COMPANY RESEARCH AND ANALYSIS REPORT

Sanki Engineering Co., Ltd.

1961

Tokyo Stock Exchange Prime Market

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Summary

FY3/22 saw YoY increases in both orders received and net sales, with operating profit increasing 21.5%

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

1. FY3/22 results: Increases (YoY) of 21.5% in operating profit

The Company reported FY3/22 results with ¥202,250mn in orders received (up 3.4% YoY), ¥193,189mn in net sales (up 1.6%), ¥9,112mn in operating profit (up 21.5%), ¥9,817mn in ordinary profit (up 19.8%), and ¥6,489mn in profit attributable to owners of parent (up 10.0%). Orders received were ¥202,250mn (up 3.4%), achieving the target (¥200,000mn). Although the increase in net sales was only slight, balance carried forward to the next period stayed at a high level at ¥150,737mn (up 6.4% YoY). The gross profit margin was 15.6%, gaining 0.5 of a percentage point due to continued rigorous unit cost management and reinforcement of frontline support operations. Selling, general and administrative (SG&A) expenses remained at ¥21,110mn, a decrease of just 0.7% despite increases in personnel expenses, etc., mainly due to the effects of other cost savings. As a result, operating profit increased 21.5% YoY.

2. FY3/23 results outlook: Operating profit is forecast to increase 4.2% YoY

For FY3/23, the Company is currently forecasting ¥200,000mn in orders received (down 1.1% YoY), ¥200,000mn in net sales (up 3.5%), ¥9,500mn in operating profit (up 4.2%), ¥10,000mn in ordinary profit (up 1.9%) and ¥6,900mn in profit attributable to owners of parent (up 6.3%). The forecast gross profit margin is 15.8% (up 0.2 pt), while SG&A expense are forecast to rise by 4.2%. The Company stated that it anticipates uncertain factors to continue, such as the impact of the COVID-19 pandemic and the increase in raw material costs, but with a brisk investment environment, it expects to meet its target through steady sales from existing projects.

3. "Century 2025" moves on to the Phase 3 medium-term management plan

The Company has announced "Century 2025" as its long-term vision for the 10-year period from FY3/17 to FY3/26, the 100th anniversary of its foundation. To achieve the targets of the vision, the Company has divided the 10-year period into three phases and promoted business strategies based on its medium-term management plans. From FY3/23, the Company entered the final Phase 3. The ultimate goal of the long-term vision (Phase 3 target), is to be "The Company of Choice." The Company's quantitative targets for the final year, FY3/26, are ¥220.0bn in net sales, gross profit margin of 16.5%, ¥12.0bn in ordinary profit, dividend payout ratio of 50% or higher, and ROE of 8.0% or above. These are by no means easy targets, but the important point is "how will the Company change qualitatively and quantitatively in order to achieve them?" The further changes made by the Company going forward will be important to monitor.

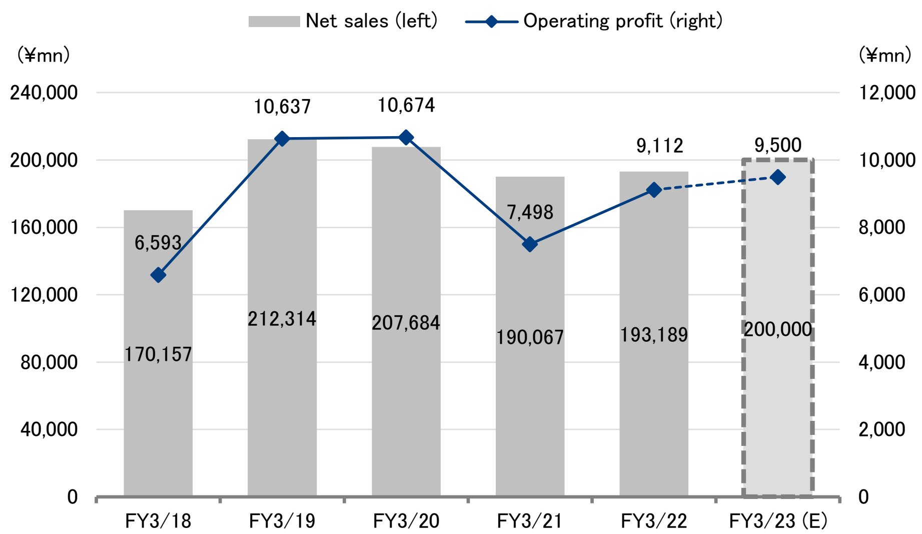
4. Actively returns profits to shareholders: Total return ratio (weighted average) for the last nine years is 87.1%

The Company has proactively conducted shareholder returns with stable dividends up to now, dividend hikes in recent years, and acquisition of treasury stock. The annual dividend (including extra dividends) was ¥80 in FY3/21 and ¥85 in FY3/22. In FY3/23 the Company plans to pay a dividend of ¥70. With regard to treasury stock, in FY3/20 the Company acquired 1,958,000 shares and retired 1,000,000 shares; and in FY3/21, it acquired a further 1,000,000 shares and retired the same number. In FY3/22, the Company acquired 1,000,000 shares of treasury stock. As a result, it expects to achieve a total return ratio (weighted average) for the past nine years of 87.1%. As such, we think the Company is deserving of high marks for its proactive shareholder return policy, rather than simply aiming to increase operating results.

