COMPANY RESEARCH AND ANALYSIS REPORT

Altech Corporation

4641

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Index

Summary

In the previous fiscal period's results, sales and profits increased and exceeded the forecasts. On the 50th anniversary of its foundation, the outlook is also for record highs in the current period's results.

1. Company profile

Altech Corporation <4641> (hereafter, also "the Company) is a comprehensive engineering outsourcer that provides high-level technological services to major manufacturing companies in fields such as machinery, electricity and electronics, software, IT, and chemistry. It places great importance on its "Heart to Heart" corporate philosophy and consistently since its foundation, it has focused on human education from the idea of maintaining the highest levels among its employees not only as engineers, but also as members of society, in addition to strengthening their technical abilities. This can be described as its corporate organizational culture that it the source of one of its strengths, of producing talented human resources. The Altech Corporation Group is comprised of the Company and four subsidiaries, and since FY12/16, it has had two business segments, the Outsourcing Business and the Global Business.

2. Establishment of a new company

Toward realizing its medium- to long-term growth vision, the Company has decided to enter into new businesses by establishing a new company. In the agriculture-related field, which is considered to have high growth potential, and in the nursing care-related field, where the shortage of workers is conspicuous, it is aiming to create a new model for the worker assignment market. It is said that in these fields, the keys are introducing state-of-the-art technologies, such as AI, IoT, and robots, and utilizing an overseas labor force, and the Company's strategy seems to be to aim for the first-mover advantage in fields that utilize its advanced technological capabilities and expertise in developing human resources (including the employment of non-Japanese) that it has cultivated up to the present time. It is considered that a long-term perspective will be necessary for these businesses' full-fledged contribution to results, but as they have enormous potential, we will need to pay attention to developments in the future.

3. FY12/17 consolidated results

In the FY12/17 results, sales and profits exceeded the forecasts and grew by double digits, with net sales increasing 13.1% YoY to ¥30,260mn and operating income rising 13.3% to ¥3,238mn. Against the backdrop of the favorable ordering environment, results in the mainstay Outsourcing Business grew significantly, due to the high mobilization rate being maintained, the rise in the contract unit price, and the increase in the number of mobilized employees. Also, the full fiscal year contribution of PANA R&D, which entered the scope of consolidation in September 2016, was a factor behind the higher sales. In terms of profits, in addition to the rise in cost prices in the Global Business due to temporary factors, costs relating to the 50th anniversary of its foundation and advertising costs also rose, but the Company still realized an increase in operating income from the effects of the higher sales, and it kept the operating margin the same as in the previous fiscal year, at 10.7%.

4. Outlook for FY12/18

On the 50th anniversary of its foundation, the Company is forecasting new record highs for the FY12/18 consolidated results, of net sales to increase 7.1% YoY to ¥32,400mn and operating income to rise 5.9% to ¥3,430mn. The reason why the growth in results will be somewhat moderate compared to in the previous fiscal year is that the effects of PANA R&D entering the scope of consolidation will have run their course, and an evaluation that growth will be sustained at a cruising pace seems reasonable. In terms of profit-loss conditions also, although it is anticipated that costs will increase in relation to the operations to mark the 50th anniversary of its foundation, they will be absorbed by the higher sales and the increase in operating income will be maintained, while the operating margin is forecast to remain basically unchanged YoY.

5. Medium- to long- term growth strategy

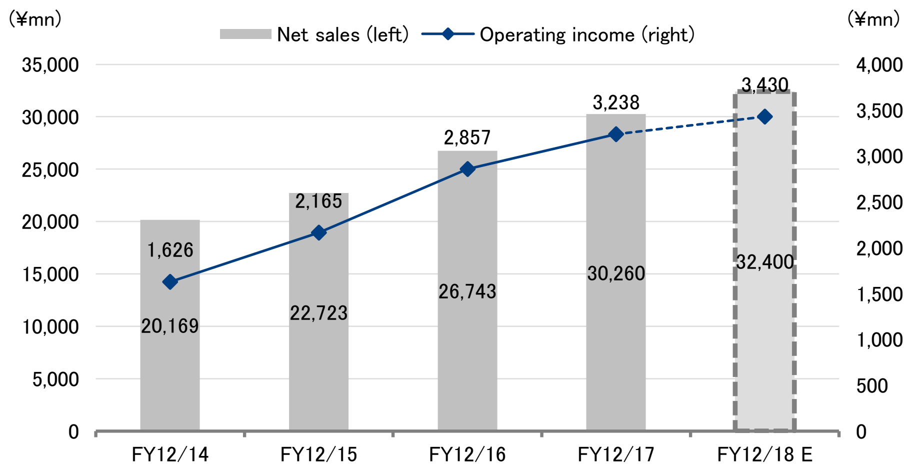
The Company announced its quantitative targets in the medium-term management rolling plan for the three years from FY12/18 to FY12/20. The final targets in FY12/20 are for net sales of ¥37,200mn and operating income of ¥3,840mn. It also forecasts that ROE will be maintained above 18%.

Moreover, as its medium- to long-term growth vision, the Company has set out a strategy on four axes, of 1) strengthening existing businesses, 2) responding to state-of-the-art technologies, 3) developing globally, and 4) taking on the challenge of new businesses. At FISCO, within a situation of the declining Japanese population and advancing economic globalization, we evaluate that the Company's direction for business development is a rational strategy that has an eye to the changes to the industrial structure in the future. The point to focus on going forward would seem to be how the Company will respond to the new technological fields where demand is increasing, including the progress in the new businesses (the nursing care and agriculture fields), and how it will connect these responses to sustainable growth. We must also continue to pay attention to M&A that utilizes its strong financial base.

Key Points

- A group of highly skilled engineers specializing in upstream processes, including development and design
- In the FY12/17 results, achieved higher sales and profits above the forecasts due to the increase in mobilized employees
- Aiming to enter into the growth fields of agriculture-related and nursing care-related through establishing a new company
- Plans to commemorate its 50th anniversary in the FY12/18 with a record-high results (and dividend)
- Aiming for sustainable growth through a strategy on the four axes of strengthening existing businesses, responding to state-of-the-art technologies, developing globally, and taking on the challenge of new businesses

Results trends



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

Company profile

From its predecessor of a design office, it has become a group of high-level engineers that provides technologies according to customer requests

1. Company profile

The Company is a comprehensive engineering outsourcing company that provides advanced technological services to major manufacturing companies in fields such as machinery, electricity and electronics, software, IT, and chemistry. Its features include that unlike fixed-term employment based employment agencies, the Company only employs full-time engineers,* and it is a group of highly skilled engineers specializing in upstream processes, such as development and design.

