

COMPANY RESEARCH AND ANALYSIS REPORT

I'LL Inc.

3854

Tokyo Stock Exchange First Section

6-Nov.-2020

FISCO Ltd. Analyst

Masanobu Mizuta



FISCO Ltd.

<http://www.fisco.co.jp>

■ Index

■ Summary	01
1. Business overview	01
2. Overview of FY7/20 results	02
3. FY7/21 outlook	02
4. Medium-term business plan	02
■ Company overview	03
1. Company overview	03
2. History	04
■ Business overview	05
1. Overview of services	05
2. Main products	07
3. CROSS-OVER Synergy strategy	08
4. Characteristics and strengths	08
5. Measures to increase sales and expand profits	11
6. Policy change	12
7. Risks, income characteristics, and measures	13
■ Results trends	13
1. Overview of FY7/20 results	13
2. Trends by business segments	15
3. Financial conditions and management indicators	16
■ Outlook	18
1. FY7/21 outlook	18
2. Priority measures	18
■ Medium-term growth strategy	19
1. New three-year medium-term management plan	19
2. Growth strategies	19
3. Aims to be a leading company in DX assistance	20
4. Medium-term growth momentum unchanged as a trend	20
■ Shareholder return policy	21
■ Information security	22

Summary

Steep sales and profit increases in FY7/20, medium-term growth momentum aimed at being a leading company in DX assistance unchanged

I'LL Inc. <3854> (hereinafter, the Company) is a total system solutions company that supports improvement in corporate management capabilities with mid-tier and small/medium-size companies as its main customers. It provides total system solutions using IT through a CROSS-OVER Synergy strategy of hybrid proposals from real-world and web perspectives of business resources to resolve the full range of management issues at mid-tier and small/medium-size companies that require effective IT utilization. It does so in such ways as mission-critical system construction, system support maintenance, network construction, human resource education, web consulting, EC site construction, mission-critical operation package software, multiple EC site integrated management software, and real-world store and EC customer and loyalty point integrated management software. As a medium-term strategy, it aims to be a leading company in Digital Transformation (DX)* assistance.

* This is a concept that "wider IT usage changes people's lives in a more positive direction in all aspects" and conversion of existing business models and business methods to digital technology creates new value.

1. Business overview

The Company's business segments are the System Solutions Business with Aladdin Office Series, a mission-critical operation package software series, as the primary product and the Web Solutions Business which has the mainstays of CROSS MALL, a software product for integrated management of multiple EC sites, and CROSS POINT, a software product for integrated management of real-world store and EC customers and loyalty points available as cloud services. Main characteristics and strengths are (1) strong sales and inventory management know-how, (2) specialization in mid-tier and small/medium-size company markets, (3) ability to accommodate real-world and web environments and high market share, (4) designated industry emphasis strategy and partner strategy, (5) high proprietary product and service ratios, (6) product ecosystem strategy that realizes total solutions, (7) operations with engineers making up about 70% of employees, (8) omni-channel strategy in retail business, and (9) ability to accommodate individual customization. The Company possesses robust offensive and defensive capabilities thanks to its strength in hybrid proposals from real-world and web perspectives and is steadily increasing the number of customer companies.

The Company changed its policy toward a profit-oriented strategy and is promoting better quality control and improved productivity in development and customization, and expanding sales in recurring-type business as a priority measure. As a result, its gross profit margin on a companywide basis has trended upward from the recent bottom of 38.0% in FY7/16 to reach 44.7% in FY7/20.

Summary

2. Overview of FY7/20 results

The Company reported FY7/20 consolidated results with ¥12,679mn in net sales (up 20.5% YoY), ¥1,700mn in operating profit (up 78.8%), ¥1,715mn in ordinary profit (up 76.3%), and ¥1,189mn in profit attributable to owners of parent (up 91.5%). Sales and each profit item posted all-time highs on steep gains beyond even upward-revised targets. Recurring-type business steadily expanded due to rising customer DX needs. Additionally, the System Solutions Business benefited from one-time special demand related to the consumption tax hike, introduction of a reduced tax rate and completion of Windows 7 support. Key contributions in earnings were higher sales, expansion of recurring-type business, improved deal accuracy through integrated sales and development SE structure, and increased quality and productivity.

3. FY7/21 outlook

In FY7/21 consolidated results forecasts, the Company targets ¥12,350mn in net sales (down 2.6% YoY), ¥1,200mn in operating profit (down 29.4%), ¥1,226mn in ordinary profit (down 28.5%), and ¥784mn in profit attributable to owners of parent (down 34.0%). It expects lower sales and profits on non-recurrence of special demand seen in the previous fiscal year. While it should still achieve sales growth on a basis excluding one-time demand considering heightened customer DX needs, it seems that the Company sees this as a period of building up orders for FY7/22 due to temporary irregularity from the removal of such special demand. In expenses, the Company is factoring in an increase in personnel costs driven by employee additions in 2H (new graduates being hired in spring 2021) and an increase in headquarter rent accompanying contract renewal. Nevertheless, FISCO thinks the Company has modest earnings upside room because of possible declines in business trip costs and socializing costs depending on the COVID-19 situation.

