eGuarantee, Inc

8771

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Index

Summary

Is focusing on risk hedging services for FinTech-related companies and aiming for further growth

The core business of eGuarantee Inc., <8771> (hereafter, also "the Company") is to provide credit risk guarantee services targeting the sales credits issued by companies to their customers. The Company hedges the credit risk it assumes by transferring the guarantees to financial institutions via reassurance contracts. It has a recurring revenue business model in which its net sales are calculated as the balance of outstanding guarantees multiplied by the guarantee fee ratio. A strength is being able to set an optimal guarantee fee ratio due to its capabilities of gathering corporate information from more than 25,000 companies per month and advanced screening capabilities. It mainly acquires new customers though collaborating financial institutions and the like and has maintained growth by continuing to increase its balance of credit guarantees outstanding.

1. FY3/19 results

In the FY3/19 consolidated results, both sales and profits once again increased, with net sales rising 9.2% year-on-year (YoY) to ¥5,573mn and recurring profit growing 10.8% to ¥2,552mn. The balance of credit guarantees, which is the foundation of earnings, increased steadily, up 12.6% on the end of the previous fiscal year to ¥388.7bn. The main reasons for the increase were the acquisitions of new customers via partner financial institutions and others, and also that the Company worked on consulting sales for large companies that are working on "reforming ways of working" to propose to them more efficient operations, such as for credit management and credit collection. The number of corporate bankruptcies trended at a low level and the average guarantee fee ratio declined, so net sales were slightly below the initial forecast. But recurring profit was basically as forecast due to the improvement to the cost ratio, and the Company has continuously achieved higher sales and profits since it was listed.

2. FY3/20 outlook

The forecasts for the FY3/20 consolidated results are for the higher sales and profits to continue, with net sales to increase 11.2% YoY to ¥6,200mn and recurring profit to rise 7.7% to ¥2,750mn. Although the economic outlook is becoming increasing unclear due to the impact of factors such as the US-China trade friction, in the Company's business model, even if the economy worsens, companies will still need to hedge the risk of sales credit bad debt, so the steady growth is expected to continue. In terms of the key measures, it intends to supplement sales resources and improve the contract-renewal rate, and to fully expand various types of risk hedging services for the FinTech-related companies, that have been market launched in the last few years, such as companies providing a payroll payment service.

3. Growth strategy

At the current time, the Company's management numerical target is consolidated recurring profit of ¥5,000mn, and the balance of credit guarantees necessary to achieve this level will be in the range of ¥700bn to ¥800bn, which is approximately double the amount at the end of the previous fiscal year. If the growth continues at the current pace, it will have this target in sight by FY3/24. The Company is expanding the targets of its risk hedging services other than for sales credits, and at the same time, it is expanding its range of risk tolerance from the previous low risk to middle risk. So it seems that going forward, it will be able to grow the guarantee balance at an annual rate of around 10% to 15%. Also, in order to strengthen its ability to undertake risk, it plans to form new funds at a pace of one per year. There are many financial institutions having problems with investment-management customers due to the low-interest rates at the present time, so the ability to recruit on comparatively favorable conditions is also proving to be beneficial for the Company.

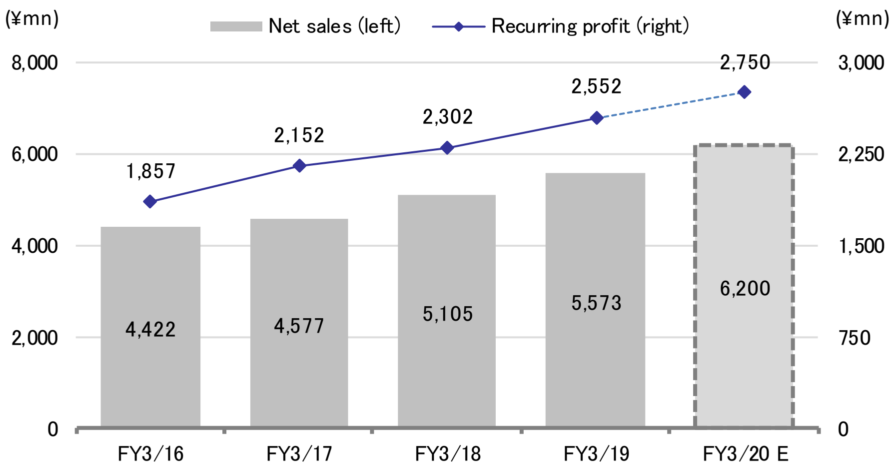
4. Shareholder return policy

Looking at the shareholder return policy, eGuarantee's basic policy is to pay dividends in line with earnings while retaining the internal reserves needed to aggressively expand business and ensure a strong financial position, targeting a payout ratio of around 30%. In FY3/20, eGuarantee plans to issue an annual dividend of ¥13.0 per share, representing a dividend payout ratio of 25.1%. If the Company achieves its target, it is likely to continue increasing its dividend. As for the Company's shareholder gift program, eGuarantee awards a QUO card worth ¥1,500 to each shareholder at the end of March every year.