* For example, even during recession periods such as the bankruptcy of Lehman Brothers, it has not dismissed a single employee.

Based on its "Heart to Heart" corporate philosophy, consistently since its foundation the Company has focused on human education from the idea of maintaining the highest levels among its employees not only as engineers, but also as members of society, in addition to strengthening their technical abilities. In particular, its strengths include that it has a corporate organizational culture that produces high-quality human resources and an original education and training system*, and its results are steadily growing, supported by its excellent reputation among its customers and the favorable ordering environment.

* Broadly dividend into the abilities development education system and career development support, the Company has established an education and training system to develop human resources to have advanced technical skills and expertise, including education according to level and needs, and follow-up from career supporters (senior engineers). Moreover, long-term education and training plans become possible when the employment period is indefinite (full-time employees).

In accordance with the Revised Worker Dispatching Act (enforced September 30, 2015), the employment-period limitation was ended for indefinite-term employment, while incidental work was also ended on the abolition of specialized work classifications, and these and other revisions have been positive developments for the Company.

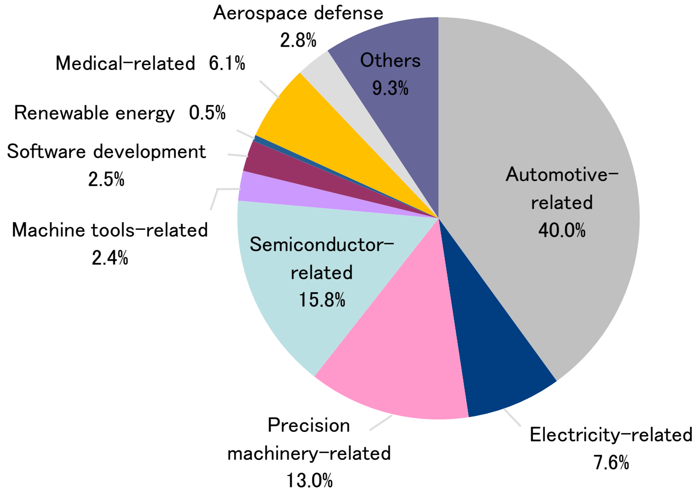
At the end of December 2017, the Company had 3,175 engineers, and of these, 3,088 were mobilized (working at customers), and it is maintaining a high mobilization rate. Also, looking at the percentages of engineers it assigns according to the fields of customer companies, machinery-related accounts for around 40%, while electricity and electronics-related and software/IT related are both approximately 30%. So it is maintaining a good balance, centered on these 3 fields.

The Company has two business segments, the Outsourcing Business, which is mainly an assignment and outsourcing business in Japan, and the Global Business, which supports Japanese companies' operations overseas. The Outsourcing Business contributes 95% of net sales, but the policy is to grow the Global Business greatly in the future.

In net sales by industry, 40.0% is provided by automotive-related*, in which R&D investment is active, and a total of 36.4% by electrical machinery, precision equipment, and semiconductor-related. So its customer industries are diverse and structured so that the Company is not easily affected by economic fluctuations. It also has around 700 customer companies, and the extent of its reliance on the top 10 customers for sales (mainly major manufacturers, such as Mitsubishi Electric <6503>, Toshiba Memory, and Canon <7751> is 19.4%, and this percentage is trending downward year by year (FY12/17 result).

* For example, even if the technological field is electrical machinery, if the final product is an EV (electric vehicle), it is classified as "automotive-related."

Percentages of net sales by industry (FY12/17 result)



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

The consolidated subsidiaries are the ALPS BUSINESS SERVICE CORPORATION, which is a provider of total staffing services; PANA R&D CO., LTD., which joined the Group in September 2016 and operates assignment of technical experts, and the two subsidiaries that conduct the Global Business, of ALPSGIKEN TAIWAN CO., LTD. (Taiwan) and Altech Shanghai CO., LTD. (China). In addition to the Head Office and the Back office and the training center, the Company has 2 Techno Parks (monozukuri centers) where it conducts manufacturing, 22 sales offices within Japan, and 1 overseas branch office (in Myanmar).

Specializes in the development and design fields and is compliant with high-level and advanced technologies

2. Business overview

(1) The Outsourcing Business

This is the Company's core business. It specializes in the development and design fields, which are manufacturing upstream processes, and it positions the provision of high-level technological services by design and development engineers as the center of its business model.

The Company provides services in the form of assignment engineers and outsourcing, and its engineers demonstrate high-level performance when responding to the wide variety of customer needs with applicable form. Assignment services take the form of spot assignments (assignment of a single engineer) and team assignments (assignment of a team of engineers whose members have various high-level skills and who conduct product design and development work). The outsourcing services take the form of on-site (the engineer is stationed at the customer's site) and off-site (the engineer returns to the Company's techno park or other site) for project outsourcing (outsourcing of design, prototyping, manufacturing, and evaluation, either on a single or collective contract basis).

Since it was founded as a design office, the Company has met the technical needs of its customers in the field of mechatronics through its concept of "machinery and electrical integrated design." In particular, it utilizes its strength of having a unique business form with its own manufacturing bases (own factories), and the Group as a whole has in place a structure able to handle all of the manufacturing processes, from development, prototyping, manufacturing to evaluation. Even within this structure, the Company's main area of technological expertise is upstream processes, where it possesses competitive advantages in the processes requiring high-level technological capabilities, including basic research, product planning, concept design, detailed and mass production design, prototypes and experiments, and evaluation and analysis.

The central areas of the technology field include machinery design, electricity and electronics design, software development, and chemistry. Alongside the transition to high-level network society, the priority items have become the development and design of a variety of advanced technologies such as for IoT and AI, 3D-CAD for which further demand is expected, CAE technologies, aerospace-related, medical-related, and robot-development technologies. Therefore, the Company's customer companies are spread across a wide range of industries, including automotive, semiconductors and LSI, industrial equipment, digital precision equipment, aerospace, space and defense, and medical and welfare equipment.

