COMPANY RESEARCH AND ANALYSIS REPORT

FUJI SOFT INCORPORATED

9749

Tokyo Stock Exchange First Section

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Summary

A major independent IT solutions vendor that celebrated the fifty-year anniversary of its establishment in 1970
Realized YoY double-digit increases in operating income and profit margin in FY12/20 even during the coronavirus pandemic

1. Company outline and business description

FUJI SOFT INCORPORATED <9749> (hereinafter, "the Company") is a major, independent IT solutions vendor established in May 1970. It has its roots in FUJI SOFTWARE LABORATORY, Ltd., which was established at the home of Mr. Hiroshi Nozawa, the Company's current Director and Executive Adviser, and two other employees. Today, half a century after this establishment, the Company has grown into a group with 28 consolidated subsidiaries, 2 equity-method non-consolidated subsidiaries, and 2 equity-method affiliates, with over 14,000 employees (as of December 31, 2020).

The Company has three reporting segments: the SI (systems integration) Business (system construction and product service), the Facility Business, and Other Businesses. In the mainstay SI Business, it provides a diverse solutions menu, centered on the development of embedded / control software and operations software. The Facility Business entails rentals of office buildings, while Other Businesses includes a BPO (business process outsourcing) services business, a contact center business, and a regenerative medicine business.

2. Its core competencies are "superiority in technologies and deep customer insight"

The Company lists its "continually advancing superiority in technologies and deep customer insight" as the reasons why it is chosen by customers. It is highly confident in its core competencies of advanced technological expertise acquired through the development of embedded / control software that requires extremely high levels of precision, such as for vehicles and semiconductor manufacturing equipment; systems construction capabilities cultivated through the solutions it has provided to a wide range of industries; and "superiority in technologies and deep customer insight" which it demonstrates in aspects such as its ability to provide flexible proposals as an independent solutions provider.

3. In the recovery period following the 2008 financial crisis, strengthened both its financial structure and growth potential

Although the Company's sales peaked before the economic downturn precipitated by the 2008 financial crisis (FY3/06), it set a new record high for sales in FY12/17. Therefore, while it actually took more than 10 years to renew its peak sales, the Company can be highly evaluated for not only recovering non-recurring revenue, but both working to strengthen its financial structure and growth potential in that time.

Specifically, the Company realized soundness of major financial indicators, with the equity ratio rising from 47.3% at the end of FY3/06 to 59.9% at the end of FY12/17, the current ratio from 96.4% to 184.9%, and net interest-bearing debt (interest-bearing debt – cash and deposits) of ¥21,295mn to excess cash of ¥6,204mn. Based on this, from FY12/15 onwards it conducted major recruitment, mainly of new graduates, multiplying the number of consolidated employees by 1.4 from 9,415 to 13,556. The percentage of certified technicians on a stand-alone basis (the percentage of specialists and project managers certified according to the Company system out of the total number of employees) also rose from 22.8% at the end of FY12/14 to 30.1% at the end of FY12/20. From this, we can see that growth potential from a human resources angle has been enhanced both in terms of quantity and quality.

As a result of the above, subsequently through FY12/19, the Company continuously achieved year-on-year (YoY) double-digit increases in sales and profits. Even in FY12/20 during the coronavirus pandemic, it secured a 4.3% increase in net sales and realized a 20.4% increase in operating income. The financial indicators deteriorated in FY12/20, with the equity ratio at 50.7% (down 3.4 percentage points (pp) compared to the end of the previous fiscal year) and the current ratio at 153.3% (down 29.6%). However, this was due to the Company's financial strategy based on the impact of the coronavirus pandemic (accumulate cash and deposits through short-term fund raising and repay long-term borrowings), and should not be considered a major cause for concern. In fact, net interest-bearing debt decreased ¥1,157mn from the end of the previous fiscal year to ¥6,341mn and the Company maintained its sound financial structure. Additionally, in terms of human resources, it has 14,422 consolidated employees, while the percentage of certified technicians on a stand-alone basis is 32.0%.

4. The FY12/21 consolidated results forecasts are for net sales to increase 3.3% YoY and operating income to rise 2.1%

For the FY12/21 consolidated results, the Company is forecasting net sales to increase 3.3% YoY to ¥249,000mn, operating income to rise 2.1% to ¥16,300mn, ordinary income to grow 3.4% to ¥16,900mn, and profit attributable to owners of parent to increase 3.8% to ¥8,900mn. Therefore, it is actually forecasting the eighth consecutive period of higher sales and operating income since 2013 when it transitioned to a fiscal period ending in December.

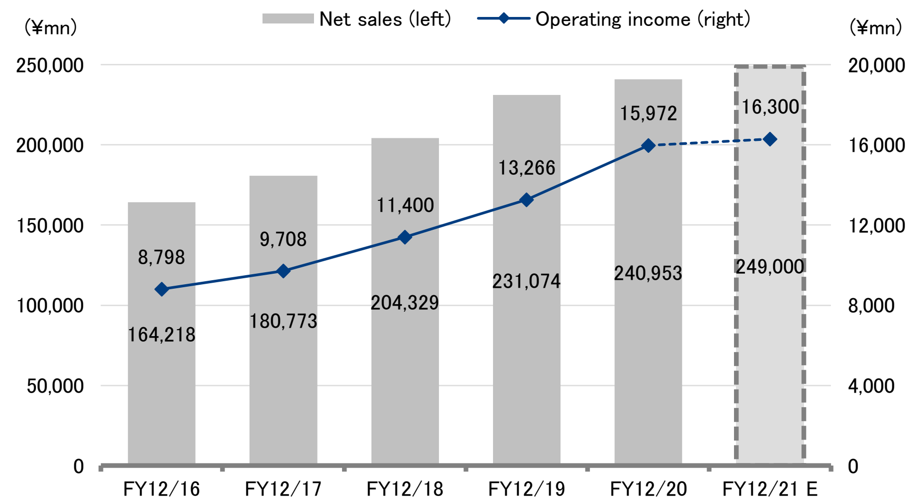
Although these results appear unsatisfactory compared to the FY12/20 results when profits increased by double digits, the Company has continued with a pattern of setting initial forecasts assuming that sales will increase by around 3% and an operating income margin on par with the results of the previous fiscal period since FY12/15. Therefore, these Company forecasts are also considered to be positioned as the minimum amounts to be achieved and do not need to be viewed negatively.

For FY12/20, the Company forecast an annual dividend of ¥50 per share (¥25 per share at the end of 2Q, ¥25 per share at the end of the fiscal year) compared to the FY12/20 annual dividend of ¥51 per share (¥28 per share at the end of 2Q, including a commemorative dividend of ¥5 to mark the 50th anniversary of the foundation, and ¥23 per share at the end of the fiscal year). Although this appears to be the first dividend decrease in six years, after excluding the commemorative dividend it is actually an increase of ¥2 per share as the total of the interim and period-end dividends. Additionally, the Company has upwardly revised the period-end dividend from the initial forecast for four consecutive fiscal periods from FY12/16 to FY12/19 based on the fact that the full fiscal year results exceeded the forecasts, so we shall be paying attention to how it responds in FY12/21.

Key Points

- A major, independent IT solutions vendor established in 1970. Its active investment in human resources and a complementary M&A strategy are proving successful, and it has exceeded the ¥100bn barrier for net sales. At the end of December 2020, it had over 14,000 consolidated employees.
- Its core competencies are "superiority in technologies and deep customer insight," as seen in its abundant track record and corporate philosophy. Although results stagnated for a period after the economic downturn precipitated by the 2008 financial crisis, it has strengthened its financial structure and growth potential and is continuing "Challenges and Creation" while aiming to be an innovative corporate group.
- FY12/20 results exceeded the Company's initial forecasts for the fifth consecutive year. For the FY12/21 full year results, is forecasting higher net sales and operating income for the eighth consecutive period in real terms.

Results trends



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

Company overview

Based on its corporate motto of "Challenges and Creation," broke through the barrier of net sales of ¥200bn, while remaining independent. Even during the coronavirus pandemic, is continuing a growth-oriented management strategy while preparing for unforeseen situations

The Company is a major, independent IT solutions vendor established in May 1970. It has its roots in FUJI SOFTWARE LABORATORY, Ltd., which was established at the home of Mr. Hiroshi Nozawa, the Company's current Director and Executive Adviser, who at that time was a teacher in a computer vocational school and started a business focusing on the prospects for the computer industry with two other employees who had previously been his students. Today, half a century after this establishment, the Company has grown into a group of 30 consolidated subsidiaries (of which, 4 are listed companies), 2 equity-method non-consolidated subsidiaries and 2 equity-method affiliates, with over 15,000 employees.

Even while achieving rapid development in terms of size, the Company, in accordance with its basic philosophy of "Being a corporate group that is more useful for society, makes customers more happy, and that is more considerate to the Earth, and that provides 'relaxed and worthwhile' work environments," has consistently conducted the enlightened management that its founder aimed for to contribute to society through business, and aims to give shape to the knowledge expressed by its corporate philosophy, such as through the Group's corporate charter and standards of conduct for executives and employees.