Key Points

- It guarantees companies' risk of irrecoverable sales credits and other credits and provides a service that contributes to their business expansion
- The outlook is for the higher sales and profits to continue in FY3/20 also from the extremely strong demand for sales credit guarantees
- Aiming to achieve consolidated recurring profit of ¥5bn as its medium-term target

Results trends



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

Company overview

It guarantees companies' risk of irrecoverable sales credits and other credits and provides a service that contributes to their business expansion

1. Company history

eGuarantee can trace its origins to its establishment as a subsidiary of ITOCHU Corporation <8001> by Mr. Masanori Eto, the current president and CEO of eGuarantee, during his third year as an ITOCHU employee in September 2000. Initially, eGuarantee set out to provide a service to hedge the risk of uncollectible sales credits, such as trade notes and accounts receivable, for B2B transactions over the Internet. However, demand for these services was lower than initially anticipated. Therefore, eGuarantee evolved into a provider of credit risk guarantee services for sales credits in real B2B business transactions that do not involve the Internet.

In March 2007, the Company was listed on the JASDAQ Securities Exchange (listing changed to the Tokyo Stock Exchange 1st Section in December 2012), and using the funds it raised from the listing, in 2008 it formed its first fund investing in corporate credit risk and started operations through a subsidiary. Previously, it had packaged its guarantees according to the degree of risk and sold these packages to all financial institutions for them to hedge risks. But by forming new funds, it is aiming to diversify its opportunities for profits and to strengthen its ability to undertake risk, thereby accelerating growth. As of June 2019, the fund association consisted of five consolidated subsidiaries and one equity-method affiliate.

In January 2012, eGuarantee acquired the factoring business of Coface Japan Finance Co Ltd., the Japanese arm of Coface Group, which is a leading French credit guarantee group. The purpose of the acquisition was to upgrade and expand the Company's business foundations and bolster its product development capabilities by obtaining expertise related to export credit guarantees. By leveraging the expertise obtained through this acquisition, eGuarantee entered into business alliances with local financial institutions in South Korea in December 2013 and China in June 2014, and has commenced export credit guarantee service business in those countries.

Alongside the expansion of its business scope, in 2013 the Company established eGuarantee Solution Inc., as a subsidiary to carry out in-house system development and sales-related administrative work (contract-related work and data registration services) and in 2014, it established RG Guarantee, Inc., as a subsidiary to be a specialized provider of small-ticket credit guarantee services. Then 2017, it separated the sales-related administrative work from eGuarantee Solution, Inc. and newly established eGuarantee Shared Services, Inc.

Company history

Month/year	Main events
September 2000	Established in Minato-ku, Tokyo as a subsidiary of ITOCHU Corp.'s financial, real estate, insurance and distribution company to guarantee financial credit held by factoring companies mainly as a result of the settlement of electronic commercial transactions
November 2001	Started offering a comprehensive guarantee service to non-financial companies through which it guaranteed the sales credit accumulated by companies in their normal course of business
February 2004	Started offering an individual guarantee service through which it guaranteed the sales credit accumulated by a single company
August 2004	Started a full-scale guarantee service for financial companies other than factoring companies
March 2007	Listed shares on the JASDAQ Securities Exchange
August 2008	Arranged Credit Creation 1, the company's first fund for investment in corporate credit risk
November 2009	Arranged Credit Investment 1
December 2011	Listed shares on the Second Section of the Tokyo Stock Exchange
January 2012	Purchased part of the business of Coface Japan Finance Co., Ltd., a member of a leading French credit guarantee group
April 2012	Established Denshi Saiken Acceptance Ltd., a joint venture with NEC Capital Solutions This joint venture purchases electronically registered credits at a discount and engages in factoring and securitization (it was dissolved in 2015)
December 2012	Listed shares on the First Section of the Tokyo Stock Exchange
November 2013	Established eGuarantee Solution, Inc. as a subsidiary to conduct contract-related administration work, data registration services and other related activities
December 2013	Entered into a business alliance with a leading local financial institution in South Korea and launched export credit guarantee services in the South Korean market
March 2014	Established RJG Guarantee Co., Ltd. as a subsidiary to provide small-ticket credit guarantee services
June 2014	Entered into a business alliance with the Tokyo Branch of China-based Bank of Communications and commenced export credit guarantee services in China
September 2014	Arranged the Credit Guarantee 1 fund
April 2015	Arranged the Credit Guarantee 1 fund
December 2017	Established the subsidiary eGuarantee Shared Services to carry out various administrative work
March 2018	Arranged Credit Guarantee 3
May 2019	Arranged the Credit Guarantee 4 fund
June 2019	Capital and business alliance with H.I.S. Impact Finance Co., Ltd., a financial subsidiary of H.I.S. <9603>

Source: Prepared by FISCO from the Company's materials

Consolidated subsidiaries (investment stakes, business content)

Company name	Investment stake (%)	Main business
eGuarantee Solution, Inc.	100.0	Systems development
RG Guarantee, Inc.	80.1	Small-ticket sales credit guarantee service
eGuarantee Shared Services	100.0	Administrative outsourcing services

Note: excluding silent partners
Source: Prepared by FISCO from the Company's securities report