4. Medium-term business plan

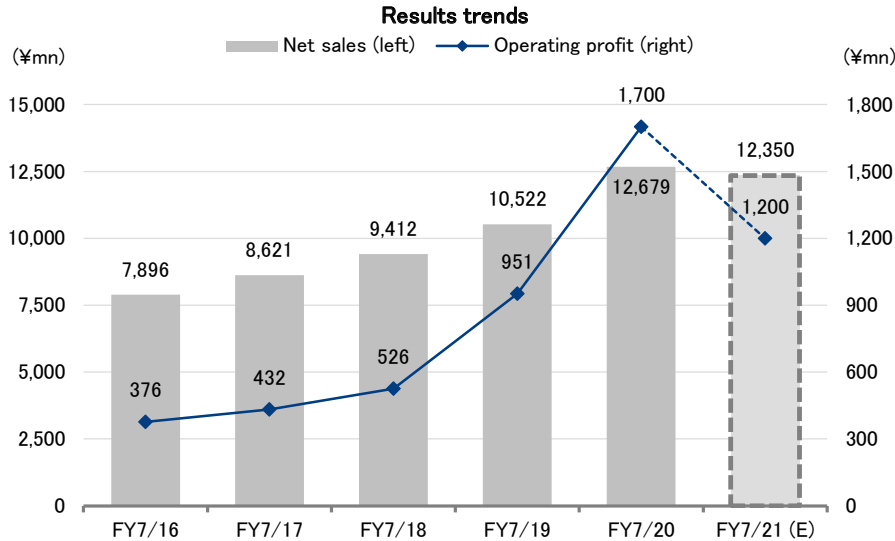
The Company delayed disclosure of new three-year medium-term management plan goals (FY7/21-23, rolling format updated each year) because of higher uncertainty due to the COVID-19 outbreak. Meanwhile, as medium-term growth strategies, it calls for (1) building a robust income foundation through stable growth in the System Solutions Business (2) cultivating the Web Solutions Business as a second major income source, and (3) entering the field of new business operation systems that incorporate new technologies. The Company promotes a unique CROSS-OVER Synergy strategy and aims to build highly profitable operations through organic coupling of proprietary developed services and products that incorporate new technologies and provision of total solution packages with high added value to the market.

The Company also wants to be a leading company in DX assistance. FISCO thinks medium-term growth momentum targeting a position as a DX assistance leader is unchanged due to healthy market conditions and an upward trend in customer volume and rising profit margins resulting from improved quality and productivity and expansion of recurring-type business.

Key Points

- Provides total system solutions through a CROSS-OVER Synergy strategy of hybrid proposals from real-world and web perspectives
- Projects temporary declines in sales and profit due to the end of special demand seen in FY7/21, though there is upside room
- Medium-term growth momentum targeting a position as a DX assistance leader is unchanged

Summary



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

Company overview

Delivers total system solutions to mid-tier and small/medium-size companies

1. Company overview

The Company is a total system solutions company that supports improvement in corporate management capabilities with mid-tier and small/medium-size companies as its main customers. It provides total system solutions using IT through a CROSS-OVER Synergy strategy of hybrid proposals from real-world and web perspectives of business resources to resolve the full range of management issues including personnel educational assistance at mid-tier and small/medium-size companies that require effective IT utilization, such as mission-critical system construction, system support maintenance, network construction, human resource education, web consulting, EC site construction, mission-critical operation package software, multiple EC site integrated management software, and customer and loyalty point integrated management software for real-world stores and EC. It operates I'LL Career Colleges (ICCs) in Osaka and Tokyo as educational entities that offer personal and corporate training.

At the end of FY7/20, the Company had ¥354mn in share capital and 25,042,528 shares (including 5,094 treasury shares) in outstanding share volume (following the 2-for-1 stock split on November 1, 2019). Its main locations are the Osaka Headquarters, Tokyo Headquarters, Nagoya Branch, Fukuoka Branch, Sendai Branch, and I'LL Matsue Laboratory opened in Matsue (Shimane Prefecture) as a next-generation cloud R&D office in October 2017. Web Base Co. has been a consolidated subsidiary since August 2011.

Company overview

2. History

The Company started as a sales company for office computers and subsequently moved into proprietary software development and sales, PC school operation, and other areas. It currently has the System Solutions Business and Web Solutions Business (CROSS Business and Other Web Business) as segments and provides total system solutions to mid-tier and small/medium-size companies.

The Company was established in February 1991. It began its digital business design (DBD) business in January 2003 and established a unique strategy and entered the web business in November 2003. It released Aladdin Office, a proprietary sales management software, in October 2004 and started the web doctor business in August 2005.

The Company went public with a listing on the Osaka Stock Exchange (OSE) Hercules Market in June 2007 (subsequently listing on the OSE JASDAQ Market accompanying a merger of OSE markets in October 2010 and then on the Tokyo Stock Exchange (TSE) JASDAQ Growth Market accompanying a merger of OSE and TSE markets in July 2013). It changed to the TSE Second Section in June 2018 and moved to the TSE First Section in July 2019.

In March 2009, the Company released CROSS MALL, a cloud-based software product for integrated management of multiple EC sites. In April 2013, it released CROSS POINT, a software product for integrated management of real-world store and EC customers and loyalty points. In June 2017, it invested in Sivira Inc. and concluded a capital and business alliance. In October 2017, it opened I'LL Matsue Laboratory in Matsue (Shimane Prefecture) as an R&D office. The Company obtained ISO 27001 (ISMS) certification in September 2016.

