.8%	20.0	26.7%	-1.0	-1.0%
ROA	2.06%		2.5		+0.44pt	
Equity ratio	11.3%		13%~15%		+1.7pt~3.7pt	
ROE	10.6%		10% or more		-	
Operating assets (Imagined)	¥2.5tn		¥3.0tn		¥0.5tn	
RT and AT	¥0.4tn		¥0.8tn		¥0.3tn	
GP	¥1.1tn		¥1.3tn		¥0.2tn	
General lease & financing	¥1.0tn		¥0.9tn		-¥0.1tn	

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

Non-financial targets (excerpt)

		FY3/27 Target
Environment	Decarbonized society	
	CO_2 reduction targets	500,000 t-CO_2/year
	Amount of investment to progress decarbonization	¥300.0bn
	Renewable energy power output	1,000MW
	Ratio of EV and FCV vehicles to number of vehicles owned	30%
	Recycling-based society	
	Reuse and recycling rate of returned equipment	100%
	Waste plastic materials/chemicals recycling rate	100%
Society and people	Customers' work reduction time	Over 1 million hours (compared to FY3/22)
Human resources investment	Human resources development-related expenses (standalone)	300% (compared to FY3/22)

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

2. The basic strategies and targets in each business field

(1) Mobility (RT field)

On the one hand, needs are growing for EV and FCV toward realizing carbon neutrality, but on the other hand, in the logistics industry environment, social issues are becoming increasing severe, such as the shortage of drivers and the long working hours. Based on this situation, the Company's strategy is to develop both domestically and overseas one-stop services centered on partner collaborations, mainly in the vehicle and logistics areas. In particular, in the vehicle area, it plans to build new business models, such as an EV one-stop service*1, and to expand the non-asset business, focused on fleet BPO*2. In the logistics area also, it is creating collaborative projects through its collaboration with the YAMATO Group, strengthening the global mobility business through collaborations with overseas Group companies, and working to strengthen truck financing and to expand into peripheral areas, mainly through YAMATO LEASE. The financial targets are ordinary profit of ¥7.0bn (FY3/22 up¥3.7bn) and ROA of 2.5% (up0.6%), while the non-financial targets include an EV and FCV ownership ratio of 30% (up30%).

*1 Through collaborations with partner companies, it will provide a one-stop service, from EV introduction review and consulting through to charger installation consulting and construction, financing and vehicle management, and energy management. This service is also highly compatible with energy & environment, which is one of the Company's strengths.
*2 Support for improving business efficiency, such as labor saving, through telematics services and optimization consulting for the vehicle mobilization rate.

(2) Circular economy (RT field)

Motivation toward realizing a recycling-based society is increasing, and within this situation is hidden the major possibility of building an infrastructure that can utilize scale merits and expansive networks even for lease companies with large-scale assets. The Company is progressing advanced measures for markets that are expected to grow, and its strategy is to aim to build a sophisticated circular economy platform. At the current time it has not set any financial targets, but its non-financial targets are 1) a returned equipment reuse and recycling rate of 100% (same as in FY3/22) and 2) a waste plastic materials / chemicals recycling rate of 100% (up100%).

(3) Energy & environment

The Company's strategy is to expand the renewable energy business on a global scale and to establish a new business in the secondary energy field. Renewable energy is not limited in terms of energy type or initiative form, and domestically and overseas the business scale will grow to 3 times its former scale. It will also accelerate joint investments with partner companies (major energy businesses, etc.) and continue to focus on the PPA business as a tool for customers' decarbonization. On the other hand, for secondary energy, it continues to work on measures for the LCM business (primary use → recycling of reuse, etc.) in the storage battery field and also with a view to participating in the power demand-supply adjustment market* that is steadily growing. The financial targets are ordinary profit of ¥5.0bn (FY3/22 up¥3.4bn) and ROA of 2.0% (up0.2%), while the non-financial targets are 1) a renewable energy power output of 1,000MWdc (up682MWdc) and 2) investment in decarbonization of ¥300.0bn (five-year cumulative total).

* The domestic market for power demand and supply adjustments was launched in April 2021. It is a framework designed to facilitate the trading of electric power needed to adjust the supply and demand of electricity at power plants and other facilities (adjustment capacity) in a nationwide integrated market.