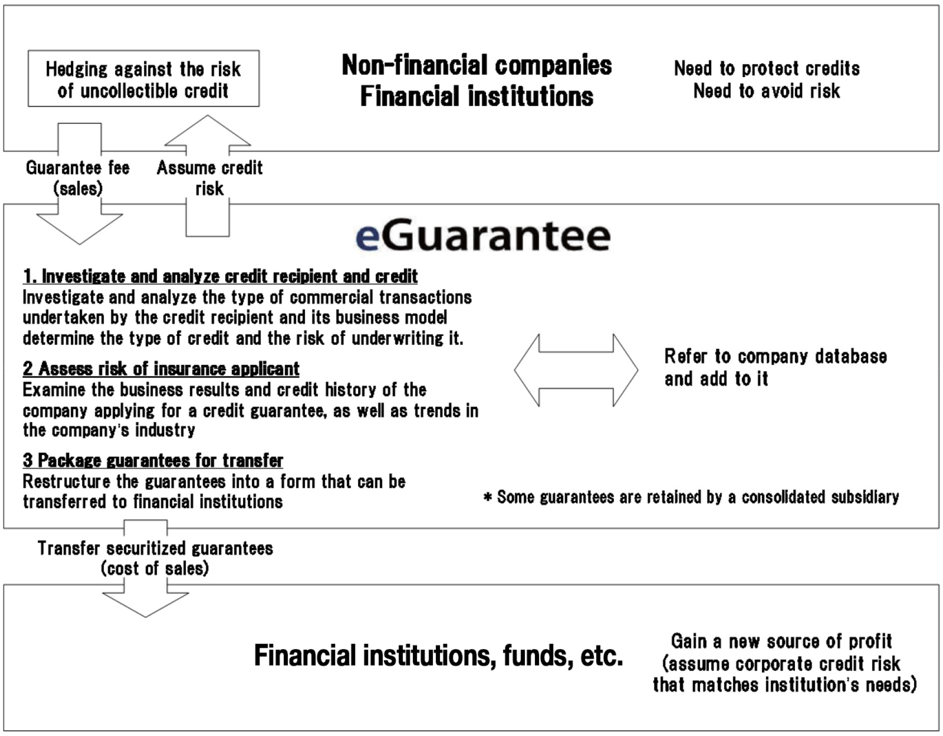
A stock-type business model that accumulates net sales from the "balance of guarantees outstanding x the guarantee fee ratio"

2. Business overview

(1) Description of businesses

eGuarantee's main business is insuring against the sales credit risk arising through transactions among companies. This business is illustrated graphically below.

Business flow



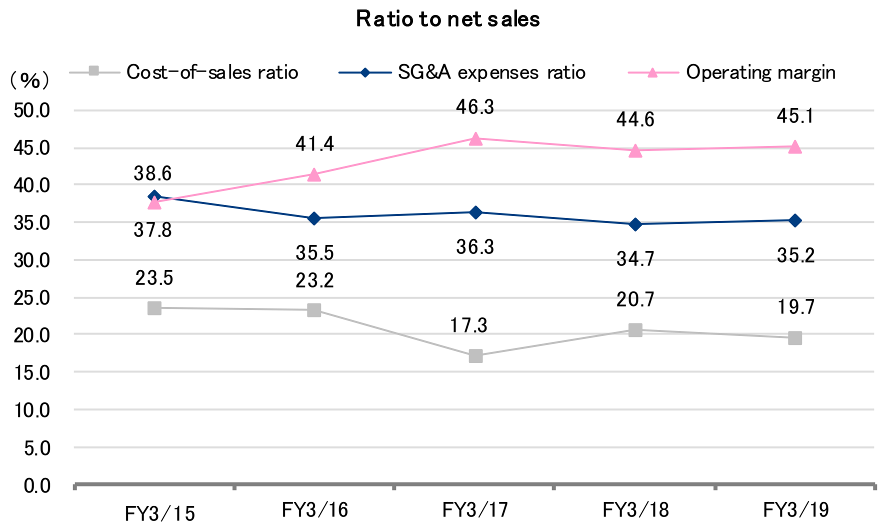
Source: Prepared by FISCO from the Company's securities report

First, eGuarantee and its client company sign a contract by which eGuarantee promises to pay to the client a fixed amount to compensate for a sales credit from transactions with other companies if it should become irrecoverable by paying a guarantee fee to eGuarantee, the client company minimizes its risk of loss from an irrecoverable sales credit. In other words, the client company is able to pay a certain guarantee fee in exchange for minimizing its risk of loss from an irrecoverable sales credit. Most contracts are effective for one year, and the client company pays the entire guarantee fee on the business day before the guarantee start date in principle. eGuarantee divides the sales proceeds into 12 equal monthly installments and records the sales every month, so month-to-month sales fluctuations are relatively small and this functions as a recurring revenue business model.

As eGuarantee's net sales are the product of its balance of guarantees outstanding times its guarantee fee ratio, the key to driving growth in net sales lies in increasing the balance of credit guarantees. eGuarantee refers to various data, including economic indicators published daily, trends in the number of corporate bankruptcies and the probability of credit default based on past experience, and revises guarantee fees every month based on this data. When the number of corporate bankruptcies is decreasing, the credit risk is lower. This means that the guarantee fee ratio will also be set lower. The actual guarantee fee ratio is set for individual contracts and based on the result of eGuarantee's investigations of risk associated with the companies subject to the guarantee. eGuarantee is not bound by industry practice in setting its guarantee fee, but sets a fee that justifies the cost of hedging the risk for the client.

In regard to the credit risk assumed by the Company, eGuarantee packages its guarantees into a portfolio of financial risk products according to risk. It then transfers the guarantees to financial institutions, investment funds and other entities (securitization). Upon the transfer of credit risk, eGuarantee pays guarantee fees and commissions to the entities that accept its guarantee packages. These guarantee fees and commissions constitute the bulk of eGuarantee's cost of sales.