The Company has been moving ahead with a strategy of making both the parent company and subsidiaries listed, and currently has four listed subsidiaries. Although the Group Company Charter states that "each company shall mutually respect the others as independent companies and shall prioritize independence and autonomy," there is a tendency to point to governance issues when listing both the parent and the subsidiaries in capital markets. However, the fact that the business companies do not only have a presence in the capital markets and that they face severe competition in the product and services markets and the labor market is extremely important. When comprehensively weighing the advantages and disadvantages for each market, the degree of satisfaction with the Company's strategy of listing the parent and subsidiaries is considered to be fairly high at the current time.

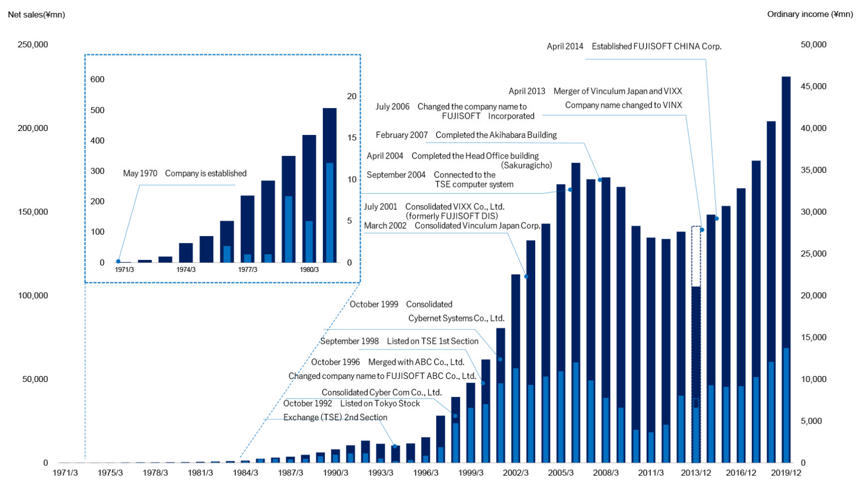
The Company has three reporting segments: the SI Business (systems construction and products and services), the Facility Business, and Other Businesses. In the mainstay SI Business, it provides a diverse solutions menu, centered on the development of embedded / control software and operations software. The Facility Business entails rentals of office buildings, and Other Businesses includes a BPO service business, a contact center business, and a regenerative medicine business.

In addition, as a business strategy to be implemented across the reporting segments, the Company is advancing initiatives in the "AIS-CRM" area. AIS-CRM, which is the Company's own unique acronym created by taking the first letters from AI, IoT, Security, Cloud computing, Robot, Mobile & AutoMotive, covers areas that are expected to grow in the medium- to long-term. While it will not be easy to accumulate and refine technologies in these growth fields, if the Company can achieve this, it may be able to curb the rapid fluctuations in utilization rates caused by the economic cycle. Among its past initiatives, the Company appears to feel confident about the results it has accumulated in the cloud computing and mobile fields. We would like to keep an eye on future developments.

At the time it was established, the Company's business was founded on the dispatch of computer operators. Subsequently, it entered into the software development and systems construction businesses and achieved rapid development supported by the explosive expansion of the computer industry. But what should not be overlooked as a factor behind this growth is the strong belief of the executive management, including Hiroshi Nozawa, a Director and Executive Adviser who founded the Company, that the time of the computer-dominated society had arrived. While bearing a considerable risk, the Company actively invested in recruiting and training engineers and pursued a complementary M&A strategy to incorporate the technologies and customer bases it did not have.

Even though the computer-dominated society has become a reality and the domestic IT services market has expanded in scale to be worth over ¥6tn, the major IT services companies with sales of more than ¥100bn are comprised almost entirely of manufacturers (such as Fujitsu Ltd. <6702>), user-related companies (such as NTT DATA Corporation <9613>), trading companies (such as SCSK Corporation <9719>), and foreign-owned companies (such as IBM Japan, Ltd.) Including the Company, there are only three companies that could be called independent. Although it has succeeded at becoming one of the groups with over ¥100bn in net sales in FY3/02, looking at the number of employees to achieve this, which is 4,002 people on a stand-alone basis and 6,353 on a consolidated basis, we can see that its business expansion has been supported by its active recruitment of human resources and training of engineers since its establishment. Additionally, in 1996, it merged with ABC Co., Ltd., which has strengths in finance-related operations systems, and subsequently also made consolidated subsidiaries of Cybernet Systems Co., Ltd. <4312>, which has its origins in an overseas company in 1999, and MYCAL Systems Corp. (currently VINX Corp. <3784>), whose main business is distribution-related business systems, in 2002. In such ways, the Company has advanced an M&A strategy to incorporate the technologies and customer bases to supplement its strengths in embedded /control software development. It is thought that it would not have been able to exceed net sales of ¥100bn solely from riding the favorable external wave, but that its bold decision making has also been vital to achieving this. Then, in FY12/18, the Company surpassed the major milestone of net sales of ¥200bn, and is forecasting net sales of ¥240.9bn in FY12/20. Therefore, despite being in the middle of the coronavirus pandemic, the Company is expecting to set a record high in net sales for the fourth consecutive fiscal year.

Since its establishment in May 1970, the Company's size has expanded dramatically



*The graph of the dotted line shows the results of the year from January, 2013 to December, 2013.

Source: From the Company's 2020 FACT BOOK

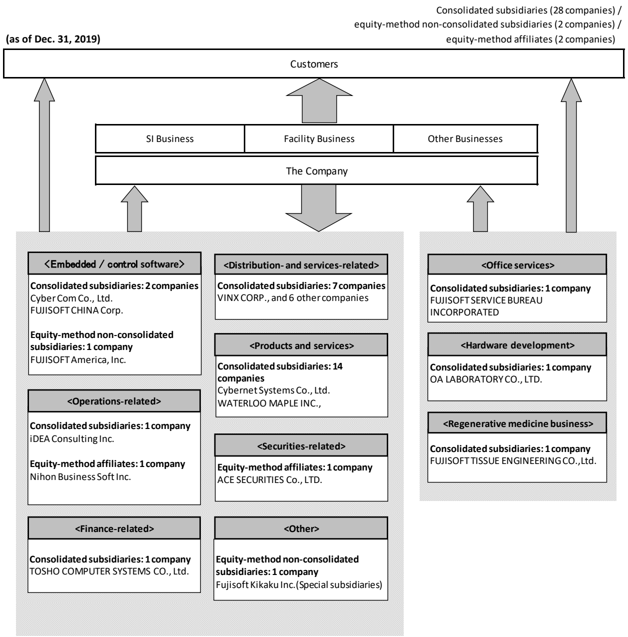
With "superiority in technologies and deep customer insight" as its core competencies, the Company is aiming to be a CSV-style innovative corporate group

The Company lists its "continuously advancing superiority in technologies and deep customer insight" as the reasons why it is chosen by customers. It is highly confident in its core competencies of "continuously advancing superiority in technologies and deep customer insight" which it demonstrates in aspects such as its advanced technological expertise acquired through the development of embedded / control software that requires extremely high levels of precision, including for vehicles and semiconductor manufacturing equipment; its systems construction capabilities cultivated through the solutions it has provided to a wide range of industries; its ability to provide flexible proposals as an independent solutions provider; and its construction of a network of bases close to customers (42 bases in Japan + a global network). In addition, the Company believes that its key mission is to further societal development through various corporate activities, alongside sustainable growth and the creation of corporate value in the medium to long term. As its medium-term policy, it aims to be "an innovative corporate group that links ICT development to improving value for our customers."

From the messages disseminated by the Company, what stands out are the strong belief in the effectiveness and potential of utilizing ICT and its sense of mission to advance this and a customer-oriented and CSV-type (a company that increases enterprise value through social contributions via its businesses) management policy. Naturally, corporate activities will have CSV-type aspects to a greater or lesser extent, even if the company itself is unaware of this. But in the Company's case, the fact that the founder's strong intentions, based on the corporate motto of "Challenge and Creation," have been incorporated into its corporate culture is worthy of note.

One of the Company's unique initiatives as a CSV-type company is the All Japan Robot-Sumo Tournament, which it has held continuously since 1990. Although the tournament began with the aim of providing a place to experience the enjoyment of building things and to improve technologies through building robots, it is currently recognized as an excellent example of support for developing human resources through manufacturing. For example, since a division for high school students was established in 1993, the National Association of Principals of Technical Senior High Schools has joined the operation, and organizations including the Ministry of Education, Culture, Sports, Science and Technology (MEXT), and Ministry of Economy, Trade and Industry (METI) are also listed as sponsors. Although the Robot Sumo Tournament and the Robot American Football Tournament, which were scheduled for 2020, were called off due to the coronavirus pandemic, the Company is currently putting its best efforts into resuming activities with safety as the first priority.