(4) BPO/ICT

Against the backdrop of the labor shortage that is becoming increasingly serious and the workstyle reforms, measures to improve productivity, including DX and reviews of non-core operations, are accelerating. In this situation, the Company's strategy is to aim to provide BPS (business process services) that support customers in realizing their business reforms from both the aspects of operations and systems. Specifically, through a synergistic collaboration between BPO (business consulting + solutions) and ICT (systems consulting + IT solutions), it is providing total solutions through work outsourcing and DX. The financial targets are ordinary profit of ¥8.5bn (FY3/22 up ¥5.1bn) and ROA of 5.4% (up3.9%), while the non-financial targets are to reduce customers' work hours by an additional 1mn (up 1mn hours).

(5) Medical/social welfare

In addition to management issues such as the decrease in medical revenue, the labor shortage, and the lack of successors, needs for medical and social welfare are expected to further increase and become more sophisticated due to the 2025 problem*. In this situation, the Company's strategy is to maximize the value of businesses' management resources in the medical and social welfare markets, including for medical, nursing care, and dispensing pharmacy businesses, by continuing to provide one-stop services based on the Fuyo Lease Platform Concept. The financial targets are ordinary profit of ¥4.5bn (up ¥2.7bn compared to FY3/22) and ROA of 3.3% (up1.3%), while the non-financial targets are 1) 1,000 rooms in nursing care facilities for the elderly, and 2) financing of ¥56.0bn to support management in the medical and social welfare markets (up¥32.7bn compared to FY3/22).

* Japan has become a "super-aging society" and its social structure and systems are approaching a major turning point that is expected to have an impact on various fields, including employment, medical care, and welfare.

(6) Real estate

The Company is focusing on increasing the sophistication of and differentiating this business, and its strategy is to aim to stably grow profits through improving profitability. In particular, while conditions in the real estate market are active, particularly in the metropolitan areas, there is a sense that the competitive environment is overheating, and in this situation, it intends to further improve profitability and steadily expand the business by strengthening collaborations with partners and even further deepening the business areas. Moreover, toward the realization of a decarbonized society, it is progressing measures targeting environmentally friendly real estate*. The financial targets are ordinary profit of ¥23.0bn (up ¥2.7bn from FY3/22) and ROA of 2.3% (unchanged YoY) (it has not set non-financial targets).

* Green buildings, such as buildings with CASBEE evaluation certification or with environment-friendly facilities installed (energy saving, solar panels, etc.)

(7) Aircraft

It is anticipated that the business environment will gradually recover, and based on this, the Company is aiming to steadily grow profits through escaping from the effects of the COVID-19 pandemic and progressing the asset turnover business. At the same time, it plans to convert from a business model that assumes long-term holdings of aircraft to an asset turnover-type business model of flexibly selling aircraft based on the market environment and other factors. Conversely, it plans to enhance the earnings structure by accumulating excellent assets through strengthening competitiveness. It is also progressing measures for new technological fields that will contribute to “resolving social issues,” such as sustainable aircraft fuel (SAF). Its financial targets are ordinary profit of ¥7.0bn (up ¥5.5bn from FY3/22) and ROA of 2.4% (up1.7%) (it has not set non-financial targets).

3. Primary focus of FISCO’s analysts

At FISCO, we think that as the business environment continues to undergo significant change, it makes sense for the Company to aim to create new value through alliances with partners in high-growth fields that are also highly-compatible with domains that the Company has built up its business in over the years. In particular, one key point will be how the Company links its initiatives aimed at “resolving social issues,” including tackling climate change in which it has been the industry leader, to growth opportunities. The medium-term management plan has just begun, and although no rapid changes to the earnings structure are expected, we shall be focusing on what ways the Company strengthens the RT and AT fields that will be the growth drivers towards evolving the earnings portfolio into the portfolio that it is aiming for. Also, with respect to initiatives for “resolving social issues,” we will follow the progress on KPI set as non-financial targets, and also pay close attention from a medium- to long-term perspective on the path the Company takes in terms of how it will link those KPI to creating new markets, strengthening competitiveness, and building new business models and other initiatives, and thereby connect to economic value (profit growth, etc.).