(2) Global Business

The Company currently has two overseas subsidiaries ALPSGIKEN TAIWAN CO., LTD. in Taiwan and Altech Shanghai CO., LTD. in China. They conduct installation and maintenance work for the production facilities and equipment of Japanese companies overseas, and also provide human resources services ancillary to this work. Within the advance of economic globalization, one strategic axis is expanding the Global Business.

Entering-into the agriculture-related and nursing care-related fields, which are considered to have growth potential

3. Establishing a new company (entering-into new businesses)

Toward realizing its medium- to long-term growth vision (described later), the Company had decided to enter-into new businesses through establishing a new company* (the business launch is scheduled for August 2018). In the agriculture-related field, which is considered to have high growth potential, and in the nursing care-related field, where the shortage of workers is conspicuous, it is aiming to create a new model for the worker assignment market. It is said that in these fields, the keys are introducing state-of-the-art technologies, such as AI, IoT, and robots, and utilizing an overseas labor force, and the Company's strategy seems to be to aim for the first-mover advantage in fields that utilize its advanced technological capabilities and expertise in developing human resources (including the employment of non-Japanese) that it has cultivated up to the present time. In particular, it would seem that for the agriculture-related business (agri-business), the Company is aiming to develop a business that only it, as a group of engineers, is capable of. For the nursing care-related business also, it has already begun training nursing-care human resources in Myanmar and it is planning on creating a business in line with the establishment of a legal system related to Japanese nursing care. Preparations are underway at the branch office in Yangon, Myanmar, toward the education and training of nursing care human resources and the construction of a scheme to send them to Japan.

* Agri & Care Corporation (head office, Yokohama City, Kanagawa Prefecture)

4. History

The Company's predecessor, the Matsui Design Office, was founded in 1968 based on the concept of "mechanical and electrical integrated design" of its founder, current Chairman and Director Toshio Matsui. At that time, electrical design and mechanical design were conducted separately, and to solve the various problems that arose from this, he proposed "mechanical and electrical integrated design" to customer companies as a proprietary and innovative method. The Company has encountered various difficulties, including the oil crises, but through constant efforts it has steadily gained an excellent reputation among its customers for being a comprehensive engineering outsourcer "that provides technologies according to customer requests." Further, under the leadership of the current President and Representative Director Atsushi Imamura, it is aiming to improve results and expand its business, including by focusing on training human resources who are specialized in upstream processes, such as development and design, and the early mobilization of new-graduate engineers.

History

Date	Major event
July 1968	Matsui Design Office was founded in Sobudai, Sagamihara City, Kanagawa Prefecture Started the first five-year plan, "Develop the Company"
January 1971	Renamed the Matsui Design Office as Altech Inc., and established it in Sobudai, Sagamihara City, Kanagawa Prefecture
July 1973	Started the second five-year plan, "Increase Business with Prime Customers and Maintain Internal Capital"
July 1978	Started the third five-year plan, "Implement an Institutionalization of the Company and Improve Technical Capabilities"
January 1981	Moved head office to Kyowa, Sagamihara City, Kanagawa Prefecture
March 1981	Reorganized the organization and transferred it to Altech Corporation
July 1983	Started the fourth five-year plan, "To be an International company and Develop Human Resources"
April 1984	Opened the Tohoku business office in Koriyama City, Fukushima Prefecture
April 1985	Opened the Shinshu business office in Shiojiri City, Nagano Prefecture
July 1985	Constructed a building in Nishi-Hashimoto, Sagamihara City, Kanagawa Prefecture and relocation of Head Office to
February 1986	Established Kita Kanto business office in Fukaya City, Saitama Prefecture
April 1986	Established subsidiary Technical Training Center CO., LTD. (currently, ALPS BUSINESS SERVICE CORPORATION) from the technical training department
July 1988	Started the fifth five-year plan, "Restructuring of the Organization and Developing the Company's own Technology."

Date	Major event
December 1989	Established Tateshina Techno Park in Chino City, Nagano Prefecture, started production of in-house developed products and the design and production of precision machinery
October 1990	Adopted a divisional organization structure to utilize profit center management and accounting systems. Established six business division below the Tohoku business division
July 1993	Started the sixth five-year plan, "Nurture High-quality Human Resources for High-quality Companies"
June 1996	Altech is listed on the OTC market of the Japan Securities Dealers Association (currently, JASDAQ) Increased capital to ¥832,619,000
July 1997	Increased capital to ¥1,502,219,000
January 1998	The Tokyo Business Division was separated from the Kanto Division, and the West Japan Division divided into the Osaka Division, the Nagoya Division and the Kyushu Division, and the Tateshina Techno Park was newly established from the Chubu Division. In addition to Tohoku Division, the Company became an eight-business division structure
July 1998	Started the seventh five-year plan, "Restructuring our Business Field and our Core Competencies."
September 1998	Completed the new building of Chubu business division as own property in Shiojiri City, Nagano Prefecture
December 1998	Established the Taiwanese subsidiary (currently, ALPSGIKEN TAIWAN CO., LTD.), in Taipei City, Taiwan
October 1999	Utsunomiya Factory (now Utsunomiya Techno Park) opened in Yaita City, Tochigi prefecture
July 2000	Tateshina Techno Park No. 2 factory completed
September 2000	Listed on the second section of the Tokyo Stock Exchange (listing date September 28, 2000)
July 2001	Completed a new building and the Training Center Relocated the Head Office
March 2003	Introduced a business headquarters system from the business division system (four blocks nationwide)
July 2003	Started the eighth five-year plan, "Creation of New Corporate Value"
October 2004	Entered-into a technical alliance with Qingdao University of Science Technology in China, opened the "Machinery Design Education Program"
December 2004	Listed on the Tokyo Stock Exchange First Section. (first section designation date, December 1, 2004)
July 2005	Introduced the central organization structure to upgrade risk management capabilities.
April 2006	Entered-into a technical alliance with China University of Petroleum, established the China University of Petroleum ALPS International Engineer Education Center
July 2006	Issued 1st unsecured convertible bond type bonds with stock acquisition rights of ¥2 billion
January 2007	Opened the Atsugi Sales Office
February 2007	Participated in the establishment of the Nippon Engineering Outsourcing Association
March 2007	Established subsidiary ALTECH QINGDAO CO., LTD.) in Qingdao City, China
July 2007	Opened the ALPS Qingdao Education Development Center (Qingdao City, China)
October, 2007	Opened the Tsukuba Sales Office (currently, the Hitachi Sales Office)
July 2008	Started the ninth five-year plan "Leap to be a Leading Company"
January 2009	Established the subsidiary Altech Forest Corporation.
March 2009	Opened the Takasaki Sales Office
March 2010	Established the subsidiary Altech Shanghai CO., LTD. (CHINA) in Shanghai, China
March 2011	Relocated Head Office to Minato Mirai, Nishi Ward, Yokohama City, Kanagawa Prefecture Opened the Hitachi Sales Office
February 2012	Opened the Kyoto Sales Office
August 2012	Established the subsidiary Alps Career Designing Corporation in Chiyoda Ward, Tokyo
July 2013	Started the tenth five-year plan "Expansion of Enterprise Scale through Innovation" ~ Accelerate growth as we move toward our 50th anniversary ~
December 2014	Subsidiary Altech Forest Corporation removed from the scope of consolidation on the transfer of shares
April 2015	Opened Yangon branch office in Myanmar (Yangon city)
September 2016	Made PANA R&D CO., LTD. a consolidated subsidiary Alps Business Services Corporation merged with Alps Career Designing Cooporation