Business structural diagram



Source: From the Company's securities report

Business overview

Offering varied ICT services and products through "Challenge and Creation"

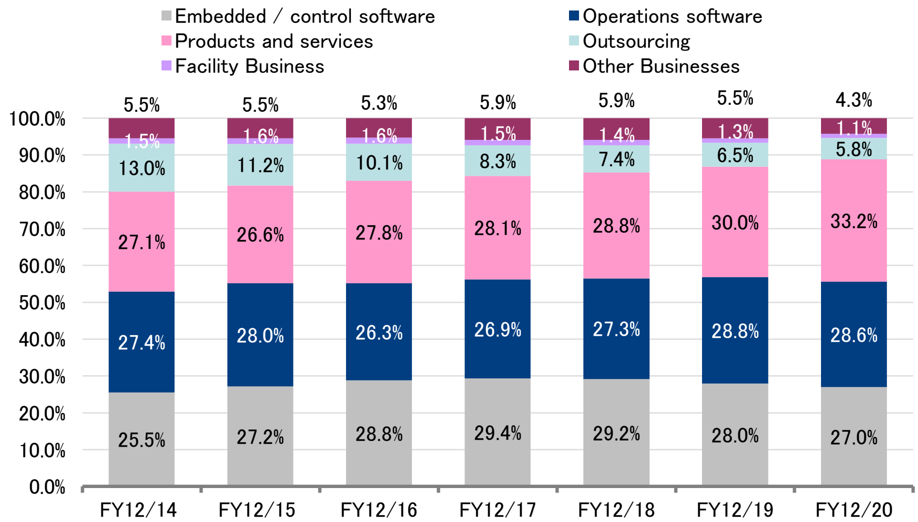
The Company has three reporting segments; the SI Business, the Facility Business, and the Other Businesses. The mainstay SI Business is broadly divided into systems construction, and products and services. Further, systems construction is subdivided into embedded / control software and operations software, while products and services are subdivided into narrowly defined products and services, and outsourcing. In addition, the Facility Business entails rentals of office buildings, while Other Businesses includes the BPO service business, a contact center business, and a regenerative medicine business.

Segment breakdown

Segment name				Breakdown
SI Business				
	Systems construction			
		Embedded / control software		
			Machine control systems	Embedded / control software such as FA, OA, digital home appliances
			Automotive-related	Automotive-related embedded / control software
			Mobile-related	Embedded / control software for mobile devices, etc.
			Social infrastructure-related	Embedded / control software for communication control (switches, routers, etc.), base stations, aerospace and defense, etc.,
		Operations software		
			Financial industry	Operations software for financial companies (life insurance, credit cards, securities companies, banks, etc.)
			Distribution and services	Operations software for distribution-related companies (retail, wholesale, trading companies, real estate, construction industry, etc.)
			Manufacturing industry	Operations software for manufacturing
			Other operations-related	Operations software that does not correspond to the above fields
	Products and services			
		Products and services		Products and services of the FUJISOFT Group and of other companies based on strategic partnerships
		Outsourcing		Data center business, systems maintenance operations, etc.
Facility Business				Sales related to the real estate rentals business
Other Businesses				Office services, hardware development, regenerative medicine business

Source: From the Company's results briefing material

Trends in percentages of total net sales by segment



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

1. Mainstay embedded/control software

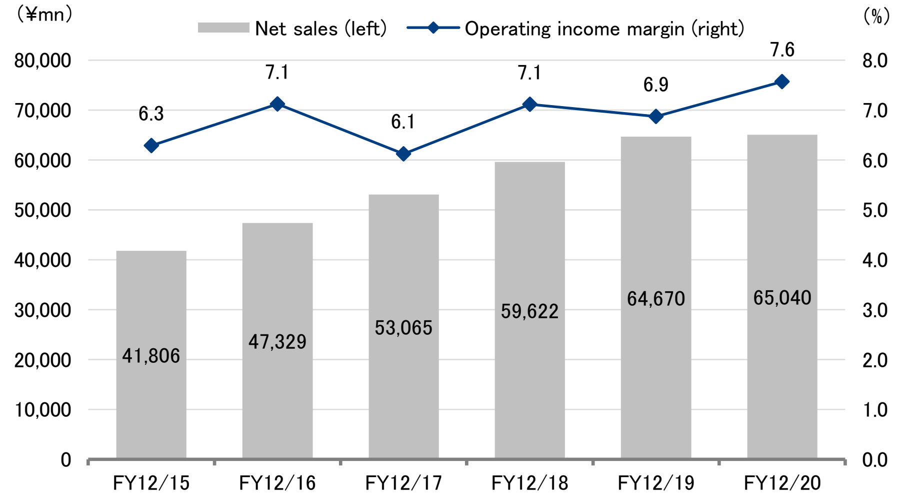
Embedded / control software, which belongs to the systems construction category in the SI Business, accounted for 27.0% of Company-wide sales (FY12/20) and 30.8% of operating income, and the segment profit margin exceeded the Company-wide level. FY12/20 performance was solid, as net sales increased 0.6% YoY, operating income rose 10.8%, and the segment profit margin was 7.6% (up 0.7pp). However, if we look exclusively at the 2H, we can see the adverse impact of the coronavirus pandemic, with net sales declining 3.0% YoY and operating income falling 6.9%. Based on the acquisitions of orders per quarter, compared to the 1Q in which they increased 8.0% YoY, orders trended downward from the 2Q, decreasing around 5%. As a result, at the end of the period, the order backlog had declined 0.4% compared to the end of the previous fiscal year.

Embedded / control software is software that runs on a microcomputer or other piece of equipment embedded into a device to provide specific functions. The Company's technologies are used in a variety of products and devices, including vehicles and mobile phones, home appliances such as TVs and air conditioners, office automation (OA) equipment including printers, robots and semiconductor manufacturing device production equipment, infrastructure equipment such as traffic lights, and medical equipment such as CT and MRI.

In this area, the Company has built up an excellent track record within Japan and boasts strengths in FA and other machine control systems and automotive-related fields. Looking strictly at vehicles installations, in practical terms it delivers products to all vehicle manufactures in Japan, and has the top share of the domestic market.

In FY12/20, although social infrastructure-related business performed strongly, there was a shift toward strengthening adjustments in the 2H for FA and automotive companies, mainly due to the impact of the coronavirus pandemic. However, there has been no change to the trend of CASE (Connected, Autonomous (driving) Shared/Service, Electric) through AI and robots for productivity reforms and in the automotive industry, where it is thought that opportunities to obtain medium- to long-term profits will increase for the Company.

Trends in embedded / control software net sales and operating income margin



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

2. Further strengthening of initiatives in the online field in operations software

Operations software, part of the system construction category in the SI Business, is a major pillar of earnings, contributing 28.6% of Company-wide net sales (FY12/20) and 24.3% of operating income. It achieved double-digit increase in sales and profits for three consecutive fiscal years up to FY12/19. Even during the coronavirus pandemic, while the sales-increase rate fell temporary in FY12/20, rising 3.6% YoY, the profit-increase rate was 21.6% and the segment profit margin was 5.6%, improving 0.8pp. In addition, the quarterly order backlog fell to 18.9% in the 2Q compared to the same quarter in the previous fiscal year, but then recovered toward the end of the period (3Q: up 7.7% compared to same quarter in previous fiscal year→4Q: up 12.9%), and at the end of the period, the order backlog had increased 4.5% on the end of the previous fiscal year.

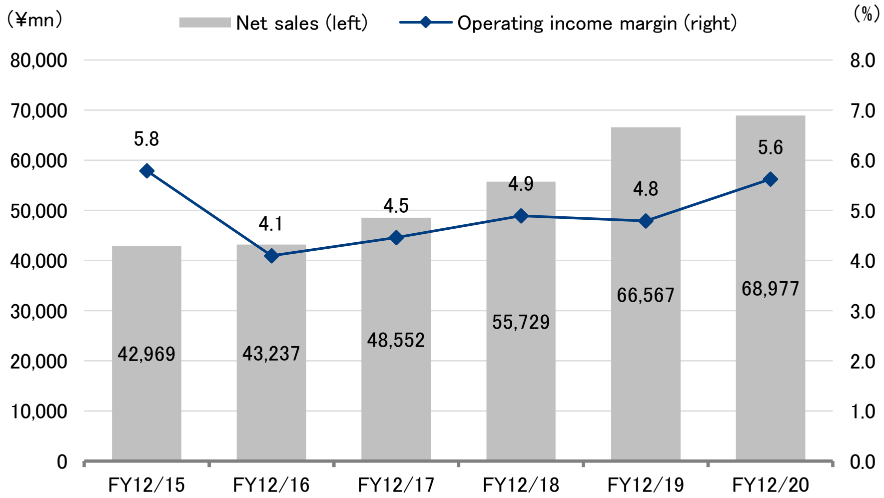
In this area, in addition to organic business growth, the complementary M&A strategy is proving successful, and the Company has established a system that is able to provide a one-stop service from consulting through to development, systems construction, and support, for various solutions, such as for backbone systems like store and ordering systems and production, sales, inventory, and accounting systems, and also information systems and online services. It provides these solutions to a wide range of industries, including distribution, finance, service, manufacturing, online businesses, social infrastructure, education, medicine, and public institutions.

In the operations software area, which is positioned as the main battlefield in the domestic IT services market, there have been structural changes in the market that could prove to be disadvantageous to the existing players, including 1) the shift from on-premises (operating IT systems, such as servers, through equipment installed within a company) to the use of cloud services, and 2), the evolution from “defensive IT (mainly to improve work efficiency)” to “offensive IT (mainly to create businesses).” Within these conditions, the Company, based on a spirit of seeing “change as an opportunity” has clearly set out and is implementing an approach of strengthening the development of outsourcing through actively investing in human resources. It truly makes management decisions in accordance with the Company motto of “Challenge and Creation.”