Company history

Dates	Main items
February 1991	Founded with the aim of selling office computers and developing computer software (Fukushima-ku, Osaka)
September 1993	Moved the headquarters to Noda (Fukushima-ku, Osaka)
April 1996	Started the PC school business
September 2000	Started the @VAL job openings and job seeker information site
July 2001	Opened the Tokyo Headquarters in Shimbashi (Minato-ku, Tokyo)
April 2002	Moved the headquarters to Kita-ku (Osaka)
January 2003	Started the digital business design (DBD) business
November 2003	Entered the web business
September 2004	Acquired privacy mark certification
October 2004	Released proprietary sales management software Aladdin Office
August 2005	Started the web doctor business
June 2007	Listed shares on the Osaka Stock Exchange's Hercules Market
August 2008	Opened the Nagoya Branch in Sakae (Naka-ku, Nagoya)
March 2009	Released CROSS MALL, an ASP service for integrated management of multiple EC sites
October 2009	Opened the East Osaka Branch in Higashi-Osaka (Osaka)
October 2010	Listed shares on the Osaka Stock Exchange's JASDAQ Market accompanying a market merger by the Osaka Stock Exchange
December 2010	Moved the Tokyo Headquarters to Shibakoen (Minato-ku, Tokyo)
August 2011	Moved the Nagoya Branch to Nishiki (Naka-ku, Nagoya)
August 2011	Acquired Web Base as a subsidiary with the purchase of all shares
September 2012	Opened the Fukuoka Branch in Hakata-ku (Fukuoka) and the Sendai Branch in Aoba-ku (Sendai)
April 2013	Released CROSS POINT, a software product for integrated management of real-world stores and EC customers and loyalty points
July 2013	Listed shares on the Tokyo Stock Exchange's JASDAQ Growth Market accompanying the Osaka Stock Exchange and Tokyo Stock Exchange merger
August 2015	Moved the Nagoya Branch to the Urban net Fushimi Building in Nishiki (Naka-ku, Nagoya)
November 2015	Mission-critical system Aladdin Office for Foods won the 45th Food Industrial Technical Award
March 2016	Moved the Osaka Headquarters to Grand Front Osaka Tower B in Kita-ku (Osaka)
September 2016	Mission-critical system Aladdin Office for Foods won the 19th Excellent Food Machine and Materials Prize
September 2016	Obtained ISO 27001 (ISMS) certification
May 2017	Ranked No.1 in Toyo Keizai Online's White 500 Companies Best for Female Recruits

We encourage readers to review our complete legal statement on "Disclaimer" page.

Company overview

Dates	Main items
June 2017	Invested in Sivira and concluded a capital and business alliance
October 2017	Opened I'LL Matsue Laboratory in Matsue (Shimane Prefecture) as a next-generation cloud R&D development office
June 2018	Changed the stock listing to the Tokyo Stock Exchange's Second Section
July 2019	Changed the stock listing to the Tokyo Stock Exchange's First Section
November 2019	Ended service by the @VAL job openings and job seeker information site
March 2020	Introduced in the METI Kansai Bureau of Economy, Trade and Industry's Interesting Kansai Company Examples – New Signs from Company Visits – KIZASHI
July 2020	I'LL services approved as tools covered by METI's IT deployment subsidies 2020

Source: Prepared by FISCO from the Company's website and releases

Business overview

CROSS-OVER Synergy strategy of hybrid proposals from real-world and web perspectives stands out

1. Overview of services

With mid-tier and small/medium-size companies as its main customers, the Company provides total system solutions using IT through a CROSS-OVER Synergy strategy of hybrid proposals from real-world and web perspectives of business resources to resolve the full range of management issues including personnel recruitment and educational assistance at mid-tier and small/medium-size companies that require effective IT utilization, such as mission-critical system construction, system support maintenance, network construction, human resource education, web consulting, EC site construction, mission-critical operation package software, multiple EC site integrated management software, and customer and loyalty point integrated management software for real-world stores and EC. It also operates I'LL Career Colleges (ICCs) in Osaka and Tokyo.

The Company's business segments are the System Solutions Business with Aladdin Office Series, a mission-critical operation package software series, as the primary product and the Web Solutions Business (CROSS Business and Other Web Business) with CROSS MALL, a software product for integrated management of multiple EC sites, and CROSS POINT, a software product for integrated management of real-world store and EC customers and loyalty points, available as cloud services. Sales breakdown by segment in FY7/20 was the System Solutions Business at 88% and the Web Solutions Business at 12% (CROSS Business at 8%, Other Web Business at 4%). The mainstay System Solutions Business and CROSS Business (under the Web Solutions Business) are expanding.

Business overview

Business activities

System Solutions Business

SI × Consulting

Operation efficiency and business management assistance

- Real-world

Aladdin Office
Mission-critical operation management system

Initial

Recurring
- Real-world

Aladdin Shop
Store management system

Initial

Recurring
- Web

Aladdin EC
BtoB EC and web orders reception and placement system

Initial

Recurring

Web Solutions Business

Cloud services × Consulting

Operation assistance that directly leads to higher sales and profits

- Web

CROSS MALL
Management system for multiple net shops

Recurring
- Web

CROSS POINT
Omni-channel, smartphone app

Recurring
- Web

CROSS STAFF
Staff management system for human resource service companies

Recurring

Source: From the Company's results overview

Sales trend by business

	(¥mn)				
	FY7/16	FY7/17	FY7/18	FY7/19	FY7/20
System Solutions Business	6,890	7,496	8,111	9,094	11,111
Web Solutions Business	1,005	1,124	1,301	1,427	1,568
(CROSS Business)	476	611	749	894	1,040
(Other Web Business)	529	513	551	533	527
Total	7,896	8,621	9,412	10,522	12,679

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

(1) System Solutions Business

The System Solutions Business designs and develops mission-critical systems and handles hardware maintenance, system operation support, network construction, and security management for customer companies almost entirely on its own. It primarily supplies the Aladdin Office Series, a proprietary mission-critical operation package software, with deployments at more than 5,000 companies and offers Aladdin Shop, a store management system for the fashion industry, and Aladdin EC, a BtoB EC and web orders reception and placement system that accommodates web usage.

The Company aims to strengthen product capabilities and differentiate itself from rivals by developing systems suited to the industries and business formats of customer companies and conducts flexible customization. Along with reinforcement of product variations designed for individual industries, it emphasizes recurring-style business that obtains revenue from maintenance and operational support after sales.

At the industry level, the Company is an approved supporting member of multiple cooperatives, including the Kansainejikyoudoukumiai (Kansai Screw Cooperative) that approved it as the first supporting member from the IT industry in 2006, and leverages industry connections in sales activities. It also enhances product value incorporating the industry's latest information into its systems. Additionally, it operates I'LL Career Colleges that provide educational services for human resource training at customer companies, such as IT and OA literacy education, engineer cultivation, credential acquisition assistance, and business skills.