Source: Prepared by FISCO from the Company's materials

Business performance

The growth in results is being driven by the active recruitment of new graduates and the increase in the number of mobilized employees through their early mobilization

1. Overview of the FY12/17 consolidated results

The Company exceeded its targets and achieved double digit growth in sales and earnings. Net sales were ¥30,260mn, up 13.1% YoY, operating income was ¥3,238mn, up 13.3%, ordinary income was ¥3,275mn, up 11.1%, and profit attributable to the owners of parent was ¥2,367mn, up 19.1%.

In sales, against the backdrop of the favorable ordering environment (particular from the strongly performing automotive and semiconductor industries), results in the mainstay Outsourcing Business grew significantly from the high mobilization rate being maintained, the rise in the contract unit price, and the increase in the number of mobilized employees. Also, the full fiscal year contribution of PANA R&D, which entered the scope of consolidation in September 2016, was a factor behind the higher sales (estimated to have contributed around ¥1.1bn). In particular, the reason why the results exceeded the forecasts was that the employee retention rate increased more than expected through various measures, such as improving employee benefits and enhancing the education system* (as a result, the number of engineer employees also increased more than expected).

* Includes the enhancement of OJT that can realize growth, such as through "team assignments," and a mechanism that can form careers autonomously

In terms of profit and loss, the cost-of-sales ratio remained basically unchanged YoY at 75.1% (75.0% in the previous fiscal year) as in addition to the improved benefits for employees, costs in the Global Business rose due to temporary factors, but this was absorbed by the growth in sales. SG&A expenses also grew due to higher costs, mainly amortization costs relating to the commemoration of the 50th anniversary of its foundation and advertising costs (including the Company's first ever TV commercial). However, it still achieved an increase in operating income from the effects of higher sales, and it was able to maintain the operating margin unchanged YoY, at 10.7% (the target was a 10% level). The fact that the growth rate of final income (net income) was large was due to a gain on the sale of investment securities (extraordinary income), so it is necessary to be aware that this is also a temporary factor.

In the Company's financial condition, total assets were up 12.0% on the end of the previous fiscal year to ¥18,435mn, due to the increases in notes and accounts receivable and in work in progress alongside the business expansion, and also because of the rise in construction in progress (non-current assets) relating to the construction of the 2nd building. Shareholders' equity also increased 13.4% to ¥12,276mn, mainly due to the accumulation of retained earnings, so the equity ratio improved slightly to 66.6% (65.8% on the end of the previous fiscal year). Interest-bearing debt was down 2.8% on the end of the previous fiscal year to ¥700mn, while the current ratio is also at the high level of 240.5% (230.0% at the end of the previous fiscal year), so there are no concerns about the Company's financial stability. ROE, which shows capital efficiency, was maintained at the high level of 20.5% (19.4% at the end of the previous fiscal year)

Overview of FY12/17 results

(¥mn)

	FY12/16 results		FY12/17 results		YoY		FY12/17 initial forecast		Achieve-ment rate
		% of sales		% of sales		%		% of sales	
Net sales	26,743		30,260		3,516	13.1%	29,000		104.3%
Outsourcing Business	24,761	92.6%	28,745	95.0%	3,983	16.1%	-	-	-
Global Business	1,982	7.4%	1,515	5.0%	-466	-23.6%	-	-	-
Cost of sales	20,057	75.0%	22,737	75.1%	2,680	13.4%	-	-	-
SG&A expenses	3,828	14.3%	4,283	14.2%	455	11.9%	-	-	-
Operating income	2,857	10.7%	3,238	10.7%	380	13.3%	3,070	10.6%	105.5%
Outsourcing Business	2,686	10.9%	3,191	11.1%	504	18.8%	-	-	-
Global Business	168	8.5%	43	2.9%	-125	-74.0%	-	-	-
Ordinary income	2,949	11.0%	3,275	10.8%	326	11.1%	3,170	10.9%	103.3%
Profit attributable to owners of parent	1,988	7.4%	2,367	7.8%	378	19.1%	2,130	7.3%	111.1%
Number of engineers	2,897		3,175		278	9.6%			
Number of mobilized employees	2,797		3,088		291	10.4%			
Mobilization hours	173.5		171.8		-1.7	-1.0%			
Contract unit price	3,856		3,903		47	1.2%			

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

FY12/17 financial condition

(¥mn)

	FY12/16	FY12/17	Change	
				%
Current assets	12,167	13,760	1,593	13.1%
(cash and deposits)	7,311	8,370	1,058	14.5%
(notes and accounts receivable - trade)	3,916	4,357	440	11.3%
Non-current assets	4,290	4,675	384	9.0%
(goodwill)	462	394	-68	-14.8%
Total assets	16,458	18,435	1,977	12.0%
Current assets	5,289	5,722	432	8.2%
(accounts payable - other)	1,396	1,265	-130	-9.4%
(short-term loans payable)	720	700	-20	-2.8%
Non-current liabilities	325	417	92	28.3%
Total liabilities	5,614	6,139	524	9.3%
Net assets	10,843	12,295	1,452	13.4%
Shareholders' equity	10,826	12,276	1,449	13.4%
Current ratio	230.0%	240.5%	10.5%	-
Equity ratio	65.8%	66.6%	0.8%	-
Interest-bearing debt ratio	6.7%	5.7%	-1.0%	-
ROA (ratio of ordinary income to total assets)	19.0%	18.8%	-0.2%	-
ROE (ratio of profit to equity)	19.4%	20.5%	1.1%	-

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

Overview of each segment is outlined below.