On this point, the strong performance of operations software in recent years can be said to be the result of the Company accurately providing services in response to changing times and the market structure-- namely, the shift to e-commerce in the distribution and services fields and the increase in demand in the digital content field, the acceleration of responses to the various digital transformations (DX) in fields centered on systems infrastructure, and the promotion of the utilization of ICT on the theme of work-style reforms.

Also, in January 2020, the Company established a new business department and is working to further strengthen initiatives in the online business field. This is part of the Company’s business strategy that directly addresses an issue that is facing existing players, which is the “inconvenient truth” of the “Amazon Effect” (the phenomenon that includes the disruption of and reforms to various markets alongside the rapid growth of Amazon.com <AMZN>. In the EC field, which is benefiting from the growth of nesting (staying-at-home) demand during the coronavirus pandemic in addition to the prior achievements, projects for B-to-C, as well as for B-to-B, are strong, and the growth trend is expected to continue in the medium- to long-term.

Trends in operations software net sales and operating income margin



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

3. Narrowly-defined products and services with increased presence

Products and services in the SI Business are divided into narrowly defined products and services and outsourcing. In FY12/20, results grew significantly for narrowly defined products and services, with net sales increasing 15.4% YoY and operating income rising 63.0%, and their percentages of the Company's total results increased by 3.2pp YoY to 33.2% for net sales and by 8.4pp to 32.1% for operating income, so their presence has further risen. Additionally, on a quarterly, orders-acquisitions basis, orders were strong basically throughout the fiscal period (1Q: up 18.5% compared to same quarter in previous fiscal year → 2Q: up 30.8% →3Q: down 19.4% → 4Q: up 24.1%), and at the end of the period, the order backlog had accumulated significantly, increasing 30.8% on the end of the previous fiscal year.

Narrowly defined products and services are comprised of 1) the Company's own products (including moreNOTE, a paperless system; Mirai School Station, a comprehensive education solution for the information society; smartBYOD, a tool for utilizing employees' personal smartphones and other devices for a company's operations; and PALRO, a communication robot, and SIM-free mobile routers FS030W and FS040W); 2) the license business (Microsoft <MSFT> products, AWS, VMware <VMW>, etc.); 3) product sales, etc. (PCs, servers, etc.)

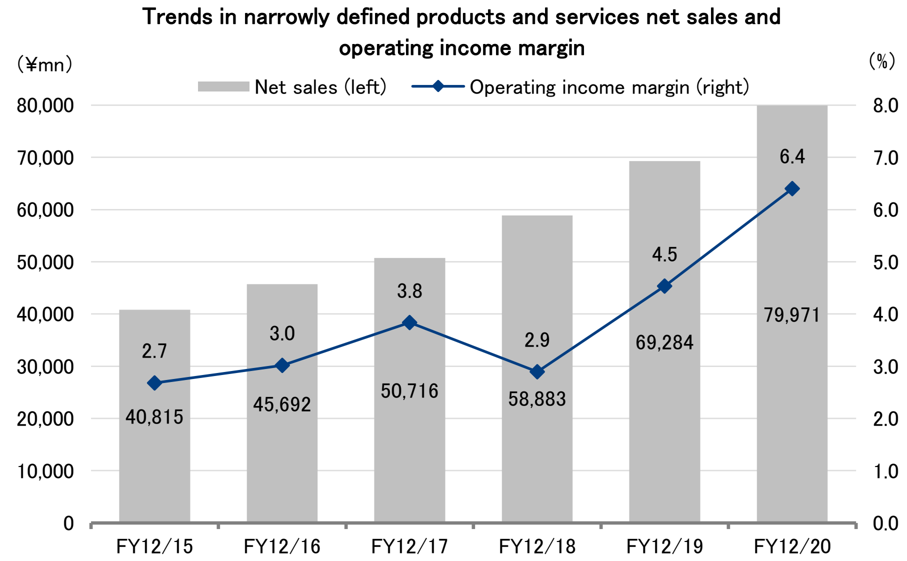
Looking at the YoY percentage increase in sales in FY12/20, sales of the Company's own products increased 38% (versus 13% increase in FY12/19), while license business sales were up 46% (versus 28% increase) and product sales, etc. decreased 14% (versus 15% increase), so the own products business and the license business showed particular strength. In the license business, AWS customers grew greatly by more than 80% YoY, while among the Company's own products, the SIM-free mobile router, which is a product in the AIS-CRM area, grew to be a hit with a 54% market share. Regarding the "Mirai School Station," the government's GIGA School Program (a system in which the government subsidizes the cost of installing communication networks and PCs at elementary and junior high schools nationwide) has been pushed forward amid the coronavirus pandemic, which is stimulating demand.

With respect to the license business, sales have continued to increase even after peaking out of special demand in conjunction with the end of support for Windows 7 (on January 14, 2020). In addition, generally speaking, it is possible that stability in the business has increased thanks to the growing shift to a subscription model for ICT products—a business model in which fees are collected based on length of use, rather than via one-time software sales—including Office 365 and various cloud services. Note that sales of support for deployment of licensed products is recorded in the Company's own products, apparently enabling it to secure high profit margins.

In addition, the Company's series of initiatives backed by long-term personnel development have been highly evaluated by its business partners. Specifically, since 2019, its awards and achievements have included the following: 1)Winner of the Modern Device Award in the Microsoft Japan Partner of the Year 2019; 2) In 2019, it became the first company in Japan to acquire certification for "Government Agency Competency," "IoT Competency," and "Management Service Provider" from Amazon Web Services (AWS), the largest provider of IT cloud services in the world, and acquired certification as an APN Premier Consulting Partner, which is only granted to partners with particularly excellent track records, in 2020. It also acquired certification for "Migration Competency" and for the "AWS well-Architected Partner Program," which require comprehensive skills and a track record to migrate from on-premises environments to AWS; 3) It attained the status of "Principal," which is the highest level of certification in the three categories (out of a total of five categories) of data center virtualization, network and security, and digital workspace, in the new partners system from 2020 implemented by IT VMware, which has the largest market share in the world of the IT virtualization market, and it won the VMware 2020 Partner of the Year Award (Cloud Platform Transformation, in Asia-Pacific and Japan); 4) It was highly evaluated by Blue Prism, which is a global leader in the corporate intelligent automation field, including for its RPA (Robot Process Automation) technological capabilities, and acquired the Silver Delivery Provider certification.

One of the Company's strengths is that, as an independent SIer, it is able to construct systems flexibly without being tied to specific hardware. At the same time, launching proprietary products, including remote education-related products and hardware such as the communication robot and mobile routers, seems to pose unique challenges. The strategy of working to create new added value through the Company's own products that are infused with its core competencies, of "superiority in technologies and deep customer insight," acts in accordance with its corporate motto of "Challenge and Creation." The Company has said that it is seeking high profitability after the investment phase.

For this point, it is worth noting that the segment profit margin of narrowly defined products and services, which had previously trended below the Company-wide level, has been significantly improving and reached 6.4% in FY12/20, an increase of 3.5pp from 2.9% in FY12/18. In addition to the fact that subsidiary CYBERNET SYSTEMS' profitability continued to improve with upfront investment targeting a bolstering of quality, the sales mix in this category also improved (the products with the thinnest profit margins fell from 50% of sales to 40% of sales, while sales in the license business rose from approximately 25% to just over 30%, and sales of proprietary products are rose 30%. Because it depends on the spot sales of products with a wide range of profitability, there is no need to worry about short-term fluctuations in the segment profit margins, but we would like to keep an eye on future trends, as we expect improvements.

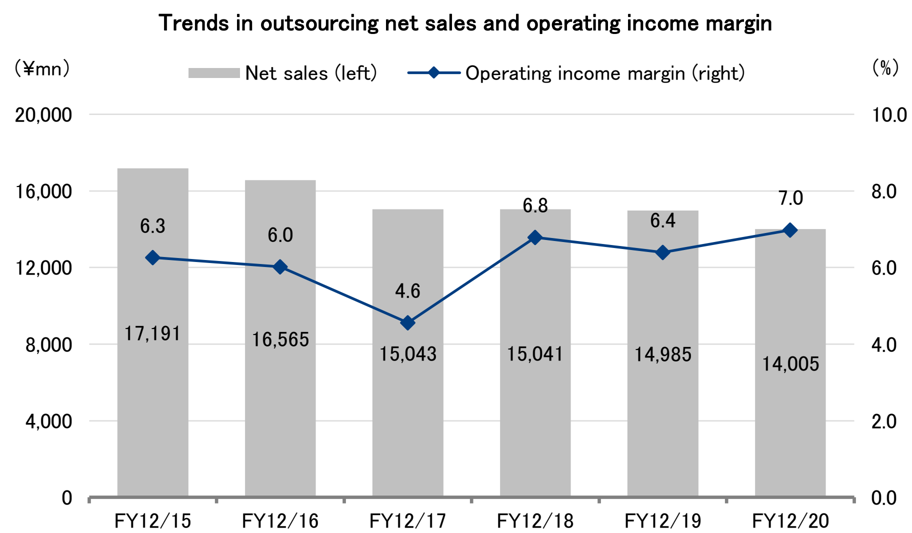


Source: Prepared by FISCO from the Company's results briefing material

4. Outsourcing is searching for the bottom

Outsourcing provides services including data centers and systems operations and maintenance, and in FY12/20 it contributed 5.8% of total net sales and 6.1% of operating income, and it had a segment profit margin of 7.0%. In FY12/20, net sales declined 6.5% YoY, operating income increased 2.1%, while the segment profit margin increased 0.6%. The order backlog as of the end of FY12/20 was 22.3% lower than at the same time in the prior year.