Key Points

- A facilities construction company affiliated with Mitsui and a domestic leader. Is currently implementing measures to improve its profit margin
- In FY3/23, operating profit is forecast to increase 4.2% YoY. Has moved to the final stage of the medium-term management plan
- Actively returns profits to shareholders. Total return ratio (weighted average) for the last nine years is 87.1%

Results trends



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

Company outline

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

1. Company outline

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

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

2. History

Prior to the 90th anniversary of its establishment in FY3/16, the Company announced the "Century 2025" long-term vision headed toward its 100th anniversary in 2025. It completed Phase 1 in FY3/19, the first step, reaching initial targets. Furthermore, since April 2020, it has been promoting Phase 2 under Hirokazu Ishida as the new President, and in FY3/22, it has mainly achieved the targets. The Company has entered Phase 3, the final phase of "Century 2025," in FY3/23. The Company's activities going forward to its 100th anniversary in 2025 will be a focus point.

History

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

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

Business description

Three main segments, particularly strong in industrial HVAC

1. Outline of business by segment

The Company's main businesses come under three segments – Facilities Construction Business, Plants & Machinery Systems Business, and Real Estate Business. Its main activities are design and construction management of various facilities. The Company obtains about half of its orders directly from facility owner clients and half indirectly through general contractors.

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

An overview of each segment is set out below.

(1) Facilities Construction Business

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

a) HVAC and plumbing for buildings

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

b) Industrial HVAC

The industrial HVAC business provides HVAC for factories and research facilities of all industries, especially clean room systems for semiconductor plants and pharmaceutical and food processing plants, which are areas of strength for the Company, as well as special air-conditioning systems and appurtenances for manufacturers of medical equipment and the like, in addition to environmental control systems and so forth for automobile manufacturers. This is a particularly strong field for the Company, partly because of its historical background.

c) Electrical systems

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

d) Facility systems

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

(2) Plants & Machinery Systems Business

The Plants & Machinery Systems Business encompasses machinery systems and environmental systems as two sub-segments.

a) Machinery systems

The machinery systems business supplies materials handling systems, including various transportation equipment (conveyors, sorting systems, etc.), and conveyance systems for factories and automated warehouses. Demand is centered on private-sector companies and is affected by capital investment trends.

b) Environmental systems

The environmental systems business provides facilities such as for water treatment (including water and sewage treatment and disposal, industrial wastewater disposal, and sludge treatment and incineration), waste treatment (including waste incineration and landfill wastewater treatment), and others. Customers are mainly local government entities and so forth.

(3) Real Estate Business

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

2. Strengths, distinguishing traits, and competitors

(1) Broad business domain and one-stop solutions

Many companies in Japan provide similar facilities construction services, but the Company's strength lies in the wide range of its businesses, which includes HVAC for building, plumbing, industrial HVAC, electrical systems, facility systems, automated control systems for buildings, transportation systems, and water treatment facilities. The Company can provide services for many types of facilities and solutions covering all phases from planning and design to installation, maintenance, repair, and replacement, depending on the life cycle of the building. This capability allows its customers to place one-stop orders to resolve their problems. Making use of "total engineering" and "life-cycle engineering," which combines a wide variety of businesses horizontally, enables the Company to provide optimal systems with high added value, which is its notable feature and the Company's strength.

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

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

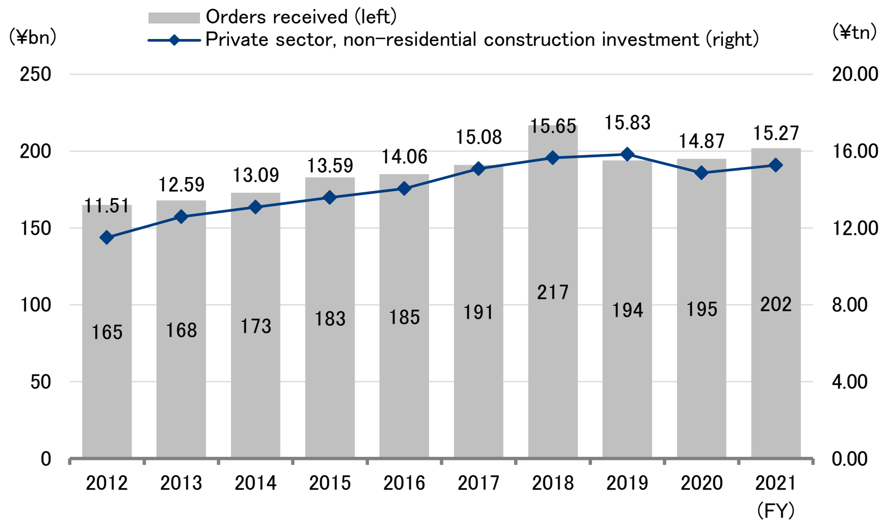
3. Main competitors

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

4. Trend in orders received and the economic environment

Orders received is the most important factor affecting results. Annual orders received are thought to be greatly affected by the Company's sales efforts, as well as the overall Japanese market, or the Japanese macro-economy. As the Company's main business is facilities construction, it is influenced by the macro indicator of private sector, non-residential construction investment. The correlation between orders received and private sector, non-residential construction investment is arguably very high.

Net sales versus private sector, non-residential construction



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

Business trends

Increases of 1.6% in net sales and 21.5% in operating profit in FY3/22, balance carried forward to the next period holding at a high level of ¥150.7bn

1. FY3/22 results overview

(1) Earnings

The Company reported FY3/22 results with ¥193,189mn in net sales (up 1.6% YoY), ¥9,112mn in operating profit (up 21.5%), ¥9,817mn in ordinary profit (up 19.8%), and ¥6,489mn in profit attributable to owners of parent (up 10.0%). Orders received were ¥202,250mn (up 3.4%), achieving the plan. Balance carried forward to the next period stayed at a high level at ¥150,737mn (up 6.4% YoY).