Therefore, eGuarantee's gross margin depends mainly on the spread between the guarantee fee ratio agreed upon by the Company and its clients and the reinsurance fee ratio that applies to fees and commissions paid by the Company to the entities that accept the transfer of credit risk. eGuarantee has been reducing the cost-of-sales ratio by diversifying and upgrading its methods of transferring credit risk to lower the reinsurance fee ratios and by forming funds at a subsidiary to strengthen its ability to undertake risk and shrink the amount of guarantee fees paid to third parties to cut costs. Each fund can accept risk to the scale of 200mn-1,000mn and is funded by the likes of financial institutions. Over the past few years maintenance and improvement of operating performance have become difficult as insurance rates have continued to be ultra-low, but there is strong demand for the funds and the Company has been able to procure funding under favorable terms. It has also benefited from a lower deflation ratio than anticipated. Although the cost of sales ratio has been on a declining trend in recent years. (In the fiscal year ended March 31, 2018 the cost of sales ratio has increased due to the start of middle-risk credit guarantee services.)



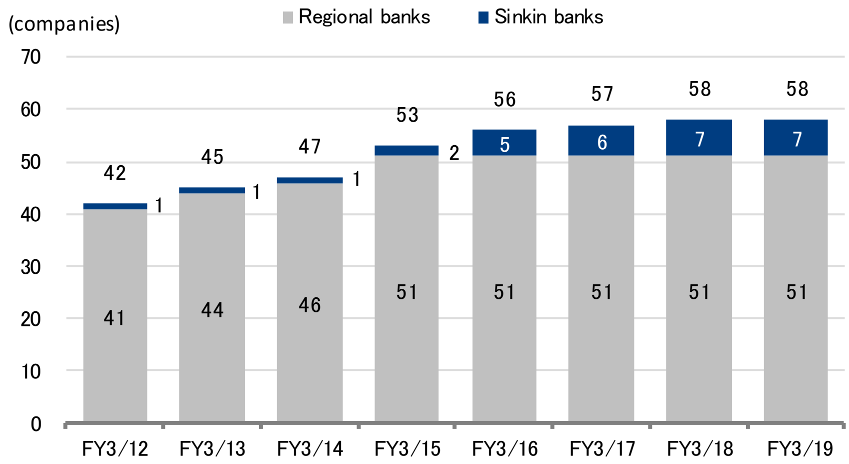
Source: Prepared by FISCO from the Company's financial results

(2) Operational structure

In addition to its head office in Tokyo, eGuarantee has opened branches in Osaka, Fukuoka, Aichi, and Hokkaido in the course of expanding its network across Japan. The Company plans to maintain its current operational structure in terms of its business locations for the time being. Meanwhile eGuarantee has efficiently developed customers by forming business alliances with financial companies, primarily regional banks, trading companies, leasing firms and other partners. In particular, eGuarantee had entered into business alliances with 51 regional banks as of the end of March 2019, establishing an alliance network spanning nearly all of Japan. Looking at the breakdown of the number of customer referrals, referrals from regional banks now account for around 80% of the total, followed by referrals via trading companies and those from other channels. Additionally, eGuarantee has been ramping up business alliances with shinkin banks, which have many local small and medium-sized companies among their customers, since FY3/16 and had alliances with seven shinkin banks at the end of March 2019.

The Company has a total of more than 2,000 customers, ranging from SMEs to major companies, over a wide range of industries, including wholesale, retail, and manufacturing, so its results are not affected by economic fluctuations in specific industries. From these customers, the Company collects information on the companies it will target to screen in its services, and it creates a database of this information. The number of screened companies exceeds 20,000 every month, and it creates a database not only of management information, but also of information such as manager-attributes data and peripheral information, and analyzes the degree of risk and sets the optimum guarantee fee ratio. The database also contains other information, including on the managers' gender, age group, and the evaluation status of external word-of-mouth sites, and finally, it sets the optimal credit guarantee rate taking into consideration factors like the screener's experience. There is no other company that conducts such as thorough analysis to this extent, and it has become one of the Company's strengths.

Number of business partners (regional banks, shinkin banks)



Source: Prepared by FISCO from the Company's materials

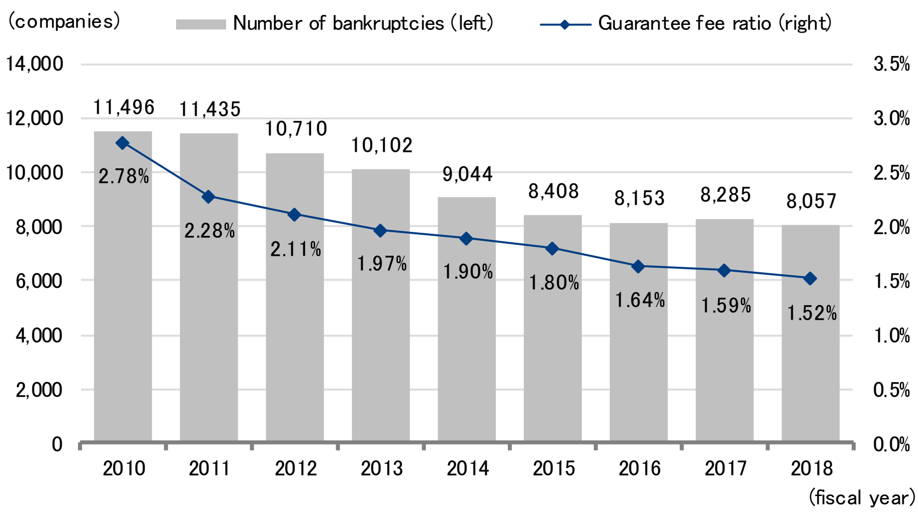
The size of the sales credit market exceeds ¥200tn with robust growth potential

3. Market size

The size of the market for trade receivables (trade notes and accounts receivable) targeted by the eGuarantee's mainstay service is estimated to be more than ¥200tn. While not all of these trade receivables will require credit risk guarantee services, trade receivables guarantee services are used extensively in the US and Europe and have robust growth potential.