Due to business structural reforms and other reasons, the profit margin has been maintained in the 6% range for the past three years, which is above the Company-wide average. However, the decline in sales in recent years has been brought on mainly by the decrease in ongoing projects for distribution and services. It is thought that the data center business, in which competition with other companies' cloud services is fierce, continues to be in a phase of searching when sales from the data center business bottom out.



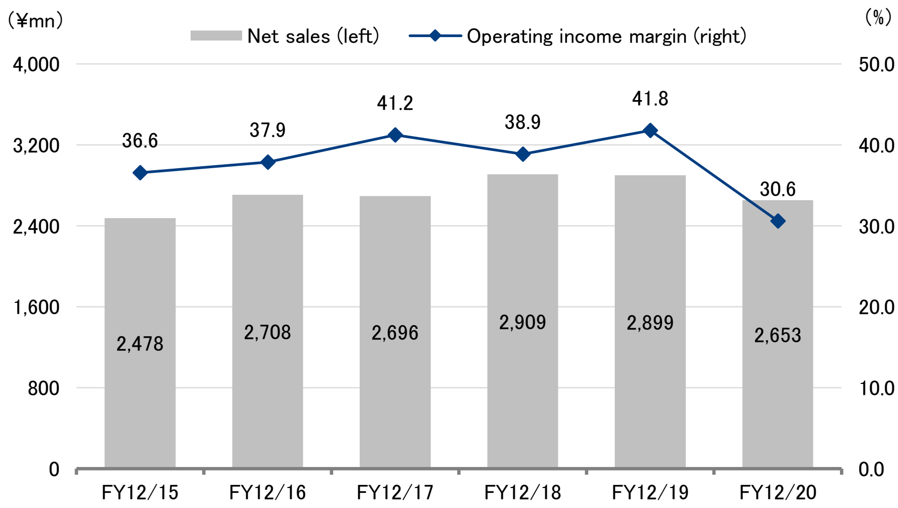
Source: Prepared by FISCO from the Company's results briefing material

5. While it is a non-core domain, the Facility Business has high earnings

The Facility Business, which obtains rental income from the office buildings owned by the Company, provides 1.1% of total net sales (FY12/20) and 5.1% of operating income, with a high segment profit margin of 30.6%. In FY12/20, the declines in the occupancy rates of some event spaces and floors were added to fluctuation factors within the Group, and net sales declined 8.5% YoY and profits fell 33.1%. However, the segment profit margin is significantly higher than the Company-wide average, and this business continues to stably perform the role of supporting the profit level, while being a non-core area.

According to the Company's securities report, there are four properties; the Yokohama Head Office (land-acquisition year: 2000, land and property book value: ¥11,135mn), the Akihabara Office (2005, ¥30,594mn), the Kinshicho Office (2000, ¥5,441mn) and the Ryogoku Office and etc. (2003 Ryogoku, ¥31,892mn).

Trends in the Facility Business net sales and operating income margin



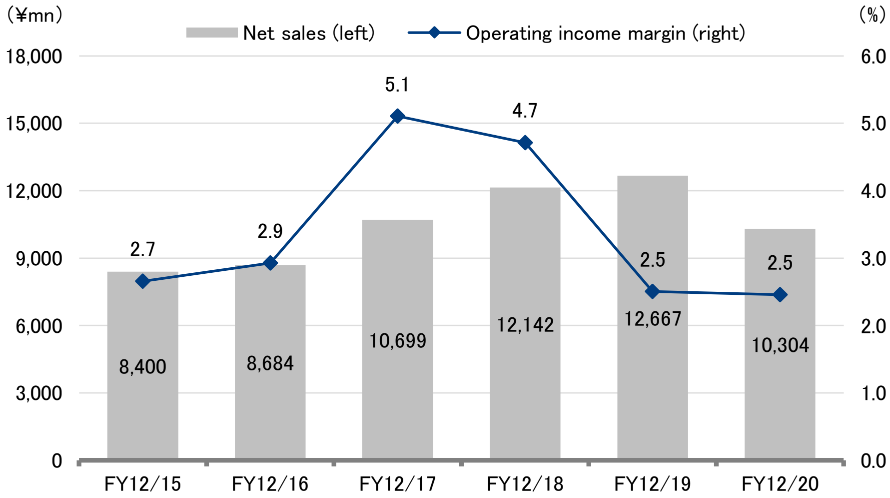
Source: Prepared by FISCO from the Company's results briefing material

6. In Other Businesses, FUJI SOFT SERVICE BUREAU's results have bottomed-out

Other Businesses provided 4.3% of total net sales (FY12/20) and 1.6% of total operating income (same). In FY12/20, net sales declined 18.7% YoY and profits fell 20.1%, but a segment profit margin of 2.5%, which was unchanged YoY, was secured.

This category's main businesses are the BPO service businesses and the contact center business operated by subsidiary FUJI SOFT SERVICE BUREAU <6188>. The main reason for the decline in performance was that the temporary suspension of FUJI SOFT SERVICE BUREAU's eligibility to participate in competitive tenders for the projects of the Japan Pension Service (from April 8, 2019 to January 7, 2020) applied the brakes to the business. However, in the FY12/20 (April to December) results of SERVICE BUREAU, which has already passed its worst period, operating income and ordinary income were both higher than the forecasts that were upwardly revised on August 5, 2020.

Trends in the Other Businesses net sales and operating income margin



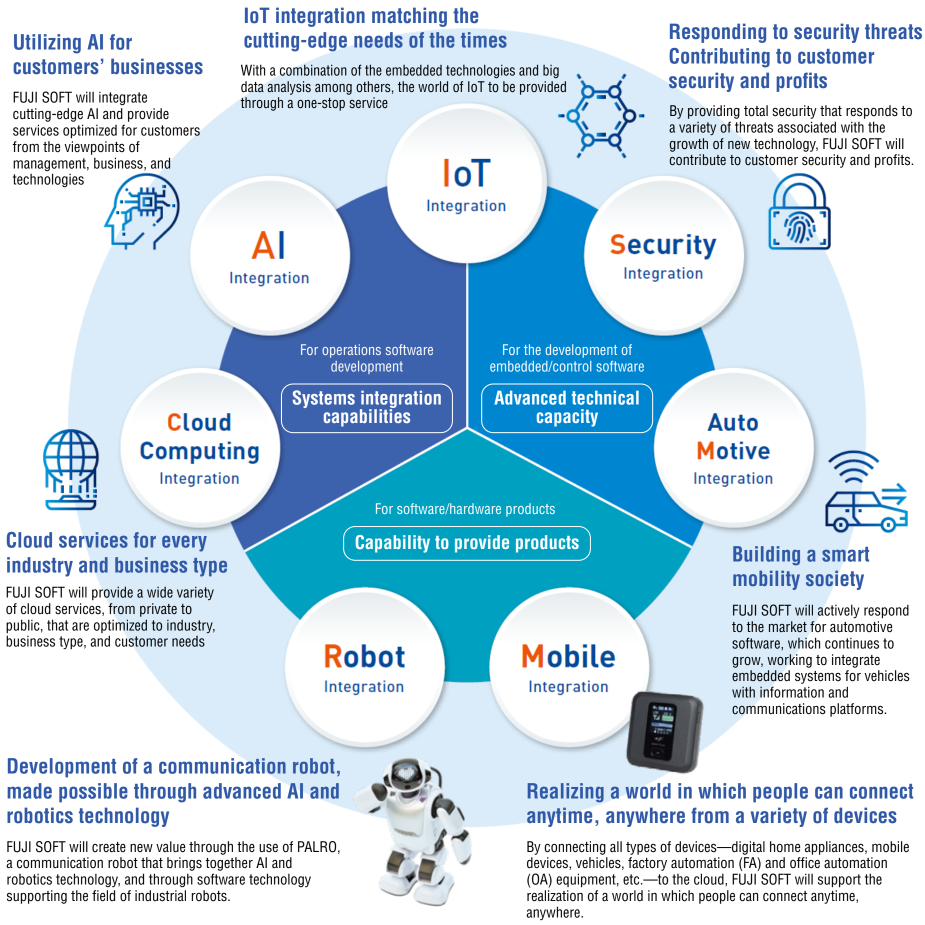
Source: Prepared by FISCO from the Company's results briefing material

7. In the business strategy for initiatives in the "AIS-CRM" area, is taking on the challenge of creating new products and businesses

As previously stated, the Company has positioned "AIS-CRM" as an important-technology field, and is focusing on creating the seeds of new products and businesses and improving the added-value of existing businesses. Although, this might look like a mere series buzzwords at first glance, the superordinate concept of the "AIS-CRM" strategy is included in the Company's core competencies, and the results of these initiatives are steadily being realized. Results are especially strong in the Cloud field, where SIM-free mobile routers have grown into hit products. Although the details have not been disclosed, the overall "AIS-CRM" field appears to have already reached a level where it accounts for a majority of the Company's stand-alone net sales.