Net sales posted an overall increase year on year, as the completion of a large project in HVAC and plumbing for buildings absorbed a decline in industrial HVAC due to difficult comparisons with the previous year. Favorable progress in environmental systems projects also contributed. Orders received saw healthy trends in industrial HVAC and electrical systems, along with solid momentum in machinery systems and environmental systems, despite a decrease in orders in HVAC and plumbing for buildings after a large-scale deal in the previous fiscal year.

In earnings, the gross profit margin increased 0.5 percentage points YoY to 15.6% as a result of booking sales for large-scale projects with robust profitability. The margin improved due to continued rigorous unit cost management and reinforcement of frontline support operations. It is commendable that the Company has maintained the gross profit margin at a high level (15% level).

Conversely, SG&A expenses were ¥21,110mn (down 0.7% YoY). Higher personnel costs were outweighed by a decrease in expenses due to the non-recurrence of costs for office relocation and COVID-19 measures from the previous fiscal year, along with efforts to reduce all kinds of expenses. This resulted in a significant YoY increase in operating profit. The growth rate of profit attributable to owners of parent only rose 10.0% YoY because of factors including the tax effect in the previous fiscal year, and was lower than the growth rate for ordinary profit, which was 19.8%.

FY3/22 results

(¥mn)

	FY3/21		FY3/22		YoY	
	Amount	Ratio	Amount	Ratio	YoY change	Change %
Orders received	195,580	-	202,250	-	6,670	3.4%
Balance carried forward	141,676	-	150,737	-	9,061	6.4%
Net sales	190,067	100.0%	193,189	100.0%	3,121	1.6%
Gross profit	28,754	15.1%	30,223	15.6%	1,469	5.1%
SG&A expenses	21,255	11.2%	21,110	10.9%	-144	-0.7%
Operating profit	7,498	3.9%	9,112	4.7%	1,614	21.5%
Ordinary profit	8,196	4.3%	9,817	5.1%	1,620	19.8%
Profit attributable to owners of parent	5,901	3.1%	6,489	3.4%	587	10.0%

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

(2) Earnings by segment

The Facilities Construction Business posted ¥155,484mn in net sales (down 0.0% YoY). In sub-segments, HVAC and plumbing for buildings posted ¥62,146mn (up 12.4%) in sales. Thanks to progress in existing large projects, the Company posted a double-digit increase sales. Industrial HVAC posted ¥57,363mn (down 10.6%) in sales, however, this was due to a decrease in projects carried forward from the previous period. Electrical systems posted sales of ¥24,933mn (down 0.0%), and facility systems maintained sales at the same level as in the previous year, at ¥11,040mn (down 0.7%).

Net sales in the Plants & Machinery Systems Business were ¥35,509mn (up 9.1% YoY). In sub-segments, machinery systems reported ¥9,666mn in sales (up 7.7%) with support from recovery in conveyor and other equipment sales. Environmental systems posted ¥25,842mn (up 9.7%) in sales mainly on progress in a major DBO* project booked as an order previously and the completion of large-scale projects involving industrial waste treatment plants. Additionally, Real Estate Business sales totaled ¥2,410mn (up 1.5%) and Others sales were at ¥566mn (down 30.5%).

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

The Company discloses gross profit and ordinary profit as segment profit indicators from FY3/20. Our report uses gross profit. In FY3/22, gross profit in the Facilities Construction Business increased to ¥24,409mn (up 5.0% YoY for an increase of ¥1,156mn). In the sub-segments, gross profit was ¥22,086mn (up 5.0%) in HVAC and plumbing for buildings, industrial HVAC, and electrical systems, and was ¥2,323mn (up 4.9%) in facility systems. Gross profit in the Plants & Machinery Systems Business was ¥5,133mn (up 8.5% for an increase of ¥401mn), which consisted of ¥1,586mn (up 1.9%) in machinery systems and ¥3,547mn (up 11.7%) in environmental systems. In the Real Estate Business and Others, gross profit was ¥876mn (up 1.1%) and ¥69mn (up 31.0%), respectively.

Net sales and gross profit by segment

(¥mn)

	FY3/21		FY3/22		YoY	
	Result	Ratio	Result	Ratio	YoY change	Change %
Net sales	190,067	100.0%	193,189	100.0%	3,121	1.6%
Facilities Construction Business	155,501	81.8%	155,484	80.5%	-17	-0.0%
HVAC and plumbing for buildings	55,293	29.1%	62,146	32.2%	6,852	12.4%
Industrial HVAC	64,152	33.8%	57,363	29.7%	-6,788	-10.6%
Electrical systems	24,941	13.1%	24,933	12.9%	-7	-0.0%
Facility systems	11,113	5.8%	11,040	5.7%	-73	-0.7%
Plants & Machinery Systems Business	32,533	17.1%	35,509	18.4%	2,976	9.1%
Machinery Systems Business	8,973	4.7%	9,666	5.0%	693	7.7%
Environmental Systems Business	23,560	12.4%	25,842	13.4%	2,282	9.7%
Real Estate Business	2,375	1.2%	2,410	1.2%	34	1.5%
Others	815	0.4%	566	0.3%	-248	-30.5%
Adjustments	-1,158	-	-781	-	376	-
Gross profit	28,754	15.1%	30,223	15.6%	1,469	5.1%
Facilities Construction Business	23,253	15.0%	24,409	15.7%	1,156	5.0%
Building HVAC, industrial HVAC, and electrical systems	21,038	14.6%	22,086	15.3%	1,048	5.0%
Facility systems	2,215	19.9%	2,323	21.0%	107	4.9%
Plants & Machinery Systems Business	4,732	14.5%	5,133	14.5%	401	8.5%
Machinery systems	1,556	17.3%	1,586	16.4%	29	1.9%
Environmental systems	3,176	13.5%	3,547	13.7%	371	11.7%
Real Estate Business	866	36.5%	876	36.3%	9	1.1%
Others	101	12.4%	69	12.2%	-31	-31.0%
Adjustments	-199	-	-266	-	-66	-