Business overview

(2) Web Solutions Business

The Web Solutions Business mainly consists of the CROSS Business (CROSS MALL, a software product for integrated management of multiple EC sites, and CROSS POINT, a software product for integrated management of real-world store and EC customers and loyalty points, available as cloud services).

The Other Web Business consists of BtoB EC assistance and web marketing assistance (corporate webpage production and operation assistance, EC site construction assistance, customer business analysis and strategy consulting, promotions, and updates and revisions based on log analysis results after webpage production). While the Company halted services offered by the @VAL job openings and job seeker information site at the end of November 2019, it has been providing CROSS STAFF, a cloud system that has been managing staff for staffing firms since 2016. CROSS STAFF is a service that delivers a mix of customer website planning and development, search engine marketing (SEM), and advertising as assistance for front-side “development of new customers at clients” and back-side operation to mid-tier and small/medium-size companies that need to effectively utilize the web more than large companies. Profitability is high as a recurring-type service.

2. Main products

Below is a list of the Company's main products and leading customer deployment examples.

(1) Mission-critical operation management system for small/medium-size companies Aladdin Office and store management system Aladdin Shop (real-world)

These products support digitalization of operation management, including sales, inventory, production, and store activities, and improved management capabilities by promoting workstyle reforms with better operational efficiency and strengthening internal compliance. Leading deployment examples are shirt and necktie firm Maker's Shirt Kamakura, stocking and socks firm Fukusuke Corporation, ladies' fashion firm ANAP <3189>, high-end leather shoes firm Madras Inc., eco-friendly product importer and wholesale firm e.oct Inc., Nagoya specialty Tenmusu firm Jiraiya, apparel and restaurant business operator under the DOG DEPT brand Net Work Co., Ltd., salt and rock salt wholesale firm Japan Seasoning, Co., Ltd., and screw specialty trading firm Touyo Screw Co., Ltd.

(2) BtoB EC and web orders reception and placement system Aladdin EC (web)

This product supports digitalization of orders reception and placement operation management between companies and internally and stronger sales through workstyle reforms with better operational efficiency and differentiation from other companies. Leading deployment examples are food trading firm PRECO GROUP (group led by Preco Foods Corporation), alcohol and alcohol-related product sales firms Suntory Marketing & Commerce Limited, cosmetics and beauty and health devices and goods firm Comfort Japan Inc., babies and kids clothing firm Kimuratan Corporation <8107>, commercial alcohol wholesale firm Shibata-ya Co., Ltd., dairy product and Western confectionery firm Kurokawa Co., Ltd., bicycle firm RITEWAY (Riteway Products Japan), and restaurant, home-delivered sushi, and catering firm Dream Dining Co., Ltd.

(3) Multiple EC site integrated management software CROSS MALL (web)

This product handles integrated management of multiple internet shops, including EC mall sites and EC carts, and boosts sales through workstyle reforms with better operational efficiency and reinforced EC initiatives. Leading deployment examples are craft beer production and sales firm YO-HO Brewing Co., Ltd., sporting goods sales firm Murasaki Sports Co., Ltd., ladies' fashion firm ANAP, men's fashion EC business P.B.I. Co., Ltd. with the Silver Bullet brand, eco-friendly product importer and wholesale firm e.oct Inc., and Maruhisa, operator of internet commerce kimono wholesaler Kimono Kyokomachi.

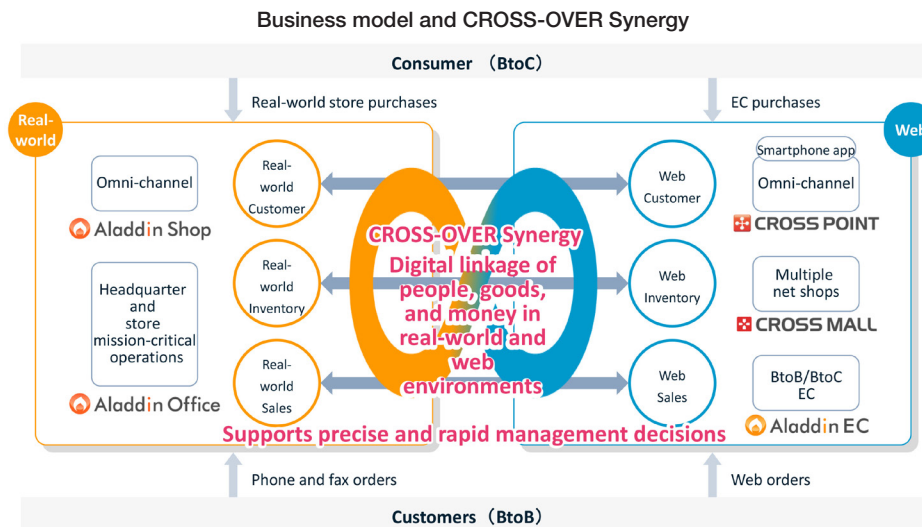
Business overview

(4) Real-world store and EC customer and loyalty point integrated management software CROSS POINT (web)

This product supports integrated management of real-world store and EC customers and loyalty points through development of a real-world store and EC omni-channel and use of a smartphone app, etc., as well as improved sales via the omni-channel and expansion of the fan segment through enhanced branding. Leading deployment examples are shirt and necktie firm Maker's Shirt Kamakura, stocking and socks firm Fukuske Corporation, babies', kids', and mothers' clothing firm BRANSHEES, casual women's clothing "w closet" firm Wears Inc., American vintage Ameri EC firm B STONE, ladies' fashion EC "flower" operator Sola Of Tokyo Co., Ltd., and bag and other apparel planning, production, and sales firm COO COMPANY LIMITED.

3. CROSS-OVER Synergy strategy

The Company is known for its CROSS-OVER Synergy strategy that presents hybrid proposals suited to customer needs from real-world (System Solutions Business) and web (Web Solutions Business) perspectives in order to promote proposals to customers more effectively and achieve powerful synergies, and thereby supports stronger management capabilities at mid-tier and small/medium-size companies. This strategy seeks realization of an "all one-stop" service that organically links mission-critical operation systems from the System Solutions Business that support better operation efficiency and services from the Web Solutions Business that assists reinforcement of sales capabilities and creation of stronger synergy effect.