In November 2020, the Company announced a collaboration (concluded a vendor agreement) with Red Team Technologies Co., Ltd.. The two companies have already started to provide a new security service (vulnerability diagnostics) that utilizes Synack, a cloud penetration testing platform, to corporations such as financial institutions that offer Internet-based services. This service is attracting attention as a measure to enhance the field of security in the AIS-CRM division.

Summary of AIS-CRM



Source: From the 2020 CSR Report

Results trends

In FY12/20, once again realized record highs for all results. Can be highly evaluated for both strengthening the financial structure backed by steady results from non-recurring business, and actively conducting upfront investment

In the FY12/20 consolidated results, net sales increased 4.3% YoY to ¥240,953mn, operating income rose 20.4% to ¥15,972mn, ordinary income grew 18.9% to ¥16,343mn, and profit attributable to owners of parent increased 9.4% to ¥8,573mn. Results continued to be steady, continuing on from FY12/19 in which operating income set a new record high above the previous high before the 2008 financial crisis (¥12,078mn in FY3/06. Record high net sales were already set in FY12/17).

Looking at the rates of progress of these results compared to the initial Company forecasts announced in February 2020 (net sales of ¥238,000mn, operating income of ¥13,600mn, ordinary income of ¥13,850mn, and profit attributable to owners of parent of ¥8,000mn), net sales were 101.2%, operating income was 117.4%, ordinary income was 118.0%, and profit attributable to owners of parent was 107.2%. The Company succeeded at surpassing the forecast in all accounting items for the fifth consecutive period; in particular, the achievement rates of operating income and ordinary income were the highest in the last five years.

In fact, more than 10 years passed since the Company set new record high net sales in FY12/17, higher than the peak net sales prior to the 2008 financial crisis (FY3/06). It can be highly evaluated for not only recovering non-recurring revenue, but strengthening both the financial structure and growth potential.

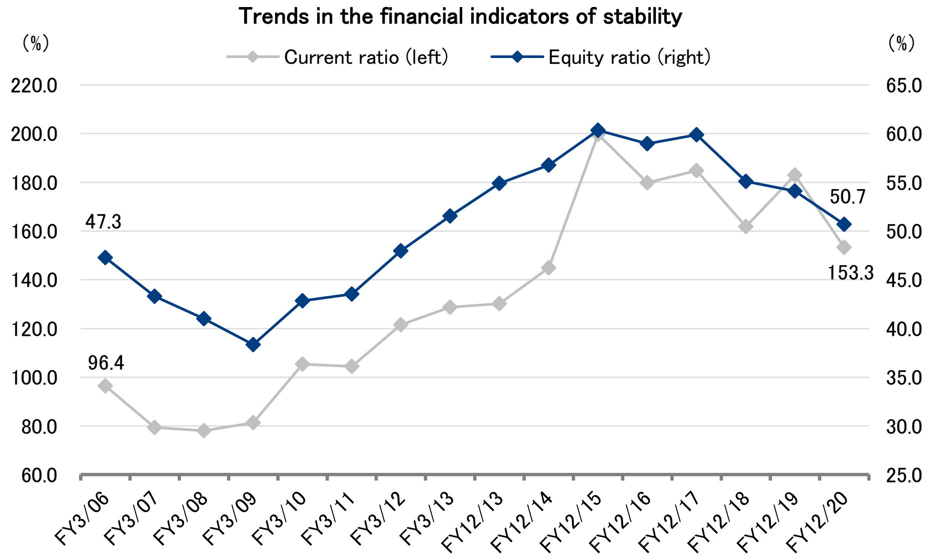
Specifically, the Company realized soundness for the representative financial indicators, with the equity ratio rising from 47.3% at the end of FY3/06 to 60.3% at the end of FY12/15, and to 59.9% at the end of FY12/17; the current ratio from 96.4%, to 199.7%, to 184.9%; and net interest-bearing debt (interest-bearing debt – cash and deposits) of ¥21,295mn, to ¥2,426mn, to excess cash of ¥6,204mn. Based on this, from FY12/15 onwards it conducted major recruitment, mainly of new graduates, so the number of consolidated employees increased by 1.4 times, from 9,415 employees at the end of FY3/06 to 13,556 employees at the end of FY12/17. The percentage of certified technicians on a stand-alone basis (the percentage of certified specialists and certified project managers, based on the Company system out of the total number of employees) also had risen from 22.8% at the end of FY12/14 to 30.1% at the end of FY12/20. From this, it can be understood that growth potential as seen from the aspect of human resources has been enhanced both in terms of quantity and quality.

As a result of the above, subsequently through FY12/19, the Company continuously achieved YoY double-digit increases in sales and profits, and even in FY12/20 during the coronavirus pandemic, it secured a 4.3% increase in net sales and realized a 20.4% increase in operating income. The financial indicators deteriorated in FY12/20, as the equity ratio was 50.7% (down 3.4pp from the end of the previous fiscal year) and the current ratio was 153.3% (down 29.6%). But this was due to the Company's financial strategy based on the impact of the coronavirus pandemic (accumulate cash and deposits through short-term fund raising and repay long-term borrowing), and should not be considered a major cause for concern. In fact, net interest-bearing debt decreased ¥1,157mn from the end of the previous fiscal year to ¥6,341mn and the Company maintained its sound financial structure. For human resources also, it has 14,422 consolidated employees, up 248 employees on the end of the previous fiscal year, and the percentage of certified technicians on a stand-alone basis is 32.0%, an improvement of 2.5pp.

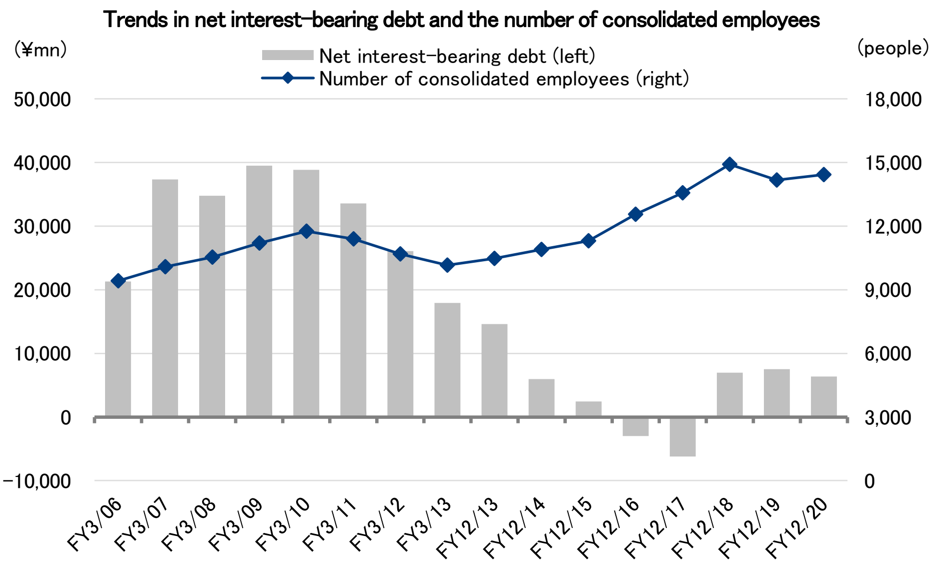
In addition, the capital investment amount increased from ¥3,028mn in FY12/14 to ¥22,608mn in FY12/18, ¥8,952mn in FY12/19, and then was ¥10,203 in FY12/20 while R&D expenses also rose from ¥488mn in FY12/13 to ¥1,011mn in FY12/17, ¥831mn in FY12/19, and then were ¥984 in FY12/20. Therefore, the Company has been expanding upfront investment, which together with its investment in human resources, indicates its intention to strengthen growth potential toward "Challenge and Creation."

Looking here at the relationship between the financial indicators and the management strategy, in FY12/15, which is when the Company launched large-scale recruitment and increased upfront investment, the equity ratio was around the 60% level, the current ratio had improved to nearly 200%, and net interest-bearing debt had been reduced to a level of excess cash in FY12/16 and FY12/17. This indicates that FY12/15 was when the Company realized a strong financial structure.

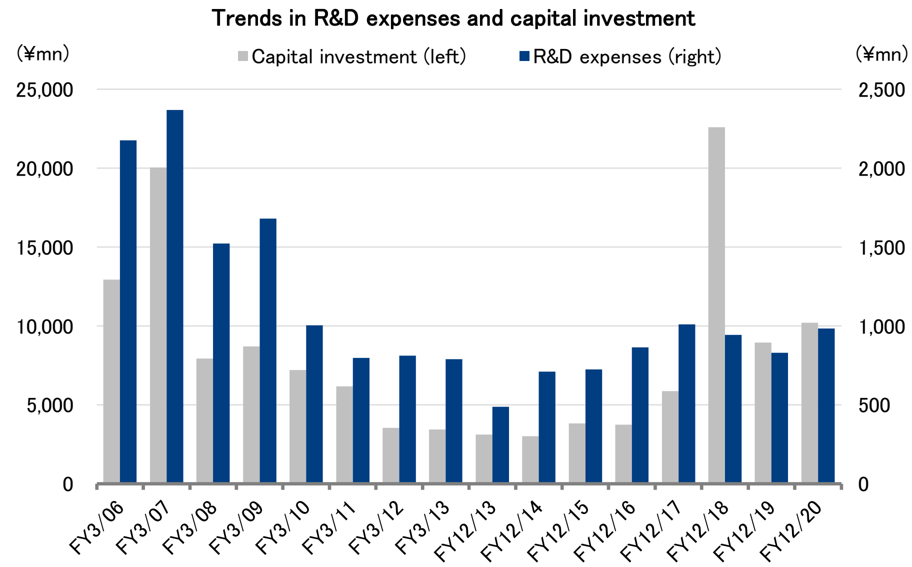
It can be said that the Company's strengths include its ability to make and implement management decisions quickly through strong leadership, including that of its founder. It did not hesitate to change to "offensive management (actively conducting upfront investment)" precisely because it had progressed "defensive management (strengthening the financial structure)" during a phase of slumping results. Therefore, the Company can be highly evaluated for making impartial management decisions that accurately reflect the changes to its business environment.