(1) The Outsourcing Business

Results grew greatly in the Outsourcing Business, with net sales increasing 16.1% YoY to ¥28,745mn and segment income rising 18.8% to ¥3,191mn. In addition to the full fiscal year contribution of PANA R&D, which previously entered the scope of consolidation, in the context of the favorable ordering environment, the increase in the number of mobilized employees and the improvement in the contract unit price from the success of the series of policies for recruitment*1, education, and sales, contributed to the growth in results. All of the indicators that emphasize results increased, as the number of engineer employees became 3,175 people (up 278 people on the end of the previous fiscal year), the number of mobilized employees became 3,088 people (up 291 people), and the contract unit price*2 became ¥3,903 (up ¥47). Moreover, the annual average mobilization rate was maintained at the high level of 96.2% (95.6% in the previous fiscal year). However, the reason for the decrease in the average number of hours worked per employee*3 to 171.8 hours (down 1.7 hours) seems to be as a result of the reforms to ways of working, particularly at major companies.

*1 In 2017, in addition to the 242 new graduates (joined the Company in April), it recruited 37 global engineers (joined in October), and around 160 mid-career recruits (joined in 2017).
*2 The unit price per hour based on the contract with the customer (does not include overtime fees)
*3 Hours worked per month, corresponding to work as an engineer

(2) Global Business

In the Global Business (which includes the design, manufacture, installation and maintenance of various plant equipment and plant machinery, and human-resources services), net sales decreased 23.6% YoY to ¥1,515mn and segment income fell 74.0% to ¥43mn. Sales and profits declined as a reaction to the fact that there were orders for major projects in the previous fiscal year, and also due to the rise in cost prices for some projects. However, on excluding these temporary factors, it can be said the results trended favorably, including due to the growth in demand from Japanese companies.

2. Summary of FY12/17 results

To summarize the FY12/17 results based on the above, in addition to the fact that results grew to levels above the forecasts, it can also be said that the Company was able to achieve some major outcomes through its measures, which included 1) achieving the recruitment plan and advancing the early mobilization of new-graduate recruits, 2) improving the employee retention rate by enhancing employee benefits (such as supplementing and newly establishing various allowances), and 3) implementing original measures to develop human resources (a mechanism to create places for engineers to be active independently). In the Group companies also, the assignments, outsourcing, and introductions businesses of ALPS BUSINESS SERVICE are performing strongly and contributing to the growth in the Group's results, while PANA R&D is starting to realize synergies, including for sales and education. In particular, for sales, it seems to be functioning as a mechanism for the introduction of customers from the Company. However, recruitment is acting as a constraint (a bottleneck) for it to respond to the plentiful requests for assignments from customers and to realize even further business expansion for the Group, so it can be said that an issue for the future (to realize growth) will be generating synergies at this place of entrance.

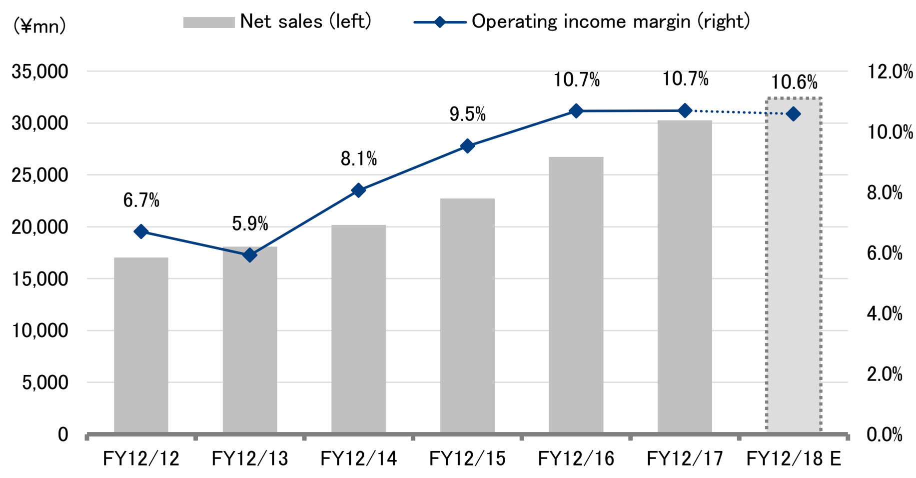
3. Trends in past results (consolidated)

Looking at results up to the present time, we see that they have steadily grown alongside the increase in the number of engineer employees. In particular, since FY12/14, despite the ongoing severe recruitment environment, the Company has still been able to recruit around 250 new graduates a year and realize their early mobilization, and this has driven the growth in results. It can be said that recruiting around 250 new graduates every year and around 40 global engineers in fields with high levels of specialism, and then completing their training at an early stage and maintaining a high mobilization rate, is a growth model that only the Company is capable of. In addition, it is coordinating with its consolidated subsidiary ALPS BUSINESS SERVICE and expanding its overseas business, while PANA R&D, which entered the scope of consolidation in September 2016, is also contributing to the growth in the consolidated results.

In terms of profit and loss, profits have trended upward alongside the growth in net sales. The operating margin has also improved, and in the last few years it has trended at the high level of above 10%.