Source: From the Company's results overview

4. Characteristics and strengths

The Company's main characteristics and strengths are (1) strong sales and inventory management know-how, (2) specialization in mid-tier and small/medium-size company markets, (3) ability to accommodate real-world and web environments and high market share, (4) designated industry emphasis strategy and partner strategy, (5) high proprietary product and service ratios, (6) product ecosystem strategy that realizes total solutions, (7) operations with engineers making up about 70% of employees, (8) omni-channel strategy in retail business, and (9) ability to accommodate individual customization.

Business overview

(1) Strong sales and inventory management know-how

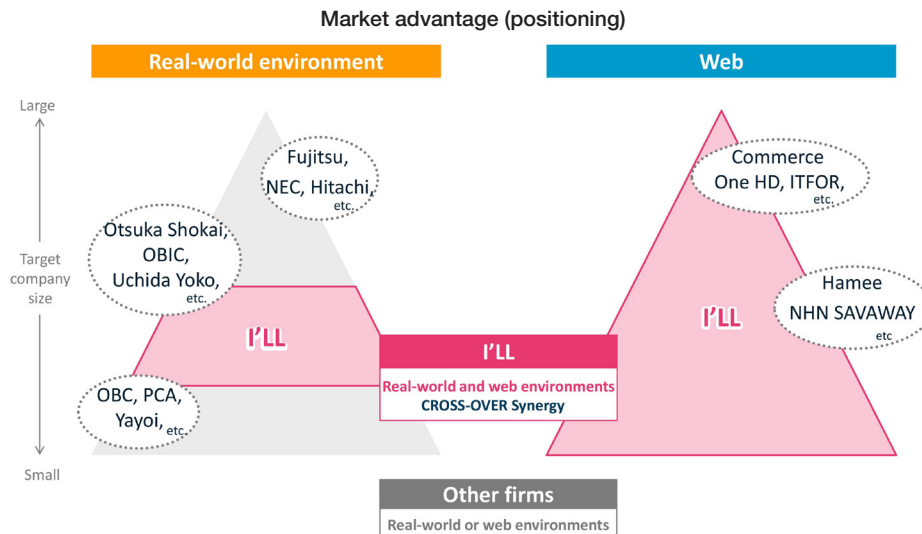
The Company has consistently provided sales and inventory management software that requires understanding of customer operations since its founding. It has extensive deployments and robust know-how in real-world and web environments for manufacturing, wholesale, retail, and other business formats and industries and sales and inventory management with different management methods for each firm.

(2) Specialization in mid-tier and small/medium-size company markets

The Company has delivered proprietary services that specialize in mid-tier and small/medium-size company markets since its founding. Small/medium-size companies with less than ¥5bn in annual sales account for roughly 90% of customer volume. In recognition of these efforts, the Company received the Special Award (Commerce and Information Policy Bureau Director-General's Award) in METI's "IT Management Awards for Small and Medium Enterprises 2011" in 2011. It also obtained certification as an "IT deployment assistance business" under the "services and other productivity improvement IT deployment assistance business" promoted by METI. Certified services are Aladdin Office, Aladdin EC, CROSS MALL, CROSS POINT, and CROSS STAFF.

(3) Ability to accommodate real-world and web environments and high market share

An important advantage in competing with other firms is the Company's ability to conduct proprietary development and provision of real-world and web support that specializes in mid-tier and small/medium-size companies. The Company is the only provider with market shares exceeding 10% in real-world and web environments.



Source: From the Company's results overview

(4) Designated industry emphasis strategy and partner strategy

Another strength is the Company's strategy of heavy focus on industries with many small/mid-size companies in wholesale, retail, and manufacturing sectors. It forms operations with robust service and sales capabilities, including development of industry-specific systems and establishment of expert teams for individual industries, and thereby boosts new customer acquisition capabilities. Specifically, it positions apparel and fashion, food, medical equipment, screws and metal parts, and steel and non-ferrous metal industries as the five main industries. It seeks to deepen market coverage with industry-specialized package software Aladdin Office Series and other products.

Business overview

A feature of the Company is that it is also highly trusted by partners in new deal introductions and sales cooperation (banks, system integrators, IT equipment manufacturers, consultants, accounting offices, etc.). Deals introduced by partners are just over 40% of new orders (on a value basis) in the System Solutions Business.

(5) High proprietary product and service ratios

The Company promotes sales expansion mainly for its own products and services as an important aspect of the management policy of building an income structure that does not depend on sales of other company products, such as hardware, readily affected by price fluctuations. Its own products and services (software, operation, maintenance, membership fees, etc.) hence have a large presence at about 70% of sales.

(6) Product ecosystem strategy that realizes total solutions

The product ecosystem strategy that consists of multiple product groups is a strength too. The Company develops proprietary products and services that cover the internet field of building internet shops and related management assistance services, the real-world store and headquarter field of store sales management and back-side inventory managements, and the real-world and web integration field of integrated management of inventories and loyalty points in real-world and EC operations. It is also capable of making hybrid proposals that combine various products and realizes total solutions for customers.

(7) Operations with engineers making up about 70% of employees

Employee composition at end-July 2020 was engineers at 75%, salespeople at 15%, and general staff at 10%. The Company places emphasis on post-system provision support too with an operation in which roughly 70% of employees are engineers. It intends to continue strengthening technology division personnel with the aim of having an organization that promotes cultivation of human resources who handle three roles (industry and operation know-how, mission-critical systems, and web) and reinforcement of technology capabilities. Meanwhile, it has adopted a policy to promote an environment and product development to overcome labor-intensive production.