In addition, the number of corporate bankruptcies, which has an impact on the guarantee fee ratio, has continued to decline since peaking out in fiscal 2008. In fiscal 2018, the number of corporate bankruptcies decreased 2.8% YoY to 8,057. In addition to the ongoing recovery of the Japanese economy, accommodative loans terms from banks under an ultra-low interest rate policy, and other positive factors form the backdrop to the declining number of corporate bankruptcies. The fewer number of corporate bankruptcies has been accompanied by a decline in the guarantee fee ratio, and the guarantee fee ratio currently dropped to the 1.5% level. A decline in the guarantee fee ratio is a negative factor that pushes down net sales. Meanwhile, considering that a lower guarantee fee ratio also reduces the fees paid to acceptors of securitized guarantees, a decrease in the guarantee fee ratio is a neutral factor that has no impact on the gross margin. During an economic recovery, companies tend to see an increase in the number of their new transaction counterparties in step with sales growth, and tend to generate surplus cash that can be used to hedge the credit risk of sales credits. For these reasons, the balance of credit guarantees outstanding tends to increase in recovery times.

Number of corporate bankruptcies in Japan



Note: Guarantee fee ratio = net sales ÷ (period-start/period-end average balance of guarantees outstanding)
Number of bankruptcies examined by Teikoku Databank
Source: Prepared by FISCO from the Company's materials

4. Risks

We examine the risk factors that should be taken into consideration when looking at eGuarantee's business performance. The following are the three primary risks that could affect the Company's business results. However, we believe that these risks do not present major concerns at this time.

(1) Profit-structure risk

The Company's profit structure is that it records as net sales the guarantee fees it receives from customers, and it records as costs of sales the payments to financial institutions and others that transfer risk to it, with the difference between these two amounts being the Company's profits. The payments to the customers that transfer risk to it are determined by the track record in executing guarantees over several years, so even if it temporarily incurs large costs from the execution of guarantees, this will not become a factor causing costs to rise in the short term. However, during a period in which the execution of guarantees continues to occur frequently, such as during an economic recession, the risk-transference cost rises. If the Company cannot transfer this rise in the risk-transference cost to the prices of guarantee fees, it becomes a factor causing profitability to deteriorate. Also, on the one hand it is possible that demand for the Company's services will increase during an economic recession due to the rise in the risk of bankruptcy, but on the other hand, it also considered possible that the balance of guarantees outstanding will decrease due to a decline in the number of contracts from a rise in the guarantee fee ratio and a fall in the contract-renewal rate. There is also the risk that the Company will be unable to execute guarantees during an unprecedented economic recession in the event of the management collapse of the financial institutions and others that transfer risk to it.

(2) Competition risk

There are hardly any other companies like the Company that specialize in providing sales credit guarantee services, but there are factoring companies affiliated to major financial institutions that provide guarantee factoring as a similar service, and also property insurance companies that provide transaction credit insurance and other such services. However, in terms of the scope of the companies that are targets of the guarantees, the guarantee-limit amount, and the credits targeted, the Company's strengths include that it is able to respond flexibly to diverse customer needs, so at the present time it is considered to have almost no competition risk. However, if in the future, financial institutions or other companies develop the same services as the Company and launch businesses, thereby causing competition to intensify, its profitability may decline. The Company does face some competition from a small-scale provider of a small-ticket sales credit guarantee service, of RACCOON FINANCIAL, Inc., which is a subsidiary of RACCOON HOLDINGS, Inc. <3031>. But small-ticket sales credit guarantees constitute only a small percentage of the Company's total business, so this competition has hardly any effect on it.

(3) Legal-regulations risk

Credit risk guarantee services are not subject to legal regulations, such as the Insurance Business Act and the Financial Instruments and Exchange Act. However, if in the future legal regulations relating to these services are newly enacted, this may affect the Company's results, such as changing its business model or changing the competitive environment.

Financial results

Met the needs of major companies working on “work style reform” to once again achieve record high results

1. Summary of FY3/19 results

In the FY3/19 consolidated results, net sales increased 9.2% YoY to ¥5,573mn, operating profit rose 10.4% to ¥2,512mn, recurring profit grew 10.8% to ¥2,552mn, and net profit attributable to owners of parent increased 12.5% to ¥1,651mn, and the results were once again record highs. The main reasons for the higher sales and profits were the acquisitions of new customers via its partner financial institutions, and also that contracts with major companies increased. Therefore, the balance of credit guarantees steadily grew, up 12.6% on the end of the previous fiscal year to ¥388.7bn.