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

(3) Orders received by segment

The Facilities Construction Business booked orders received of ¥160,504mn (up 2.4% YoY). By subsegment, HVAC and plumbing for buildings booked ¥58,603mn in orders (down 10.4%), though this is a lull phase after two straight years of high results and not a concern. Industrial HVAC had ¥63,113mn in orders (up 6.5%). The Company explained that orders related to semiconductors and R&D areas in particular were robust. Electrical systems had a solid ¥27,856mn in orders (up 29.7%), reflecting the contribution from a large project for a datacenter. Facility systems posted ¥10,930mn in orders (up 2.3%). This can be considered a healthy level.

The Plants & Machinery Systems Business reported orders received of ¥39,554mn (up 8.2% YoY), a healthy result. Orders received for machinery systems appeared to be favorable at ¥8,914mn (up 13.4%) with particularly brisk activity in orders for logistics warehouses. Environmental systems had orders received of ¥30,640mn (up 6.7%). The result reflected a relatively large order received for maintenance and management at a subsidiary. As a result, together with the Facilities Construction Business, orders received for the facilities work segments overall reached ¥200,059mn (up 3.5%).

In areas other than facilities work segments, orders received in the Real Estate Business totaled ¥2,410mn (up 1.5% YoY), and in Others totaled ¥563mn (down 7.4%). Total orders received in FY3/22 (including adjusted amounts) was ¥202,250mn (up 3.4% YoY). Balance carried forward to the next period at the end of FY3/22 hence stayed at a high level at ¥150,737mn (up 6.4% YoY). While orders declined YoY in electric machinery, pharmaceutical industry, automobile, and other areas, orders increased YoY in machinery, chemicals, services, education, and other areas.

Orders for large-scale projects (orders exceeding ¥1,000mn) included 25 projects totaling ¥47,103mn. Both orders volume and value narrowed YoY, but average value per deal rose to ¥1,884mn (compared to ¥1,796mn in the previous year).

Orders received by segment

(¥mn)

	FY3/21		FY3/22		YoY	
	Result	Compared to orders received	Result	Compared to orders received	YoY change	Change %
Orders received	195,580	100.0%	202,250	100.0%	6,670	3.4%
Facilities Construction Business	156,768	80.2%	160,504	79.4%	3,736	2.4%
HVAC and plumbing for buildings	65,371	33.4%	58,603	29.0%	-6,767	-10.4%
Industrial HVAC	59,234	30.3%	63,113	31.2%	3,878	6.5%
Electrical systems	21,472	11.0%	27,856	13.8%	6,384	29.7%
Facility systems	10,690	5.5%	10,930	5.4%	240	2.3%
Plants & Machinery Systems Business	36,569	18.7%	39,544	19.6%	2,985	8.2%
Machinery Systems Business	7,858	4.0%	8,914	4.4%	1,055	13.4%
Environmental Systems Business	28,710	14.7%	30,640	15.1%	1,929	6.7%
Real Estate Business	2,375	1.2%	2,410	1.2%	34	1.5%
Others	609	0.3%	563	0.3%	-45	-7.4%
Adjustments	-742	-	-782	-	-	-

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

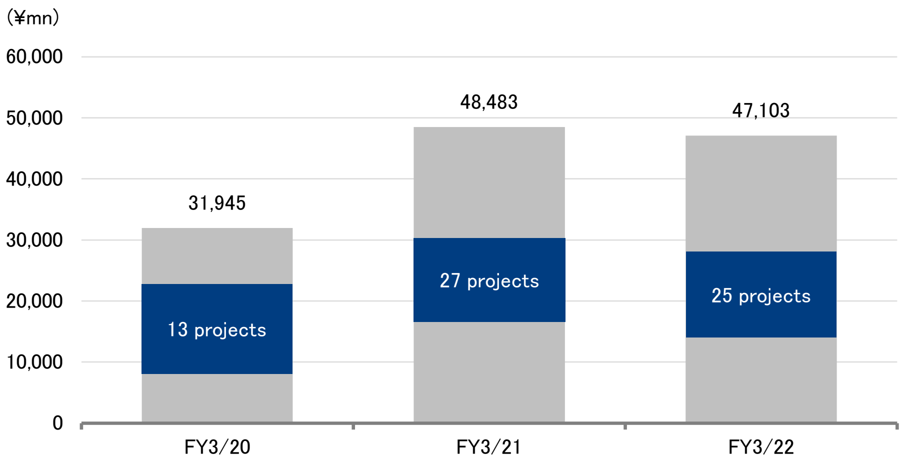
Breakdown of large-scale projects with orders exceeding ¥1,000mn

(projects)

	FY3/20	FY3/21	FY3/22
Offices	1	4	3
Multipurpose building	-	-	1
Factories	3	6	7
Stores	-	-	1
Hospitals and clinics	1	3	1
Research institutes	2	3	2
General government buildings	1	-	-
Public halls and cultural centers	-	-	1
Other building interiors	2	3	5
Railways and airports	-	1	-
Power plants and substations	1	-	-
School buildings and auditoriums	-	1	-
Waste processing facilities	1	1	2
Water and sewage treatment plants	1	5	2
Total (projects)	13	27	25
Total (¥mn)	31,945	48,483	47,103

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

Large-scale projects with orders exceeding ¥1,000mn



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

2. Financial condition

Looking at financial conditions at the end of FY3/22, current assets totaled ¥125,742mn (up ¥9,688mn compared to the end of FY3/21). This was mainly due to increases of ¥6,692mn in cash and deposits, decrease of ¥5,323mn in sales receivables (notes and accounts receivable, electronic record claims, notes and accounts receivable on completed construction contracts and other and contract assets), and a ¥3,000mn increase in securities. Noncurrent assets were ¥57,866mn (up ¥2,608mn), which was primarily because of an increase of ¥2,758mn in investments and other assets from buying low-risk securities. As a result, total assets at the end of FY3/22 were ¥183,609mn (up ¥12,296mn).