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



Source: Prepared by FISCO from the Company's securities report and results briefing material



Source: Prepared by FISCO from the Company's securities report and results briefing material

Simplified income statements

(¥mn)

	FY12/16	FY12/17	FY12/18	FY12/19	FY12/20	FY12/21 (E)
Net sales	164,218	180,773	204,329	231,074	240,953	249,000
YoY	6.9%	10.1%	13.0%	13.1%	4.3%	3.3%
Cost of sales	126,024	138,708	156,808	178,337	186,105	-
YoY	7.2%	10.1%	13.0%	13.7%	0.0%	-
Gross profit	38,193	42,065	47,520	52,736	54,847	-
YoY	5.8%	10.1%	13.0%	11.0%	4.0%	-
Gross profit margin	23.3%	23.3%	23.3%	22.8%	22.8%	-
SG&A expenses	29,394	32,357	36,119	39,470	38,875	-
YoY	6.2%	10.1%	11.6%	9.3%	-1.5%	-
SG&A expenses ratio	17.9%	17.9%	17.7%	17.1%	16.1%	-
Operating income	8,798	9,708	11,400	13,266	15,972	16,300
YoY	4.5%	10.3%	17.4%	16.4%	20.4%	2.1%
Operating income margin	5.4%	5.4%	5.6%	5.7%	6.6%	6.5%
Ordinary income	9,166	10,260	12,071	13,749	16,343	16,900
YoY	0.8%	11.9%	17.7%	13.9%	18.9%	3.4%
Profit attributable to owners of parent	5,042	5,797	6,516	7,836	8,573	8,900
YoY	2.4%	15.0%	12.4%	20.3%	9.4%	3.8%

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

Simplified balance sheets

(¥mn)

	End-FY12/16	End-FY12/17	End-FY12/18	End-FY12/19	End-FY12/20	Change
Current assets	67,350	72,457	77,315	88,009	105,363	17,354
Cash and deposits	19,134	18,851	22,554	22,278	38,330	16,051
Notes and accounts receivable - trade	36,727	40,288	44,456	49,570	52,750	3,179
Non-current assets	96,513	102,110	115,310	119,609	129,173	9,564
Property, plant and equipment	65,796	65,220	82,356	86,334	89,928	3,594
Intangible assets	5,949	6,821	4,738	4,043	4,705	661
Investments and other assets	24,766	30,068	28,214	29,231	34,539	5,307
Total assets	163,863	174,568	192,625	207,618	234,537	26,919
Current liabilities	37,461	39,197	49,428	48,106	68,751	20,644
Notes and accounts payable - trade	9,444	9,977	9,526	13,361	12,519	-842
Short-term loans payable and others	9,410	8,464	16,207	7,158	24,156	16,998
Non-current liabilities	17,400	16,959	23,526	32,691	30,623	-2,068
Long-term loans payable	6,723	4,182	13,319	22,618	20,515	-2,102
Total liabilities	54,861	56,156	72,955	80,797	99,374	18,576
(Interest-bearing debt)	16,134	12,647	29,527	29,776	44,671	14,895
Total net assets	109,001	118,411	119,670	126,820	135,163	8,342

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

Simplifies cash flow statements

(¥mn)

	FY12/16	FY12/17	FY12/18	FY12/19	FY12/20
Net cash from operating activities (a)	9,530	9,244	11,192	12,584	14,787
Net cash from investing activities (b)	-4,337	-4,524	-23,424	-9,442	-16,109
Net cash from financing activities	1,076	-4,462	-14,766	-1,451	12,703
Free cashflow (a) + (b)	5,192	4,720	-12,232	3,142	-1,322
Cash and cash equivalents at end of period	21,790	22,157	24,587	26,158	37,450

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

Outlook

With the business environment moving in an overall positive direction, we look forward to "the next move" targeting medium- to long-term growth

1. FY12/21 consolidated results forecasts

For the FY12/21 consolidated results, the Company is forecasting net sales to increase 3.3% YoY to ¥249,000mn, operating income to rise 2.1% to ¥16,300mn, ordinary income to grow 3.4% to ¥16,900mn, and profit attributable to owners of parent to increase 3.8% to ¥8,900mn. Therefore, it is actually forecasting the eighth consecutive period of higher net sales and operating income since 2013 when it transitioned to a fiscal period ending in December.

These results may appear unsatisfactory compared to the FY12/20 results when profits increased by double digits. However, since FY12/15, the Company has continued with a pattern of setting initial forecasts assuming that net sales will increase by around 3% and an operating income margin of the same level as the previous period's result. Therefore, these Company forecasts are also considered to be positioned as the minimum amounts to be achieved and do not need to be viewed negatively.

The business environment is thought to be moving in a generally positive direction, based on factors such as the fact that the order backlog in FY12/20 had risen 10.1% on the end of the previous fiscal year on a Company-wide basis. In the embedded / control field, strong results are expected to continue for social infrastructure-related fields, including 5G, while positive signs have also started to appear in terms of the economic sentiment and inquiry conditions for FA and for automotive business, for which adjustments are being strengthened. In the operations-related field, in addition to the increase in demand in the EC field, there is a strong sense of increased demand for DX in other industries as well. For narrowly defined products and services, it appears that the favorable conditions are continuing for the license business and the Company's own products.

For the dividend forecast, compared to the FY12/20 annual dividend of ¥51 per share (¥28 per share at the end of 2Q, including a commemorative dividend of ¥5 to mark the 50th anniversary of the foundation, ¥23 per share at the end of the fiscal year), the forecast is for an annual dividend of ¥50 per share (¥25 per share at the end of 2Q, ¥25 per share at the end of the fiscal year). Although this appears to be the first dividend decrease in six years, after excluding the commemorative dividend it is actually a forecast dividend increase of ¥2 per share as the total of the interim and period-end dividends. In addition, the Company upwardly revised the period-end dividend from the initial forecast for four consecutive fiscal periods from FY12/16 to FY12/19 based on the fact that the full fiscal year results exceeded the forecasts, so we shall be paying attention to how it responds in FY12/21.

The impact of the coronavirus pandemic and the work-promotion structure

	2020	2021
Approach	The Company implemented its own countermeasures, prioritizing prevention of transmission, ahead of the government's declaration of a state of emergency.	Whilst assuming that the impact of COVID-19 on economic activity will persist to some extent, the Company will prepare to be able to quickly adapt to any changes in the operating environment.
Communication with customers	The Company encouraged work from home and the taking home of projects from the viewpoint of preventing transmission.	Whilst continuing to encourage remote working, the Company will also actively conduct activities to win orders for onsite projects based on consultation with customers.
Business implementation framework	The Company introduced measures such as work from home and physical attendance during off-peak times. The Company reduced costs through online training and other measures. The Company assessed and reviewed productivity, quality, rules and other aspects of operations.	The Company will ensure that the productivity of employees working from home reaches a certain level and continue to operate with around 30-40% of employees working from home. The Company will build an adaptable framework, allowing fluctuation of the work-from-home rate to 70-80% depending on the rate of infections. The Company will continue to reduce costs through a shift to online recruitment, training and promotional activities, the termination of office lease contracts and other measures.
Promotion of DX (internally)	The Company introduced AI into some of its internal administrative operations. The Company also implemented AI validation and some PoC testing as part of development. The Company applied virtual offices as part of workstyle reforms.	The Company will increase AI use in its value chain, strengthen communication between virtual offices, and harness the IOT to improve productivity, whilst further strengthening security.

Source: From the Company's results briefing material

Results forecast

(¥mn, %)

	Net sales		Operating income		Ordinary income		Profit attributable to owners of parent		Net income per share (¥)
	Amount	YoY	Amount	YoY	Amount	YoY	Amount	YoY	
FY12/19	231,074	13.1	13,266	16.4	13,749	13.9	7,836	20.3	250.40
FY12/20	240,953	4.3	15,972	20.4	16,343	18.9	8,573	9.4	273.96
FY12/21 (E)	249,000	3.3	16,300	2.1	16,900	3.4	8,900	3.8	284.40

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

2. Productivity is improving from the focus on upfront investment and work-style reforms

On the one hand, the Company is focusing on investing in human resources, centered on the large-scale recruitment of new graduates, while on the other hand, it is assiduously implementing work-style reforms that are tailored to a variety of lifestyles, and providing support for these reforms, toward realizing "relaxed and worthwhile" working environments.