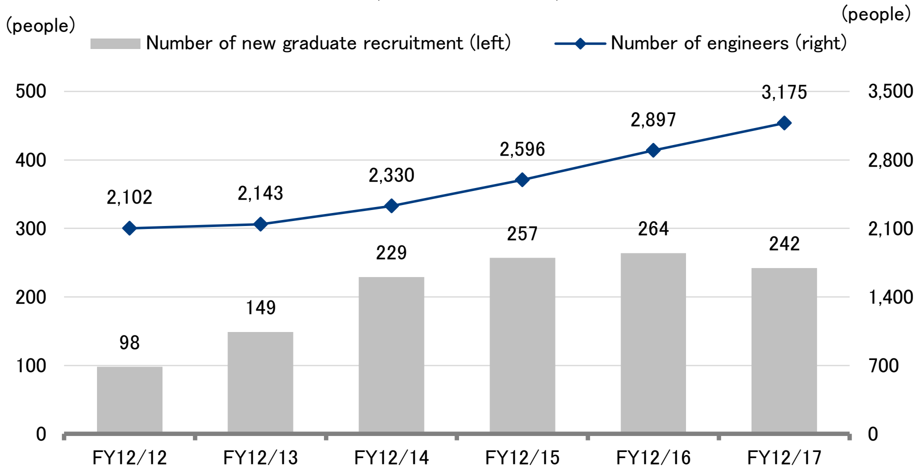
For the Company's financial condition, total assets grew following the increases in cash and deposits and other items, and while the equity ratio is trending downward slightly, it remains at a level of above 65%. On the other hand, ROE, which indicates capital efficiency, is rising year by year, and in the last fiscal period it reached a level of above 20%. Therefore, the Company's financial condition can be evaluated as being extremely good. It also has plentiful liquidity on hand (cash and deposits), which serves as a buffer against unforeseen circumstances and also expands the range of strategies it can adopt for growth, so it will be necessary to pay attention to developments in the future.

Trends in net sales and operating income margin (consolidated)



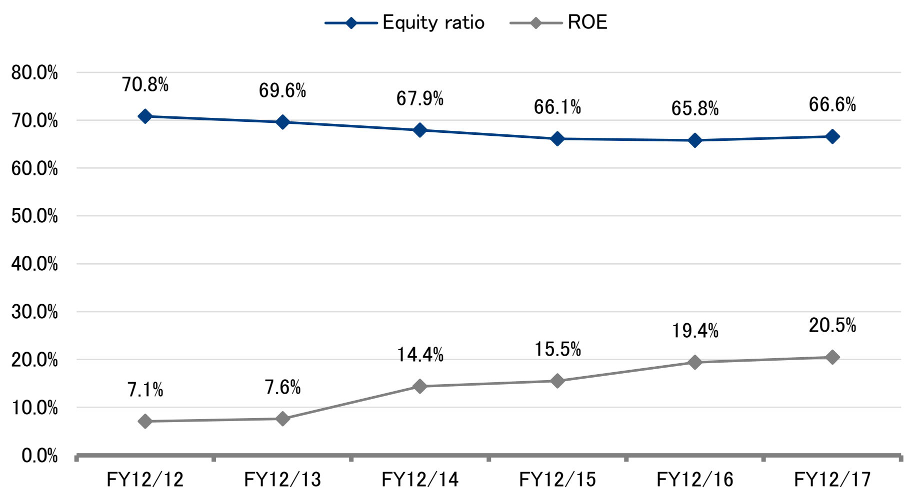
Source: Prepared by FISCO from the Company's financial results

Trends in the number of new-graduate recruits and engineers (stand-alone basis)



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

Trends in equity ratio and ROE



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

Business outlook

On the 50th anniversary of its foundation, the outlook is for record high results

1. Outlook for FY12/18

For the FY12/18 consolidated results, the Company is forecasting higher sales and profits, with net sales to increase 7.1% YoY to ¥32,400mn, operating income to grow 5.9% to ¥3,430mn, ordinary income to increase 7.2% to ¥3,510mn, and net income attributable to the owners of the parent to climb 0.1% to ¥2,370mn. Moreover, the forecasts are for new record highs.

Requests for assignments continue to be strong from the various major manufacturers, which are the Company Group's main customers, and this trend is expected to continue. The reasons why the growth in results will be somewhat moderate compared to in the previous fiscal year is that the effects of PANA R&D entering the scope of consolidation will have run their course, and an evaluation that growth will be sustained at a cruising pace seems reasonable. On the 50th anniversary of its foundation, the Company is aiming for growth in the Group as a whole.

In terms of profit and loss, although an increase* in costs relating to the operations to commemorate the 50th anniversary of its foundation is expected, the Company is forecasting that this will be absorbed by the higher sales and it will secure an increase in profits, while the operating margin is set to remain basically unchanged YoY. Final income (net income) will only increase slightly on the end of the extraordinary-income item recorded in the previous fiscal year (gain on the sales of investment securities).

* In addition to the construction of the 2nd building (to be utilized for the entry into new fields as a symbol of the 2nd foundation period) and the donation of wheelchairs (as part of its CSR activities, it plans to donate around 450 heavy-duty wheelchairs to local governments, welfare councils and other organizations throughout the country with which it has deep connections), it is planning other spending, including on advertising to improve name awareness.

At FISCO, we think that on considering the favorable external environment (such as the plentiful requests for engineer assignments), and also the internal factors (including the improvement in the employee retention rate and the early mobilization of the new graduate recruits), it is fully possible that the Company will achieve its results forecasts.

2. Plan for activities

On approaching the 50th anniversary of its foundation, the Company will implement the following measures on the start of the 2nd foundation period (to build foundations).

(1) Measures to create the next generation (individual)

The Company will reform the three pillars that support its growth (recruitment, education, and sales) and realize a virtuous circle that produces mutually positive effects. In particular, its policy is to aim to ascertain in advance changes to technologies and industries and to respond to growth fields.

a) Recruitment

It is working on measures including 1) establishing long-term relations of trust with priority universities and colleges, 2) strengthening recruitment through collaborations with engineers and within the Group, and 3) expanding the recruitment of global engineers and the training scheme. Within the severe recruitment environment, the Company will continue its policy of prioritizing quality for the recruitment of new graduates in 2019 (in addition to the recruitment of quality human resources, this also means recruitment within the scope of its capabilities for education and training), and it plans to recruit 250 new graduates, which is the same number as in 2018. Also, in addition to (the target of) 120 mid-career recruits in 2018, it is actively working to recruit global engineers.

b) Education

It is working on measures including 1) providing education and training that utilizes the original education expertise that it has cultivated over the last 50 years, and 2) providing training toward entering into growth industries. In particular, it will incorporate customized training that is tailored to meet customer needs, starting with strengthening for the fields of state-of-the-art technologies, such as AI and IoT.

c) Sales

It is implementing measures including 1) conducting priority sales for growth-industry fields, 2) strengthening sales toward improving CS (customer satisfaction), and 3) conducting rotation so that the engineers themselves can realize growth. Particularly for 2), in a situation in which the Company individually is close to full operations, it intends to create proposals together with all the other Group companies in order to respond to the plentiful requests for assignments from customers.