Current liabilities were ¥79,210mn (up ¥11,328mn compared to the end of FY3/21). This was mainly due to increases of ¥55,274mn in accounts payable (accounts payable on construction contracts, including electronic record liabilities). Noncurrent liabilities were ¥10,121mn (down ¥1,610mn), with the main factors including a decrease of ¥3,140mn in long-term loans payable and increases of ¥871mn in liability for retirement benefits and ¥385mn in deferred tax liabilities. As a result, total liabilities at the end of FY3/22 were ¥89,331mn (up ¥9,717mn). Total net assets totaled ¥94,278mn (up ¥2,579mn), mainly due to an increase of ¥1,939mn in retained earnings, ¥1,384mn in acquisition of treasury stock, and an increase of ¥1,263mn in unrealized gains on securities.

Balance sheet

(¥mn)

	End of FY3/21	End of FY3/22	YoY change
Cash and deposits	36,087	42,779	6,692
Notes and accounts receivable on completed construction contracts and other, contract assets, and electronic record claims	72,085	66,761	-5,323
Current assets	116,054	125,742	9,688
Tangible noncurrent assets	13,972	13,504	-468
Intangible noncurrent assets	937	1,255	318
Investments and other assets	40,348	43,106	2,758
Noncurrent assets	55,258	57,866	2,608
Total assets	171,313	183,609	12,296
Accounts payable on construction contracts, electronic record liabilities	41,709	40,520	-1,189
Short-term loans payable	7,135	8,885	1,750
Advances received on uncompleted construction contracts	8,580	-	-8,580
Contract liabilities	-	14,754	14,754
Current liabilities	67,882	79,210	11,328
Long-term loans payable	3,460	320	-3,140
Liability for retirement benefits	1,710	2,581	871
Noncurrent liabilities	11,731	10,121	-1,610
Total liabilities	79,614	89,331	9,717
Total net assets	91,699	94,278	2,579

Note: In FY3/22, the Company recorded current assets of ¥4,300mn and current liabilities of ¥4,300mn due to a change in "Accounting Standard for Revenue Recognition."
Source: Prepared by FISCO from the Company's financial results and Summary of Financial Results

3. Cash flow conditions

In FY3/22, net cash provided by operating activities was ¥18,529mn. The main inflows were the recording of profit before income taxes of ¥9,514mn, depreciation and amortization of ¥1,587mn, and a decrease of ¥5,389mn in notes and accounts receivable on completed construction contracts. The main outflows included decreases of ¥1,218mn in notes and accounts payable on construction contracts and other and ¥2,080mn in other current liabilities. Net cash used in investing activities was ¥3,384mn. The main outflows were ¥1,010mn in purchase of property, plant and equipment and ¥19,000mn in acquisition of securities (net basis). Net cash used in financing activities was ¥7,518mn. The main outflows were ¥1,390mn in long-term loans payable, ¥1,438mn in treasury stock acquisition, and ¥4,537mn in cash dividends paid.

Cash and cash equivalents hence increased ¥7,692mn in FY3/22 to a period-end balance of ¥44,779mn.

Statement of cash flows

(¥mn)

	FY3/21	FY3/22
Cash flows from operating activities	-483	18,529
Profit before income taxes	7,797	9,514
Depreciation and amortization	1,700	1,587
Change in notes and accounts receivable on completed construction contracts and other (- indicates increase)	4,770	5,389
Change in notes and accounts payable on construction contracts and other (- indicates decrease)	-10,777	-1,218
Cash flows from investment activities	-1,423	-3,384
Purchase of securities	-1,700	-1,900
Purchase of property, plant and equipment	-1,494	-1,010
Cash flows from financing activities	-6,974	-7,518
Change in short- and long-term loans payable (- indicates decrease)	-125	-1,390
Outlays for acquisition of treasury stock	-1,171	-1,438
Cash dividends paid	-5,474	-4,537
Change in cash and cash equivalents (- indicates decrease)	-8,859	7,692
Cash and cash equivalents at end of period	37,087	44,779

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

Outlook

In FY3/23, operating profit is forecast to increase 4.2% YoY

For FY3/23, the Company is currently forecasting ¥200,000mn in orders received (down 1.1% YoY), ¥200,000mn in net sales (up 3.5%), ¥9,500mn in operating profit (up 4.2%), ¥10,000mn in ordinary profit (up 1.9%) and ¥6,900mn in profit attributable to owners of parent (up 6.3%). The forecast gross profit margin is 15.8% (up 0.2 pt), while SG&A expenses are forecast to rise year on year by 4.2%. The Company stated that it anticipates uncertain factors to continue, such as the impact of the COVID-19 pandemic and the increase in raw material costs, but with a brisk investment environment, it expects to meet its target through steady sales from existing projects.