(8) Omni-channel strategy in retail business

The retail industry has shown interest in recent years in omni-channel strategy that integrates real-world stores and web stores and realizes an environment and distribution paths in which customers are capable of purchasing products in the same way from all channels (sales channels and customer contact points). Since the Company has commercialized integration of real-world and web environments from its founding and accumulated business know-how and a track record that was not achieved in a short period of time, FISCO thinks it possesses an advantage in advancement of omni-channel strategy in the retail industry that cannot be copied by other firms.

(9) Ability to accommodate individual customization

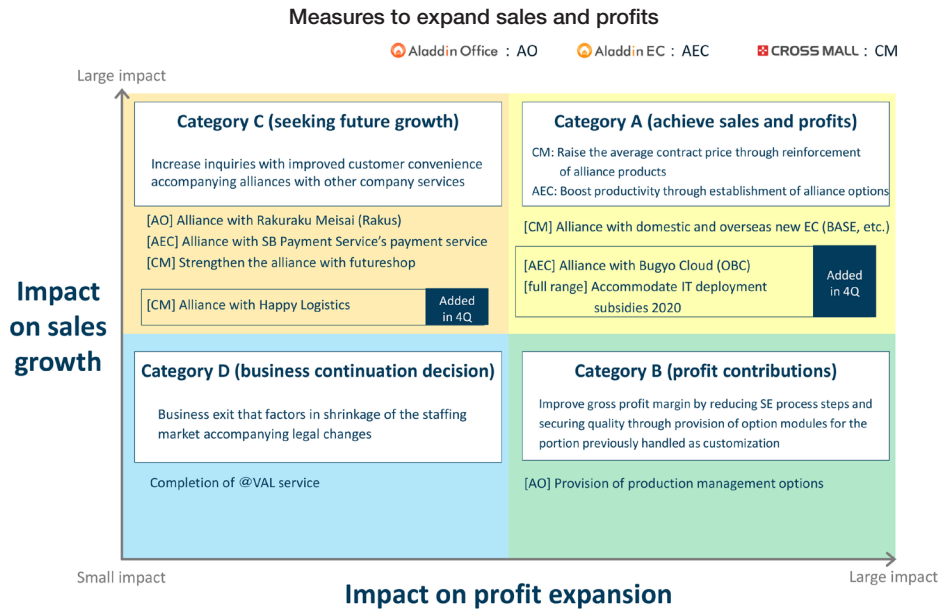
Given differences in operation implementation methods by industries and individual cases at mid-tier and small/medium-size companies, the Company adheres to a fundamental strategy of supporting individual customization of software that meets diverse needs. Meanwhile, the number of companies capable of handling individual customization of software has been trending lower in the software development market in recent years. This shift has lowered orders competition and is boosting profit margin.

Customer volume is steadily increasing thanks to the Company's robust offensive and defensive capabilities as a result of its advantages and strengths from the ability to make real-world and web proposals as a single entity. The customer repeat rate is high too (98.2% in FY7/19).

Business overview

5. Measures to increase sales and expand profits

The Company promotes upgrades to existing products, service alliances with business partners in various areas, and other strategies as part of its pursuit of higher sales and profits.



Source: From the Company's results overview

The Company added a production management option to Aladdin Office in January 2020 as an updated version of the existing product. With this capability, manufacturing customers can efficiently systematize production management functions that they require. It also provides functionality handled in customization work as an option. The Company's gross profit margin benefits from reduction of SE process steps and ensuring quality.

Regarding business partners and service alliances, Aladdin Office has a book ledger data collaboration with Rakus' <3923> web form issuance system "Rakuraku Meisai" (November 2019) and Aladdin EC interacts with SB Payment Service's payment service (November 2019) and OBIC Business Consultants' (OBC) <4733> Bugyo Cloud (August 2020).

CROSS MALL complies with Amazon's <AMZN> EC operator product inventory storage and delivery agent service "FBA Multichannel Service" (June 2019), supports inventory collaboration with LOCONDO's <3558> LOCONDO.jo, STRIPE DEPARTMENT CO., LTD.'s smarby, ZenMarket's ZenPlus, and Qoo10 PTE. LTD.'s (Singapore) Qoo10.com (September 2019 in all cases), supports orders, inventory, and product collaboration with Z Holdings Corporation's <4689> EC mall PayPay Mall (November 2019), complies with the CMS function of Future Shop Co., Ltd.'s "futureshop" (March 2020), interacts with BASE's <4477>BASE (June 2020), and interacts with Brain Wave Co., Ltd.'s Happy Logistics (July 2020).

In July 2020, the Company's IT services received certification for METI's IT deployment subsidies 2020 program.

Meanwhile, the Company phased out services offered by the @VAL job openings and job seeker information site in November 2019 on likely shrinkage of the staffing market following changes in the legal system.

Business overview

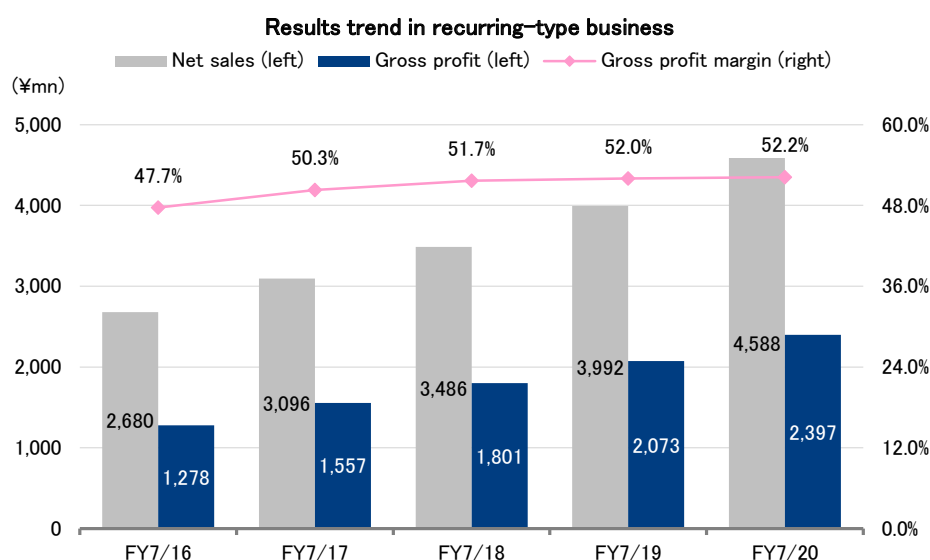
6. Policy change

The Company presented a policy of putting emphasis on profits from FY7/17 and has promoting improved quality control in development and customization, enhanced productivity, expansion of recurring-type business, etc. as priority measures since then. As a result, company-wide gross profit margin moved upward from the recent bottom of 38.0% in FY7/16 and reached an all-time high at 44.7% in FY7/20.