The number of corporate bankruptcies declined and the average guarantee fee ratio fell more than expected, so net sales were 2.2% below the initial forecast. However, both operating profit and recurring profit were basically as the Company forecast, as the sales-costs ratio declined 1.0 percentage point (PP) YoY, including due to the rise in the percentage of claims targeted for guarantees in the low-risk zone, and also as SG&A expenses were less than expected.

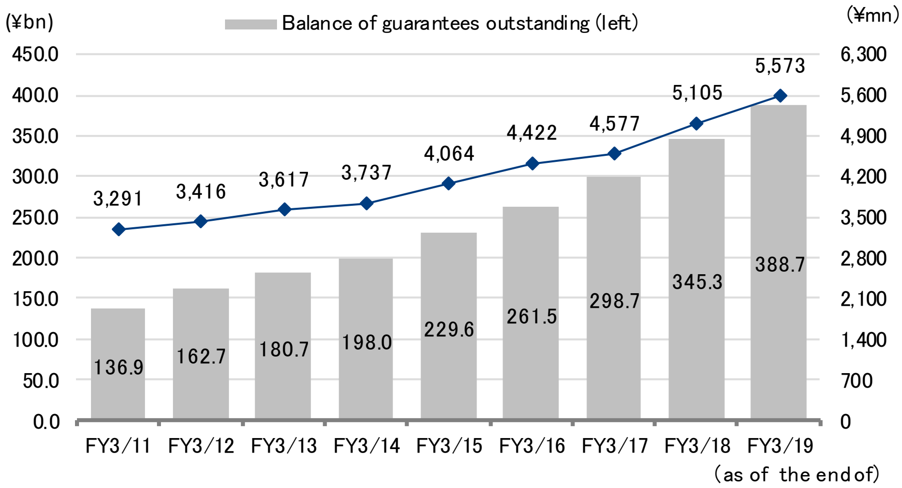
Consolidated financial results for FY3/19

(¥mn)

	FY3/18		FY3/19				
	Results	Ratio to net sales	Forecasts	Results	Ratio to net sales	YoY change	vs. forecast
Net sales	5,105	-	5,700	5,573	-	9.2%	-2.2%
Cost of sales	1,056	20.7%	-	1,098	19.7%	4.0%	-
SG&A expenses	1,772	34.7%	-	1,962	35.2%	10.7%	-
Operating profit	2,276	44.6%	2,510	2,512	45.1%	10.4%	0.1%
Recurring profit	2,302	45.1%	2,550	2,552	45.8%	10.8%	0.1%
Net profit attributed to owners of parent	1,468	28.8%	1,620	1,651	29.6%	12.5%	2.0%

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

Balance of credit guarantees outstanding and net sales



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

In particular, in the current fiscal period, the Company strengthened consulting sales to major companies that are working to "reform ways of working," which contributed to the growth of the balance of credit guarantees. Specifically, it proposed to its customer companies that they reduce the costs of the credit management work for their client companies (small-scale transaction client companies) that they conduct in-house by using the Company's sales credit guarantee services, and this led to new contracts. For example, in the event that the bad debt rate among 1,000 client companies with sales credits of less than ¥5mn is 0.2%, the annual credit loss would be ¥20mn. In order to carry out credit management for these 1,000 companies, usually 4 to 5 specialist staff would be required for annual personnel costs of around ¥30mn. In other words, the credit management costs for the 1,000 client companies, including the bad debt loss, would be ¥50mn. But the Company proposed reducing this to around ¥40mn by using its sales credit guarantee services.

For customer companies, this not only reduces costs, but also enables them to allocate the four or five staff that would have conducted this work to more productive work, and therefore in the last few years an increasing number of major companies have been introducing this service. The Company does not disclose the balance of credit guarantees according to the sizes of customers, but it seems that while the percentage provided by major companies was only about 10% 5 years' ago, recently this has risen to around 30%. These companies have a larger guarantee fee per contract, so this trend can be said to be having a large positive effect on results.

In this fiscal period, the Company newly entered into a business alliance agreement with RICOH LEASING COMPANY, LTD., (October 2018). RICOH LEASING will provide a customer referral service for the Company's sales credit guarantee services. Through this alliance, RICOH LEASING's 6,000 vendor companies and approximately 400,000 client companies will become potential customers for the Company's services. Although there are hardly any sales results as yet, the Company expects that it will lead to referrals of SMEs in city centers.

Is financially sound and building a business model that is highly profitable and stable

2. Financial conditions and indicators

Looking at the financial condition at the end of FY3/19, total assets were up ¥2,058mn on the end of the previous fiscal year to ¥16,427mn. The main change factors were that in current assets, cash and deposits increased ¥1,018mn alongside the growth in earnings, while in non-current assets, investment securities rose ¥397mn and tangible non-current assets grew ¥383mn (of which, ¥250mn was to acquire land for Company housing).

Total liabilities were up ¥537mn on the end of the previous fiscal year to ¥5,350mn, due to deposits increasing ¥559mn following the sales of shares held in the Employee Stock Ownership Plan (ESOP) Trust. Also, net assets were up ¥1,520mn on the end of the previous fiscal year to ¥10,960mn. This was because retained earnings increased ¥1,177mn, and also as treasury shares decreased ¥71mn (an increase factor) following the sale of shares in the ESOP Trust, and because capital and the capital surplus both rose ¥115mn due to the exercising of stock options.