Breaking down net sales, the Facilities Construction Business is expected to provide ¥160,000mn (up 2.9% YoY) with sub-segment forecasts of ¥59,000mn in HVAC and plumbing for buildings (down 5.1%), ¥63,000mn in industrial HVAC (up 9.8%), ¥27,000mn in electrical systems (up 8.3%), and ¥11,000mn in facility systems (up 0.4%). The Company projects ¥38,000mn in net sales in the Plants & Machinery Systems Business (up 7.0% YoY) with sub-segment forecasts of ¥12,000mn in machinery systems (up 24.1%) and ¥26,000mn in environmental systems (up 0.6%).

In the mainstay Facilities Construction Business, orders received are expected to increase to ¥165,000mn (up 2.8% YoY). Sub-segment forecasts are for ¥63,000mn in HVAC and plumbing for buildings (up 7.5%), ¥65,000mn in industrial HVAC (up 3.0%), ¥26,000mn in electrical systems (down 6.7%), partly reflecting a fallback from a large project in FY3/22, and ¥11,000mn in facility systems (up 0.6%). The Company expects ¥33,000mn in orders in the Plants & Machinery Systems Business (down 16.5% YoY). Sub-segment forecasts are for ¥13,000mn in machinery systems (up 45.8%), while environmental systems are forecasting orders received for ¥20,000mn (down 34.7%), reflecting the high level of orders over the past two years. As a result, overall orders received, including the Real Estate Business, is expected to be ¥200,000mn (down 1.1%)

The Company is forecasting gross profit of ¥31,500mn (up 4.2% YoY), and a gross profit margin of 15.8%. SG&A expenses are expected to be ¥22,000mn (up 4.2%), mainly as a result of increases in personnel expenses. As a result, operating profit is forecast to be ¥9,500mn, an increase of 4.2% YoY.

FY3/23 forecast

(¥mn)

	FY3/22		FY3/22 (E)			
	Result	Component ratio	Amount	Component ratio	YoY change	Change %
Orders received	202,250	100.0%	200,000	100.0%	-2,250	-1.1%
Facilities Construction Business	160,504	79.4%	165,000	82.5%	4,496	2.8%
HVAC and plumbing for buildings	58,603	29.0%	63,000	31.5%	4,397	7.5%
Industrial HVAC	63,113	31.2%	65,000	32.5%	1,887	3.0%
Electrical systems	27,856	13.8%	26,000	13.0%	-1,856	-6.7%
Facility systems	10,930	5.4%	11,000	5.5%	70	0.6%
Plants & Machinery Systems Business	39,544	19.6%	33,000	16.5%	-6,544	-16.5%
Machinery systems	8,914	4.4%	13,000	6.5%	4,086	45.8%
Environmental systems	30,640	15.1%	20,000	10.0%	-10,640	-34.7%
Real Estate Business	2,410	1.2%	2,400	1.2%	-10	-0.4%
Others	563	0.3%	500	0.3%	-63	-11.2%
Net sales	193,189	100.0%	200,000	100.0%	6,811	3.5%
Facilities Construction Business	155,484	80.5%	160,000	80.0%	4,516	2.9%
HVAC and plumbing for buildings	62,146	32.2%	59,000	29.5%	-3,146	-5.1%
Industrial HVAC	57,363	29.7%	63,000	31.5%	5,637	9.8%
Electrical systems	24,933	12.9%	27,000	13.5%	2,067	8.3%
Facility systems	11,040	5.7%	11,000	5.5%	-40	-0.4%
Plants & Machinery Systems Business	35,509	18.4%	38,000	19.0%	2,491	7.0%
Machinery systems	9,666	5.0%	12,000	6.0%	2,334	24.1%
Environmental systems	25,842	13.4%	26,000	13.0%	158	0.6%
Real Estate Business	2,410	1.2%	2,400	1.2%	-10	-0.4%
Others	566	0.3%	500	0.3%	-66	-11.7%
Adjustments	-781	-	-900	-	-119	-
Gross profit	30,223	15.6%	31,500	15.8%	1,277	4.2%
Operating profit	9,112	4.7%	9,500	4.8%	388	4.2%
Ordinary profit	9,817	5.1%	10,000	5.0%	183	1.9%
Profit attributable to owners of parent	6,489	3.4%	6,900	3.5%	411	6.3%

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

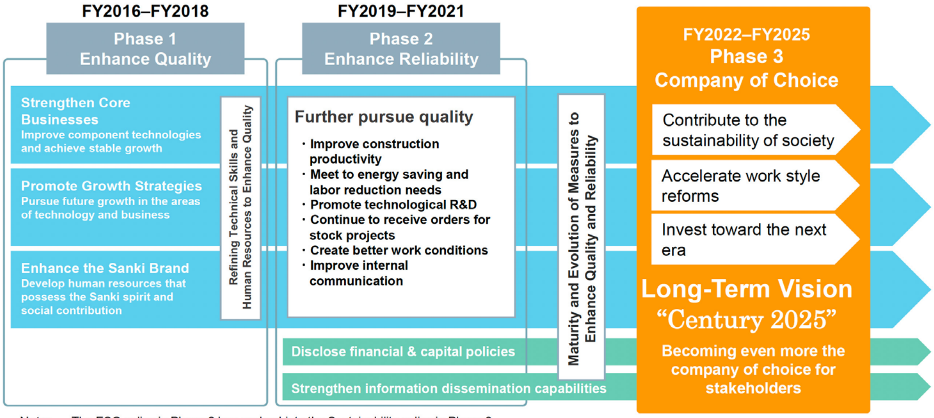
Medium-term management plan

Now entering "Century 2025" Phase 3

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

In March 2016, the Company announced the long-term vision "Century 2025," which covers the 10-year period until the 100th anniversary of its establishment. The first three years of this plan (FY3/17 to FY3/19) are Phase 1, the next three years (FY3/20 to FY3/22) are Phase 2, and the final four years (FY3/23 to FY3/26) are Phase 3. In each phase, the company has set various qualitative and quantitative goals, and it has mainly achieved these up to the completed Phase 2. Now, the Company has entered Phase 3, starting from FY3/23, which is the finishing phase of "Century 2025." The key strategies for Phase 3 are "contribute to the sustainability of society," "accelerate work style reforms," and "invest toward the next era," as the Company aims to be a "Company of Choice" for its stakeholders.