As ways of strengthening quality control and improving productivity in development and customization, the Company implements comprehensive measures to boost quality and productivity and gross profit margin enhancement measures, such as reducing customization steps and preventing trouble ahead of time through reinforced collaboration between sales and development teams at the orders stage. Since FY7/20, it integrated sales and support (system sales and system support) with organizational change and further enhanced collaboration. Additionally, despite the Company's support for individual customization as a fundamental strategy, it intends to promote further improvement in the gross profit margin by expanding orders that do not require customization and shortening lead time with enhanced quality and productivity.

Sales from recurring-type business, such as system maintenance in the System Solutions Business and CROSS MALL and CROSS POINT in the Web Solutions Business, are steadily expanding, and ratios in company-wide sales and gross profit have been climbing too.

Recurring-type business results in FY7/20 were ¥4,588mn in net sales (up 15% YoY), ¥2,397mn in gross profit (up 16%), and 52.2% gross profit margin (up 0.2ppt). Even with one-time decline in recurring-type business share due to special demand impact in FY7/20, net sales continued to expand, and there was no change in profit contributions leading an increase in total profit margin. The Company has established income operations in which gross profit from recurring-type business covers a large portion of salary costs in overall fixed expenses and wants to cover even more personnel expenses and fixed costs from this business.



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

7. Risks, income characteristics, and measures

System development-related companies confront fluctuation in profit margin from profitability of individual development projects. General income risks are longer development periods accompanying increasingly larger projects, increase in personnel costs and outsourcing expenses, individual projects becoming unprofitable and other factors. In the Company's case, however, since it mainly develops and sells package software, there is less risk of incurring losses on individual projects compared to system development companies that primarily handle consigned development work.

The Company encounters profit margin setback from increase in process steps and software bugs in development and customization because it pursues differentiation from rivals through provision of flexible customization suited to customers. It is addressing this challenge with the policy of stronger emphasis on earnings described above. Specific measures are efforts to reduce customization process steps and prevent trouble ahead of time by strengthening collaboration between sales and development and initiatives to boost quality and productivity with improvements in the workplace environment.

Another income feature at system development-related companies is volatility in quarterly results due to booking sales from large projects and timing of customer inspections. The Company (July fiscal year) similarly tends to book higher sales and profits in 2H (February to July) than in 1H (August to January). To adjust this tendency, it has been trying to rectify unevenness in sales recognition timing by spreading out orders and increasing orders for maintenance and other continuous services. It expects gradual progress in standardizing income recognition. In FY7/20, meanwhile, 1H was stronger because of one-time special demand from the consumption tax hike and introduction of a reduced tax rate in October 2019 and completion of Windows 7 support in January 2020. SG&A expenses are typically higher in 4Q due to entry of new employees and incentives.

While personnel recruitment is an issue for system development companies, the Company is generally smoothly hiring and training engineers thanks to successes with workstyle reforms and workplace environment improvement measures. It also strives to eliminate fluctuations in development efficiency by actively hiring engineers throughout the year with the aim of maintaining engineer technology levels at a certain threshold.

Results trends

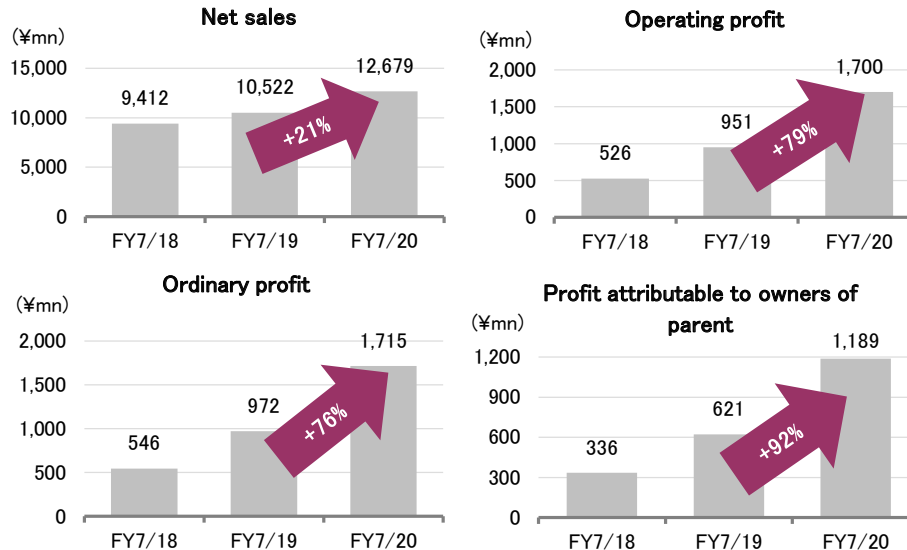
Special demand contributed to steep sales and profit increases in FY7/20

1. Overview of FY7/20 results

The Company reported FY7/20 consolidated results with ¥12,679mn in net sales (up 20.5% YoY), ¥1,700mn in operating profit (up 78.8%), ¥1,715mn in ordinary profit (up 76.3%), and ¥1,189mn in profit attributable to owners of parent (up 91.5%). Sales and profits posted all-time highs on steep gains beyond even upward-revised targets from December 6, 2019 (¥12,342mn in net sales, ¥1,519mn in operating profit, ¥1,536mn in ordinary profit, and ¥1,008mn in profit attributable to owners of parent).