Looking at the financial indicators, the equity ratio, which is an indicator of financial stability, increased 1.7 PP on the end of the previous fiscal year to 59.7%, and as the Company is practicing debt-free management, the level of cash and deposits is increasing by more than ¥9bn each year, and it can be judged to be highly financially sound. Looking at the indicators of profitability as well, the operating profit margin is 45.1%, which is a high level of profitability is being maintained, and although both ROA and ROE declined slightly YoY, they are being maintained in the 16% to 19% range. So a feature of the Company is that it is both highly profitable and financially stable.

Consolidated balance sheet and indicators

(¥mn)

	FY3/16	FY3/17	FY3/18	FY3/19	YoY
Current assets	7,443	8,809	10,828	12,036	1,208
(Cash and deposits)	5,403	6,627	8,453	9,471	1,018
Fixed assets	3,202	2,924	3,540	4,390	850
Total assets	10,645	11,733	14,368	16,427	2,058
Current liabilities	3,389	3,342	4,812	5,350	537
(Advances received)	2,233	2,389	2,549	2,647	97
Fixed liabilities	146	115	115	115	-
Total liabilities	3,536	3,457	4,928	5,466	537
(Interest-bearing debt)	70	5	-	-	-
Equity capital	6,031	7,092	8,331	9,810	1,478
Share capital	1,481	1,515	1,528	1,643	115
Capital surplus	891	925	938	1,053	115
Retained earnings	3,905	4,889	5,936	7,114	1,177
Treasury shares	-246	-238	-71	0	71
Stock acquisition rights	27	72	85	117	31
Equity attributable to noncontrolling interests	1,050	1,110	1,023	1,033	9
Net assets	7,109	8,275	9,440	10,960	1,520
(Stability)					
Equity ratio	56.7%	60.4%	58.0%	59.7%	1.7pt
Interest-bearing debt ratio	1.2%	0.1%	-	-	-
(Profitability)					
ROA	18.3%	19.2%	17.6%	16.6%	-1.0pt
ROE	19.9%	20.4%	19.0%	18.2%	-0.8pt
Operating margin	41.4%	46.3%	44.6%	45.1%	0.5pt

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

Business outlook

Is focusing on providing risk hedging services to FinTech-related companies, and the outlook is for the higher sales and profits to continue in FY3/20 also

1. FY3/20 outlook

The outlook for the FY3/20 consolidated results is for net sales to increase 11.2% YoY to ¥6,200mn, operating profit to rise 7.5% to ¥2,700mn, recurring profit to climb 7.7% to ¥2,750mn, and net profit attributable to owners of parent to grow 33.2% to ¥2,200mn. While the effects on corporate earnings are starting to appear of the prolonging of the trade friction between the US and China and the slowdown of the Chinese economy, it is considered that under such market conditions, the need for risk hedging, such as for sales credits, actually grows stronger, and the Company's policy is to continue to actively undertake risk to meet this need among its customers. In May 2019, it newly established Credit Guarantee 4 (silent partner) as a subsidiary (50% ownership ratio) in order to strengthen its ability to undertake risk, and the period-end guarantee balance is forecast to grow by 10% to 15% on the end of the previous fiscal year, the same as previously. Although the net profit increase rate grew larger, this was due to a decrease in corporation tax alongside the ESOP Trust distribution (which is included in deductions).

Consolidated results outlook for FY3/20

(¥mn)

	FY3/19		FY3/20		
	Results	Ratio to net sales	Forecasts	Ratio to net sales	YoY change
Net sales	5,573	-	6,200	-	11.2%
Operating profit	2,512	45.1%	2,700	43.5%	7.5%
Recurring profit	2,552	45.8%	2,750	44.4%	7.7%
Net profit attributed to owners of parent	1,651	29.6%	2,200	35.5%	33.2%
Dividend per share (¥)	39.11		51.76		

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

2. Key policies

The Company is working on two key policies for FY3/20; "improving the renewal rate and supplementing sales resources" and "providing risk hedging services to FinTech-related companies. "

(1) Improving the renewal rate and supplementing sales resources

In order to improve the contract-renewal rate, the Company has newly created a specialist, contract-renewal team with the aim of improving the renewal rate through improving customer satisfaction. At the same time, its strategy is to stimulate potential demand through providing proposals to existing customers that envisage various guarantee-utilization scenes, which will lead to an expansion in the guarantee scale per customer.

In addition, it is aiming to secure sales resources through improving customer satisfaction and reducing administrative work by shifting its existing customers' contract administrative work to online and realizing labor saving. Moreover, it is aiming to construct a credit management portal site through which it expects to connect with customer companies and others, and it intends to develop this site to be a foundation on which to provide new services.

The number of employees was around 180 people at the end of FY3/19, including approximately 70 in the sales department. It recruited 20 new graduates in April 2019 and intends to recruit around the same number in 2020 also.

(2) Providing risk hedging services to FinTech-related companies

In recent years, there have been a growing number of start-up companies and financial institutions that offer new services utilizing FinTech, such as credit sales companies that conduct small-lot payments for corporate customers, and companies that provide payroll third-party payment services. The Company is providing risk hedging services to these companies.

As a specific example of the introduction of its services, the Company is providing a hedging service for the risk of non-collection of the payroll third-party payment part for companies providing a payroll third-party payment service. Payroll third-party payment services are increasingly being introduced by companies, such as those that utilize part-time workers and by temporary staffing companies, with the aims of securing human resources and improving the employee retention rate. Therefore, the need for the Company's services is expected to increase in the future.