* The Company is incorporating a mechanism that enables the engineers themselves to feel their own growth through creating a database of the career plans of each individual engineer, and then matching them to the requests from customers.

(2) Measures for the Group

It is working to further enhance cooperation within the Group, to strengthen recruitment and education, and to expand the business domains together with the Group as a whole. In particular, it is striving to create synergies with its domestic subsidiaries and overseas business, and to launch new businesses.

a) Domestic business

For ALPS BUSINESS SERVICE, the aim is to increase the number of employees through Group cooperation and to expand its business (including the provision of one-stop services in its post-process assignments, outsourcing, and introduction businesses). It is also working on measures including establishing an education system as the base for the education of Group human resources (such as training for interpersonal skills) and improving benefits. For PANA R&D, it is working to further strengthen the Outsourcing Department and to establish and improve a foundation environment.

b) Overseas business

The Company is further expanding the Global Business (the installation and maintenance of production facilities and related for Japanese companies and others, and human-resources services) through its local subsidiaries in Shanghai and Taiwan. In addition, in the Yangon branch office (Myanmar), it is working to launch new businesses (agriculture and nursing care) through the education and training of human resources. It is also continuing to aim to expand the routes for recruiting global engineers in China and Vietnam.

3. Industry trend and the Company's position

The number of assignment workers nationwide peaked at 2.02 million people in 2008, which was around the time of the bankruptcy of Lehman Brothers, and then trended downward after that and had bottomed out in 2013 falling to 1.29 million people by 2017. Also, the environment surrounding the worker assignment business seems to have reached a major turning point due to factors including the revisions to the Worker Dispatch Act (enforced on September 30, 2015) and the guidelines on equal pay for equal work. It is considered that the situation in this business will change greatly in the future, depending on what assignment companies expect of the assignment employees, such as their technical capabilities and expertise. In short, the need for new human resources with high-level technical capabilities and expertise will remain steady, but it seems there will be major changes in the work in downstream processes, for example due to economic trends.

In the Company, the position of engineers is stable as they are employed indefinitely (full-time employees) and they acquire high-level technical capabilities and expertise from the education and training they receive, and therefore they earn the trust of the customer companies. The results of the Company, which specializes in the assignment of indefinitely employed engineers, are expected to steadily expand in the future. Of course, in order to be assigned upstream processes, the Company will need to strive ceaselessly so that its engineers may utilize their technical capabilities and expertise and meet the needs of customers in industries such as electricity and machinery, automotive, and aerospace and space. Supported by its long-term education for its engineers, it is considered that the Company will be able to continuously expand its business by earnings its customers' trust.

Medium- to long-term growth strategy

Aiming to expand its portfolio by developing new technologies and for new markets

1. The new medium-term management plan (2018 to 2020)

Since its foundation, the Company has been formulating qualitative targets for every five years and quantitative targets for every three years (rolling targets in the medium-term management plan). As the FY12/17 results exceeded their forecasts, it upwardly revised the amounts for the previous quantitative targets* and also formulated a new three year medium-term management plan. The targets for FY12/20, which is the plan's final year, are net sales of ¥37,200mn, operating income of ¥3,840mn, ordinary income of ¥3,960mn and net income attributable to the owners of the parent of ¥2,680mn. It also plans to secure ROE of above 18%.

* Through raising the assumption for the number of engineer employees, which was a factor behind the FY12/17 results exceeding their forecasts.

The major themes for the tenth five-year plan are "Expand the corporate scale through innovation – accelerating growth as we move toward our 50th anniversary," and the Company has implemented the following three measures.

(1) Anticipate changes to technologies and industries and provide a variety of high-level technological services
(2) Accelerate the expansion in the scale of the Company Group through the independence and growth of affiliated companies
(3) Making a leaping forward to become a global corporate group developing businesses in Asia

The Company plans to announce the next five-year plan (the 11th Five-year Plan) on the occasion of the 50th anniversary of its foundation in July 2018.

At FISCO, we think that the targets in the newly announced medium-term management plan are fully achievable, as they assume growth at the same cruising pace as the Company has achieved so for. Therefore, we are focusing on the possibility that the further development of Group synergies and the early launches of the new businesses (mainly the nursing care and agriculture businesses) will become factors causing results to exceed their targets.

2. Medium to long-term growth vision

Together with the medium-term management plan, the Company has explained its direction for its next business development in the process after the 50-year anniversary in terms of a portfolio with 4 quadrants divided on 2 axes, of markets and businesses / technologies, and also into existing and new areas for each axis.

(1) Provision of high-level technological services (existing markets, existing business / technologies)

These are existing services, such as for machinery design, electricity and electronics design, and development. They are the Company's stable source of earnings and going forward, it is aiming to strengthen the project management structure and other structures for business expansion.

(2) State-of-the-art technologies' (high unit price zone) development and design work (new markets, existing business / technologies)

This is development and design work in various advanced-technology areas, including AI and IoT, robots, hybrid and EV vehicles, aerospace-related, and medical-related, and the Company is responding to changes in technologies to meet societal needs to expand into the corresponding markets.