Long-term vision "Century 2025"



Note: The ESG policy in Phase 2 has evolved into the Sustainability policy in Phase 3

Source: Company's medium-term management plan materials

2. Summary of Phase 2

Phase 2 was completed in FY3/22. The Company mainly achieved its main quantitative goals. However, while some were achieved ahead of schedule, others remained unachieved in the final fiscal year, partly because of the impacts of COVID-19. The status of management targets was similar. While the Company did not achieve its targets for treasury stock acquisition and ROE, it achieved its targets for ordinary profit dividends, and total rate of return, among others. Considering the unprecedented global situation caused by the COVID-19 pandemic during this three-year period, these results show an extremely solid effort.

"Century 2025" Phase 2 targets and results

(¥bn)

	FY3/20		FY3/21		FY3/22	
	Target	Result	Target	Result	Target	Result
Net sales	200.0	207.6	200.0	190.0	200.0	193.1
Gross profit	30.0	32.1	31.0	28.7	32.0	30.2
Gross profit margin	15.0%	15.5%	15.5%	15.1%	16.0%	15.6%
Ordinary profit	9.0	11.2	9.5	8.1	10.0	9.8
Ordinary profit margin	4.5%	5.4%	4.8%	4.3%	5.0%	5.1%

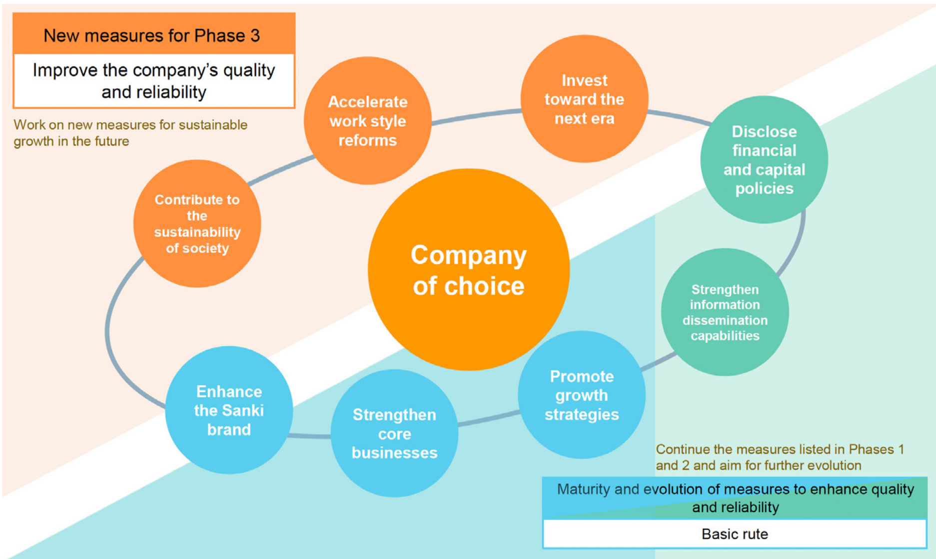
	FY3/20-FY3/22 Target	FY3/20 Result	FY3/21 Result	FY3/22 Result
Ordinary profit margin	5.0% or higher (final fiscal year)	5.4%	4.3%	5.1%
Annual dividend	¥60 per share	¥95	¥80	¥85
Acquisition of treasury stock	Approximately 5,000,000 shares	1,958,000 shares	1,000,000 shares (Cumulative total of 2,958,000 shares)	1,000,000 shares (Cumulative total of 3,958,000 shares)
Total return ratio	70% or above	111.4%	97.3%	95.7%
ROE	8.0% or higher (final fiscal year)	8.6%	6.6%	7.0%

Note: "Target" refers to the initial target values of the plan.
Source: Prepared by FISCO from the Company's Status of Business Progress in the Medium-Term Management Plan

3. Overview of Phase 3 basic policy and measures

Phase 3 is the finishing medium-term plan for the long-term vision "Century 2025." The basic policy of the plan is to further mature and evolve its existing strategies for increasing quality and reliability, adding the three new strategies of "contribute to the sustainability of society," "accelerate work style reforms," and "invest toward the next era," aiming to be the "Company of Choice." The Company will continue and further evolve the existing measures from Phase 1 and Phase 2, while executing the three new key measures for Phase 3.

Overview of Phase 3 measures



Source: Company's medium-term management plan materials

(1) Contribute to the sustainability of society

1) Promote the development of new technology to realize a carbon-free society
2) Reduce overall greenhouse gas emissions, including in the supply chain
3) Strengthen SANKI YOU Eco Contribution Points
4) Formulate and make use of a BCMS*1 to maintain an effective BCP*2

*1 BCMS: Business Continuity Management System
*2 BCP: Business Continuity Plan

(2) Accelerate work style reforms

The Company aims to realize the value of achievement, growth, self-actualization, contribution to social development, etc., and receive appropriate treatment based on respect for human rights.

1) Continuation of Smile Project led by top management
2) Reform of personnel system centered on active appointment of young people and extension of retirement age
3) Improve quality and productivity with DX and reduce working hours
4) Securing and training human resources in consideration of promoting diversity

(3) Invest toward the next era

Nurture the growth of new engineering businesses in these fields that society requires as we advance toward the future.