The Company is also providing a service to hedge the risk of the uncollected part of payments for companies providing payment agency services. Particularly in the last few years, against the backdrop of the spread of the Internet, the number of SMEs, venture companies, and other companies that make Internet payments has been rising. So the market for online payment agency services is also growing rapidly and the number of participating companies is increasing.

The Company intends to further grow its guarantee balance by meeting needs for risk hedging that will arise alongside this expansion of the FinTech market.

Aiming for consolidated recurring profit of ¥5bn as the medium-term target

3. The medium-term target

As its medium-term management target, the Company is aiming for consolidated recurring profit of ¥5bn. In terms of the standard to achieve this target, the balance of guarantees outstanding must approximately double the current amount to approximately ¥700bn to ¥800bn. If growth continues at around the current pace of around 10% to 15%, then the prospect is that it will be able to achieve this target in FY3/24.

In order to grow the guarantee balance, it will be important to acquire customers, such as major companies and FinTech-related companies, and to increase the guarantee amount per customer through supplementing sales resources, as previously mentioned. It is also considered that the Company will be able to grow the guarantee balance even if it expands the scope of the targeted credits (to middle risk and various credits other than sales credits*).

* Small-ticket credits, purchase credits, special credits, loan credits, long-term bonds, etc.

In addition, about 80% of new customers are currently referred to it from regional banks, but the earnings environment is becoming severe even for these banks. In this situation, there are appearing banks that are actively implementing measures such as developing their own services in combination with the Company's services. Specifically, in April 2019, the Hiroshima Bank <8379> started offering the Hirogin Sales Expansion Support Loan service, which is a product that packages a loan and the Company's sales credit risk consulting service*. As a measure against the risk of bankruptcy at sales customers, which has become a problem for the expansion of sales channels by SMEs, the aim is to promote financing and to support sales growth in companies in Hiroshima Prefecture through combining a loan with the Company's service. In particular, many local companies are conservative, and therefore many of them are also cautious about bad debt risk. So by utilizing the Company's sales credit guarantee service as the trigger for the use of this product, the banks are able to actively advance customer acquisition. It is expected that the Company's guarantee balance will grow even more if a similar development spreads to other banks in the future.

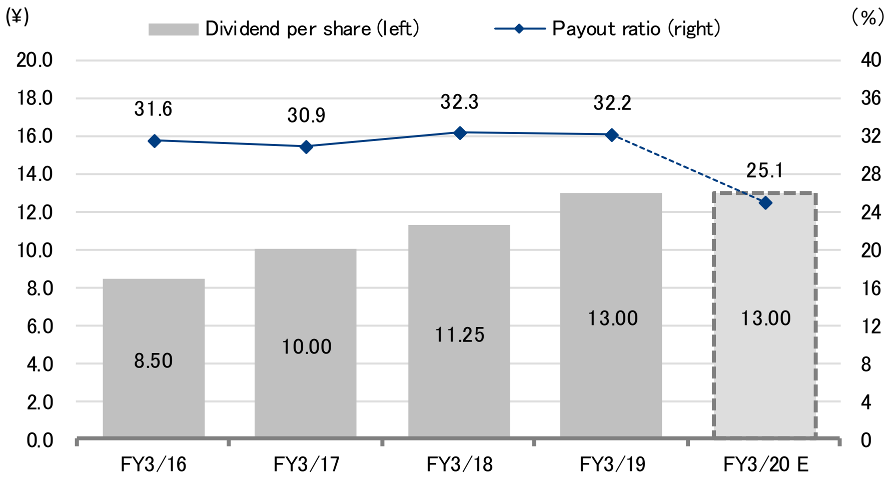
* The content of sales credit risk consulting is a service to provide a report on the portfolio analysis of the seller requested by the use company (three times a year), to calculate the theoretical damage estimate based on the amount of the transaction with the seller and management information, and to provide advice based on simulations of how the estimated loss will change, such as due to the shortening of payment terms. Also, if the use company wants support for specific measures, the Company will separately contract with it for sales credit guarantee services.

Shareholder return policy

Is continuously increasing dividends, targeting a dividend payout ratio of 30%

The Company's basic dividend policy is to pay dividends in line with earnings while also considering supplementing the internal reserves it needs to strengthen its financial structure and to actively develop its business. The standard for the dividend payout ratio is around 30%. Looking at the trend up to the present time, since the Company starting paying dividends in FY3/09, it continuously and consecutively increased it up to FY3/19, and it has expressed its intention to continue to increase the dividend in the future also, if the profit growth is maintained as planned. In FY3/20, it plans to pay a dividend of ¥13.0 (dividend payout ratio, 25.1%), which is unchanged YoY. But at FISCO, we think that it is highly possible it will increase it, if the results achieve their forecasts. In addition, the Company has a shareholder gift program. Specifically, eGuarantee uniformly awards a QUO card worth ¥1,500 to each shareholder who holds 100 or more shares at the end of March every year.

Dividend trend



Note: The Company implemented 2-for-1 stock splits in March and August, 2018. The dividend was adjusted retroactively.
Source: Prepared by FISCO from the Company's financial results

Information security

As the Company handles information on its customer companies and others through its guarantee service business, it is aware that information security measures are an important management issue. Therefore, it is taking various steps to ensure information security, including updating to the latest security software, restricting access to the information management system according to the person in change and the managerial position, and providing education and training on information management.

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