Shareholder returns

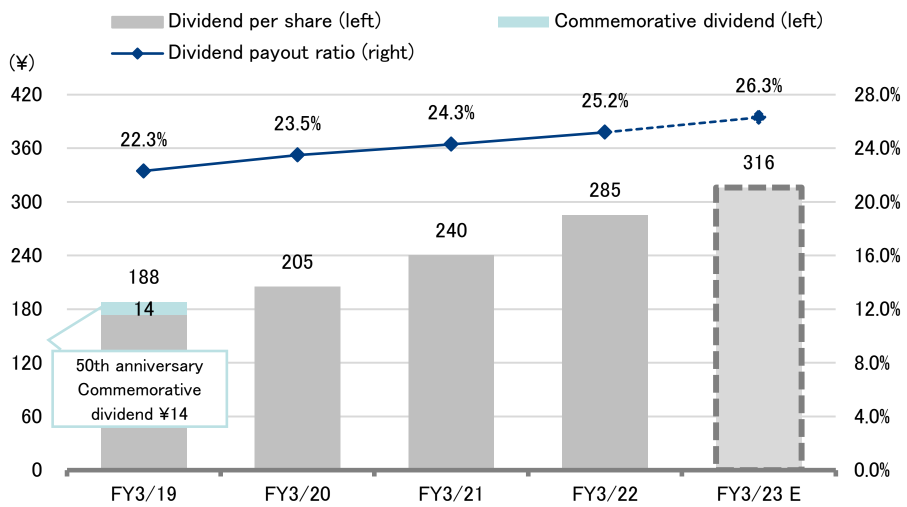
In FY3/23, is forecasting a dividend per share of ¥316, up ¥31 YoY. Is aiming to increase the dividend payout ratio to at least 30% by the final fiscal year of the medium-term management plan

The Company follows a fundamental policy of striving to return profits to shareholders by reinforcing shareholders' equity and continuing long-term, stable dividends to ensure a solid business foundation and robust financial position, taking into account its profits and business goals. Supported by strong profits, the Company has been continuously increasing its dividend since its shares were listed in 2004. Under the medium-term management plan, the Company has a policy of aiming for a dividend payout ratio of 30% or more by the final year of the plan.

For the FY3/23 annual dividend, it is forecasting a dividend per share of ¥316 (interim dividend of ¥158 and period-end dividend of ¥158), an increase of ¥31 YoY (forecast dividend payout ratio, 26.3%).

In addition to the higher dividend from profit growth, the Company has been gradually raising the dividend payout ratio, so at FISCO we think that there remains considerable room for the dividend to increase in the future due to both of these factors.

Dividend per share and dividend payout ratio



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

Disclaimer

FISCO Ltd. ("FISCO") offer stock price and index information for use under the approval of the Tokyo Stock Exchange, the Osaka Stock Exchange and Nikkei Inc.

This report is provided solely for the purpose of offering information, and is not a solicitation of investment nor any other act or action.

FISCO prepared and published this report based on information which it considered reliable; however, FISCO does not warrant the accuracy, completeness, fitness nor reliability of the contents of this report or the said information.

The issuers' securities, currencies, commodities, securities and other financial instruments mentioned in this report may increase or decrease in value or lose their value due to influence from corporate activities, economic policies, world affairs and other factors. This report does not make any promises regarding any future outcomes. If you use this report or any information mentioned herein, regardless of the purpose therefor, such use shall be made based on your judgment and responsibility, and FISCO shall not be liable for any damage incurred by you as a result of such use, irrespective of the reason.

This report has been prepared at the request of the company subject hereto based on the provision of information by such company through telephone interviews and the like. However, the hypotheses, conclusions and all other contents contained herein are based on analysis by FISCO. The contents of this report are as of the time of the preparation hereof, and are subject to change without notice. FISCO is not obligated to update this report.

FISCO and its affiliated companies, as well as the directors, officers and employees thereof, may currently or in the future trade or hold the financial instruments or the securities of issuers that are mentioned in this report.

Please use the information in this report upon accepting the above points.

■ For inquiry, please contact: ■
FISCO Ltd.
5-13-3 Minami Aoyama, Minato-ku, Tokyo, Japan 107-0062
Phone: 03-5774-2443 (IR Consulting Business Division)
Email: support@fisco.co.jp