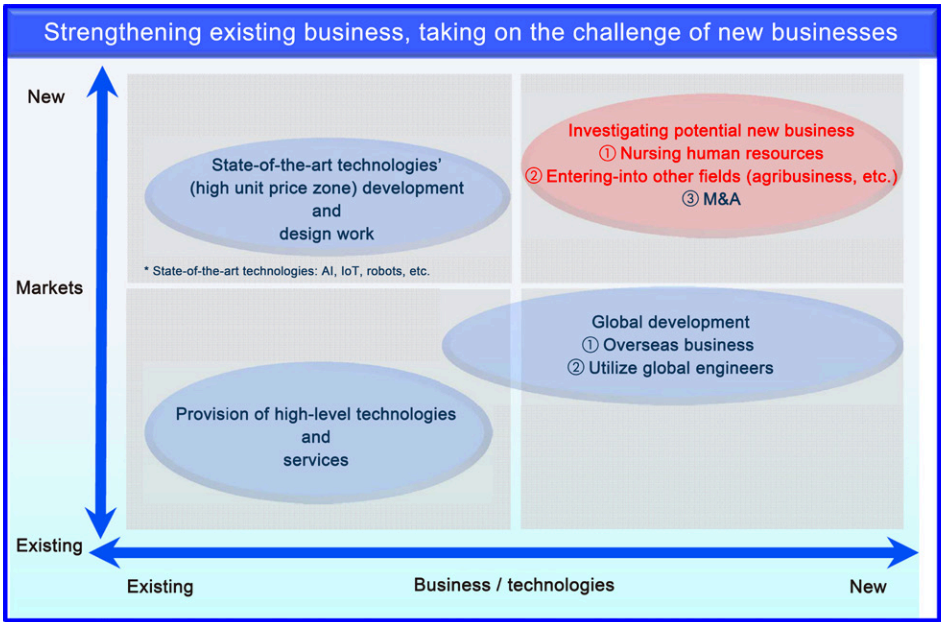
(3) Global development (existing markets, new business / technologies)

Basically, this is the provision of services like the construction and management of production facilities locally alongside the overseas expansion of its customer companies. For the time being, the Company's regional focus is on China and Asia, and it is also aiming to utilize global engineers, such as to act as bridging engineers.

(4) Investigating potential new businesses (new markets, new business / technologies)

The Company intends to advance various measures, including developing nursing care human resources, opening-up other fields (including the agri-business), and conducting M&A. As previously mentioned, it has decided to establish a new company for the agriculture-related field and nursing care-related field, and it has begun specific measures toward the development of a new worker assignment business.

The medium- to long-term growth vision (direction of the business development)



Source: From the Company's results briefing materials

At FISCO, within a situation of the declining Japanese population and advancing economic globalization, we evaluate that the Company's direction for business development is a rational strategy that has an eye to the changes to the industrial structure in the future. Up to the present time, it has responded at high levels to the changes to technological needs, and the point to focus on going forward would seem to be how it will respond to new technological fields in which demand is expanding, and how these responses will connect to sustainable growth. Particularly for the new businesses, including in the agriculture-related field (agri-business) and the nursing care-related field, because of their great potential from societal demands, it seems fully possible that the Company will grow these business to become its profit drivers in the future, as it will be able to utilize its expertise and networks for developing human resources that it has acquired overseas. It is expected that some time will be required for the nursing care-related business, but it is possible that it will be able to launch the agri-business in some form at a comparatively early stage, so we will be watching the developments closely. We must also continue to pay attention to M&A that utilizes its strong financial base.

Shareholder return policy

In FY12/18, plans to pay a record-high dividend, including a commemorative dividend.

1. Basic dividend policy

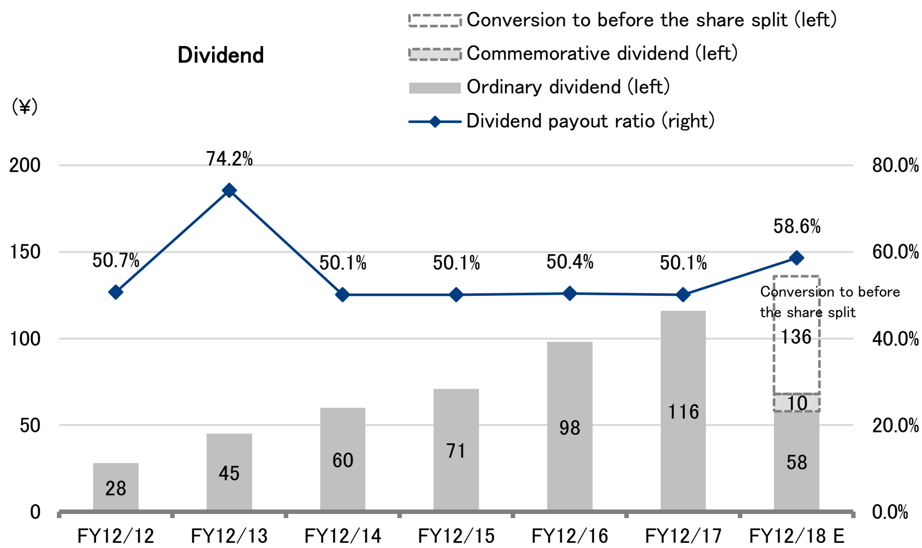
The Company pays dividends as its policy to return profits to shareholders. It aims for a payout ratio on a consolidated basis of 50%, and its basic policy is to pay an annual dividend of ¥20, regardless of results.

2. Dividend trend and plan

On looking at how dividends have trended in the past, we see that the Company has continued to steadily increase the dividend against the backdrop of the favorable results. It has maintained the dividend payout ratio at around 50%.

For FY12/17, the Company decided to upwardly revise the initial dividend forecast and pay an annual dividend of ¥116 (interim ¥52, end-of-term ¥64) which is an increase of ¥18 YoY and also a new record high (dividend payout ratio, 50.1%) It also implemented a (2 for 1) share split on January 1, 2018, with the aim of expanding its investor base and improving the liquidity of the Company's shares.

The FY12/18 dividend (after the share split) will include a commemorative dividend of ¥10 to mark the 50th anniversary of its foundation. After adjusting for the share split, it is planning an annual dividend of ¥68 (interim ¥39, end-of-term ¥29), which is a ¥10 increase YoY (dividend payout ratio, 58.6%).



Note: For FY12/18 (scheduled), the amounts converted to before the split are additionally shown.
Source: Prepared by FISCO from the Company's financial results

Information security

The Company Group works on maintaining information security as a priority, because its engineers work externally at the places to which they are assigned. Specifically, it is constructing a system to thoroughly ensure information security through establishing a personal information protection policy, an information security basic policy, and related regulations, and it is managing these policies and regulations appropriately and educating all employees on them. It also regularly provides thorough guidance on compliance with security rules at the places to which its engineers are assigned.

FISCO

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