1) Fields
- Decarbonization technology (energy saving, energy creation,etc.)
- Automation and labor-saving technology (material handling)
- LCE business (stock business)
- DX

2) Measures
- Growth investment about ¥20bn
- External collaboration such as open innovation
- M&A

4. “Century 2025” Phase 3 results and management targets

The Company’s quantitative targets for the final year, FY3/26, are ¥220.0bn in net sales, gross profit margin of 16.5%, ¥12.0bn in ordinary profit, dividend payout ratio of 50% or higher, and ROE of 8.0% or above. These are by no means easy targets, but the important point is “how will the Company change qualitatively and quantitatively in order to achieve them?” The further changes made by the Company going forward will be important to monitor.

Phase 3 (FY3/26) results targets

(¥bn)

	FY3/26
Net sales	220.0
Gross profit	36.0
Gross profit margin	16.5%
Ordinary profit	12.0
Ordinary profit margin	5.5%

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

Phase 3 (FY3/26) management targets

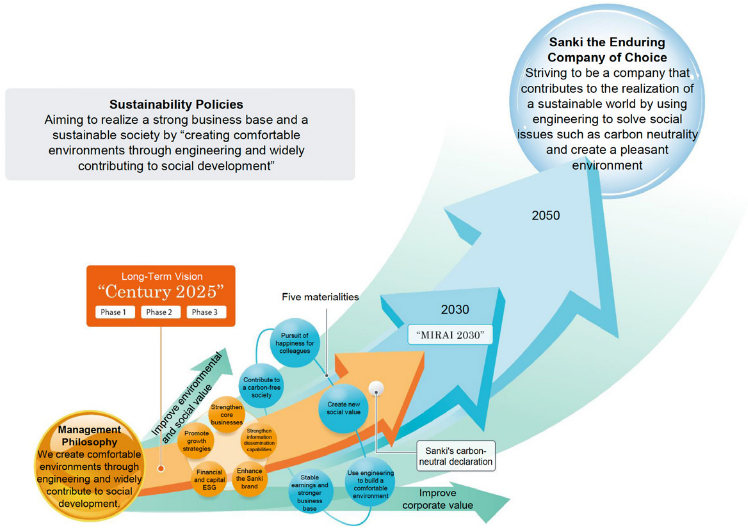
Ordinary profit margin	5.0% or above
Dividend policy	Dividend payout ratio of 50% or above Annual dividend of ¥70 or above per share
Acquisition of treasury stock	Approximately 5,000,000 shares*
ROE	8.0% or above
Growth investment	Approximately ¥20bn*

*Accumulative over the period of the plan
Source: Prepared by FISCO from the Company’s medium-term management plan materials

5. Vision for 2050 (Ultra long-term vision)

The Company has established a Vision for 2050 aligned with Phase 3 to respond to various social issues such as climate change while looking ahead to the future. Under the theme of “Sanki, ‘The Enduring Company of Choice,’” the Company aims to produce answers with engineering that creates comfortable environments and contribute to the realization of a sustainable world, including working to achieve carbon neutrality.

Promotion of the sustainability management



Source: Company's medium-term management plan materials

Shareholder return policy

Proactive stance toward shareholder returns with dividend hikes and acquisition and retirement of treasury stock. Total return ratio (weighted average) for the past 9 years of 87.1%

The Company actively returns profits to shareholders. While its basic annual dividend was ¥15 through FY3/14, a change in profit structure prompted a dividend increase beginning in FY3/15. Recently, in FY3/20, the Company had an initial annual dividend target of at least ¥60 and raised the dividend to ¥95 (¥35 interim, ¥60 year-end) including a ¥25 extra dividend to reflect robust earnings. In FY3/21, it paid an annual dividend of ¥80, comprised of a regular dividend of ¥70 and an extra dividend of ¥10. In FY3/22, it paid a regular dividend of ¥85 (including an extra dividend of ¥15). In FY3/23, the Company currently plans to pay an annual dividend of ¥70 (regular dividend).

The Company actively acquires its own shares in the market and retires them as part of the shareholder return policy. It acquired 1,958,000 shares and retired 2,000,000 shares of treasury stock during FY3/20. Meanwhile, thus far in FY3/21, the Company has already retired 1,000,000 shares and acquired another 1,000,000 shares of treasury stock. The Company has announced a plan for acquisition of treasury stock totaling 1,000,000 shares in FY3/22 too. The total return ratio (weighted average) for the past nine years covering FY3/14 to FY3/22 worked out to 87.1%. The Company's ability to maintain a high average total return ratio over a long period is commendable.

Also, the Company actively responds to stakeholders other than shareholders. For the payment terms for partner companies, it has changed to entirely cash payments for partner companies with capital of less than ¥40mn.

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

Shareholder returns

(¥mn)

	Acquisition of treasury stock		Dividend amount (B)	Amount of shareholder returns (C) = (A) + (B)	Profit attributable to owners of parent
	Number of shares	Amount (A)			
FY3/22	1,000,000	1,438	4,773	6,211	6,489
FY3/21	1,000,000	1,171	4,568	5,739	5,901
FY3/20	1,958,000	2,899	5,543	8,442	7,576
FY3/19	1,000,000	1,191	3,595	4,786	9,046
FY3/18	3,000,000	3,679	2,136	5,815	3,906
FY3/17	0	0	1,906	1,906	4,698
FY3/16	0	0	1,906	1,906	5,327
FY3/15	2,000,000	1,604	1,270	2,874	2,461
FY3/14	4,000,000	2,408	983	3,391	1,763
			Total	41,070	47,167
			Total return ratio (weighted average)		87.1%

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

FISCO

Disclaimer

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