Specifically, based on the upgraded version of the Super Flex System introduced in 1990 that had no core working hours, the Company introduced the Ultra Flex system (the Super Flex system + a system enabling the acquisition of paid leave on units of 30 minutes without fixing the time period and 'refresh time' of 10 minutes). Based on this, it has been working on reducing overtime work, promoting acquisitions of qualifications, establishing an environment for remote work, and also working on the fully fledged operations of an at-home work system geared toward all Company employees. In 2020, it adopted the system two months prior to the Japanese government's declaration of a state of emergency. Beginning in April 2020, it introduced a system for homeworking allowance (temporary allowance payments for initial expenses) and a support fund (monthly allowance payments for electricity and communication expenses).

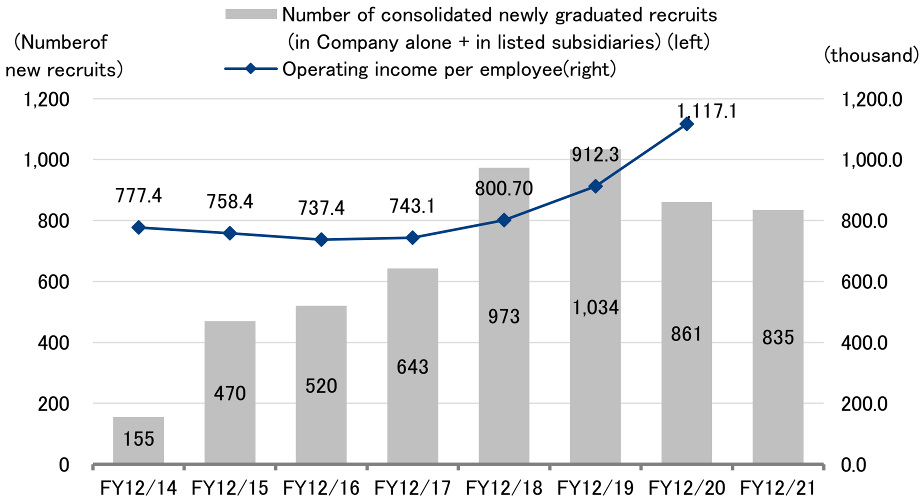
As a result of the above, the Company achieved excellent results in FY 2019 (statistics compiled from April to March) for 1) a paid-leave acquisition rate: 71.8% (private-sector average 56.3%, government target, 70% in 2020), 2) home-work employees: 9,614 employees in total, 3) employees taking childcare leave: 177 employees, 4) annual average overtime hours (other than predetermined): 23 hours 26 minutes. These excellent results are also being highly evaluated and recognized by external organizations. For instance, the Company was awarded the Platinum Kurumin Certification based on the Act on Advancement of Measures to Support Raising Next-Generation Children (Ministry of Health, Labour and Welfare) and the highest rank of the Eruboshi Certification based on the Act on Promotion of Women's Participation and Advancement in the Workplace (Ministery of Health, Labour and Welfare). Moreover, it has been included in the Top Hundred Telework Pioneers (Ministry of Internal Affairs and Communications), the Certified Health & Productivity Management Outstanding Organizations Recognition Program (Ministry of Economy, Trade and Industry), and certified as a Kanagawa business that promotes the support of children and child-raising (Kanagawa Prefecture).

Work-style reforms, which will cause a reduction in the working hours of existing employees, and the large-scale recruitment of new graduates will lead directly to a dilution in the fighting strength of employees and an increase in upfront costs. Therefore. in many cases, these are factors keeping down the productivity indicator of operating income per employee (operating income / the average number of employees at the end of the period) in the short-term. In the case of the Company, in the two years after FY12/15, when it began the large-scale recruitment of new graduates while producing positive effects from work-style reforms, operating income per employee decreased. However, since FY12/17, it changed direction and has been increasing. In FY12/20, it improved to just under ¥1.12 million (up 51.5% versus FY12/16).

Taking a closer look, the new graduate inclusion rate found using a simple calculation (the number of recruited new graduates in the Company along + in listed subsidiaries / the number of employees on a consolidated basis at the end of the previous year) rose each year from 1.5% in FY12/14 to 7.2% in FY12/18, and subsequently stayed at a high level in the 6% range. In addition, the FY2019 (April 2019–March 2020) average monthly overtime hours were 23 hours and 26 minutes, which was a significant decline from the 30 hours and 49 minutes in FY2014, while the paid-leave acquisition rate has stayed at a high level above 70% for three straight years from FY2017. Amid this, the Company has achieved an increase in work productivity (operating income per employee increased from just under ¥780,000 in FY12/14 to just under ¥1.12 million in FY12/20) in conjunction with the increase in expenses per employee (from ¥5.98 million in FY12/14 to ¥6.17 million in 12/20) (consolidated personnel costs / the number of employees on a consolidated basis at the beginning and end of the fiscal year). This is something that we should evaluate highly, as it appears to be the result of the Company's earnest efforts to improve the work framework and create relaxing and rewarding working environments for employees through the utilization of ICT and by continuously reviewing employee statuses and work environments.

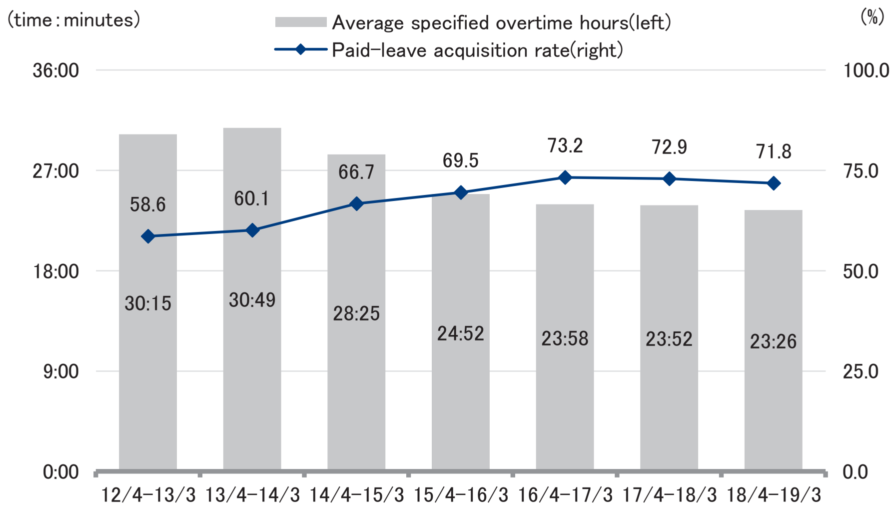
It is expected that, in the future, there will be a smaller amount of leeway to reduce overtime and increase the number of people taking paid leave, that the efficiency of remote work will improve, and that the inclusion rate of new graduates will peak out. Therefore, the positive effects from improving hourly productivity will become more likely to materialize. We have high expectations for the future of the Company, which is aiming to further improve profitability in the long term.

Trends in the number of newly graduated recruits and operating income per employee



Source: Prepared by FISCO from the Company's securities report and results briefing material

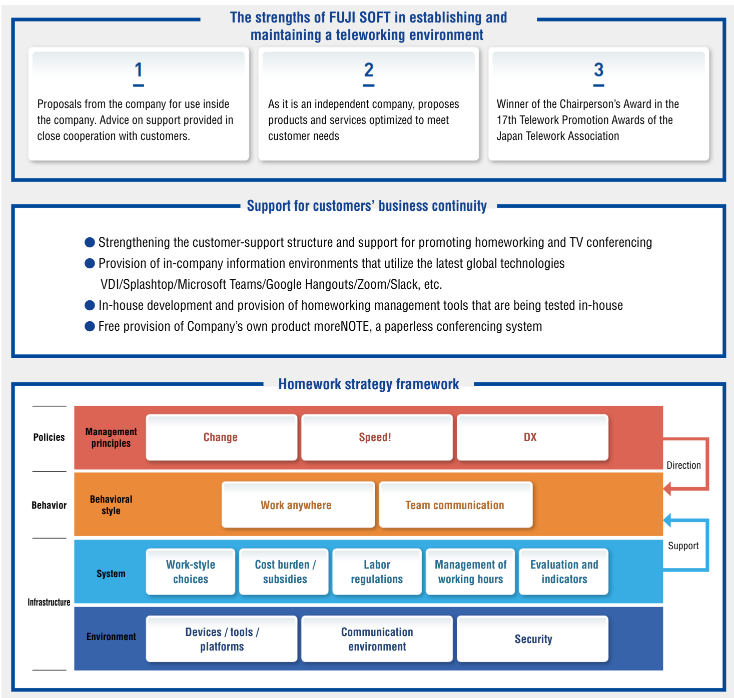
Trends in average specified overtime hours and the paid-leave acquisition rate



Source: Prepared by FISCO from the Company's CSR Report

The work-style reforms advanced by the Company up until now have become a powerful weapon to continue business without significant disruptions even during the coronavirus pandemic. Furthermore, the large-scale implementation of teleworking and homeworking using IT solutions vendors can be said to be typical "dogfooding" (trialing products and services in-house before providing them to customers), and this is considered to be extremely significant in terms of experiencing their advantages (reducing costs, improving work efficiency, etc.) and disadvantages (security issues, lack of communication, etc.)

Establishing and maintaining a teleworking environment



Source: From the 2020 CSR Report

Disclaimer

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