Results trends

FY7/20 highlights



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

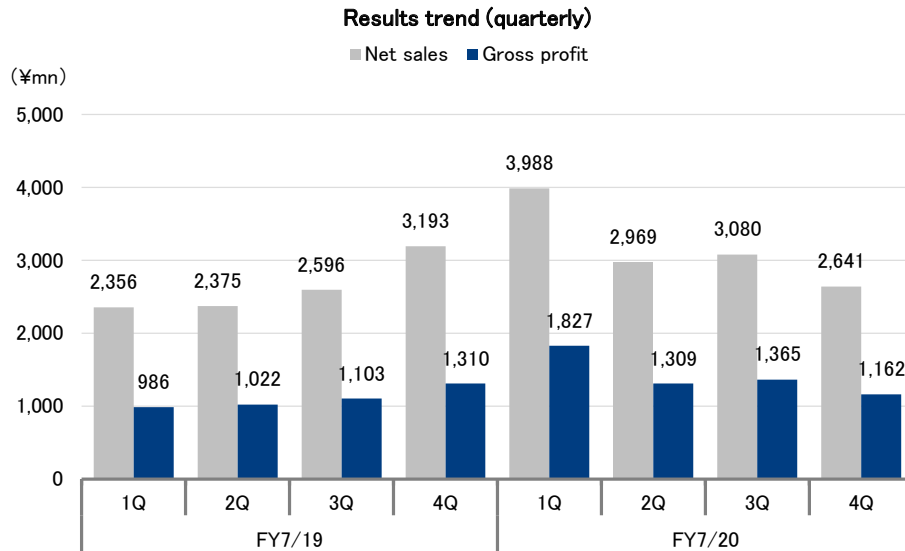
In segment trends, the Systems Solutions Business sales rose 22% YoY and the Web Solutions Business sales were up 10%. Both segments posted higher sales. Recurring-type business steadily expanded due to rising customer DX needs. Additionally, the System Solutions Business benefited from one-time special demand from the consumption tax hike and introduction of a reduced tax rate in October 2019 and completion of Windows 7 support in January 2020.

The COVID-19 outbreak did not have much impact on an overall basis. In the System Solutions Business, despite curtailment of face-to-face sales activities in April and May during the state of emergency declaration period, the Company restored normal sales operations from June and inquiries are moving upward. The CROSS Business, meanwhile, handles the entire process from opportunity development to the contract over the web.

Key contributions in earnings were higher sales, expansion of recurring-type business, improved deal accuracy through a structure integrating sales and development SE, and increased quality and productivity. Gross profit increased 28.1% YoY to ¥5,664mn, and gross profit margin climbed 2.7ppt to 44.7%. SG&A expenses were up 14.2% to ¥3,964mn, though the SG&A expenses ratio dropped 1.7ppt to 31.3%. Despite higher personnel expenses accompanying increases in headcount and incentives and expanded advertising and promotional costs driven by reinforced sales promotion measures, operating profit, ordinary profit, and profit attributable to owners of parent were sharply higher as increased gross profit more than absorbed these impacts.

Looking at the quarterly level, sales and profits improved significantly in 1Q FY7/20 thanks to special demand, while non-recurrence of special demand that started a year earlier caused YoY declines of 17% in net sales and 11% in gross profit in 4Q.

Results trends

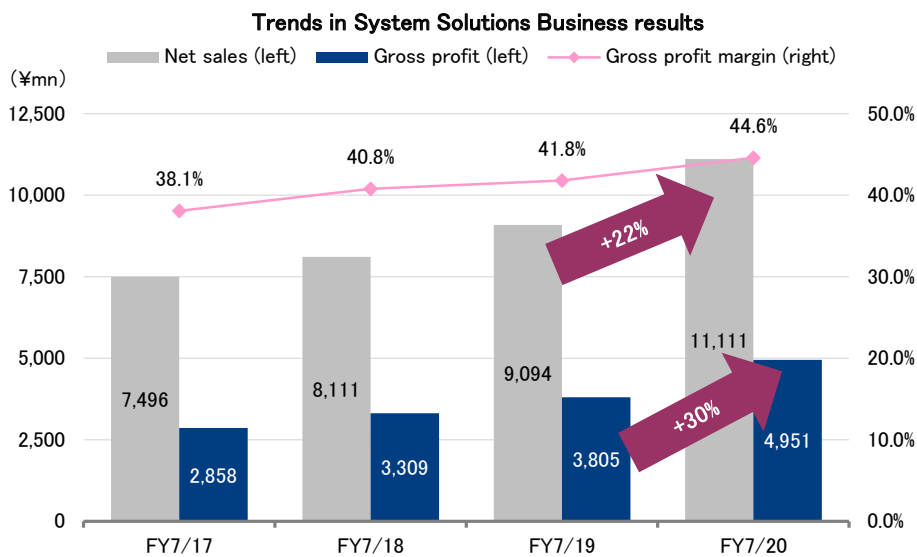


Source: Prepared by FISCO from the Company's results overview

2. Trends by business segments

(1) System Solutions Business

The System Solutions Business reported ¥11,111mn in net sales (up 22% YoY) and ¥4,951mn in gross profit (up 30%). Main sales drivers were increase in customer DX needs and special demand from the consumption tax hike and introduction of a reduced tax rate and completion of Windows 7 support. Earnings benefited from higher sales, enhanced profitability on build-up of recurring-type sales, improved deal accuracy through integrated sales and development SE structure, and reduction of customization process steps via addition of the production management option feature, etc. Gross profit margin improved 2.8ppt to 44.6%, rising on the success of measures placing more emphasis on earnings.

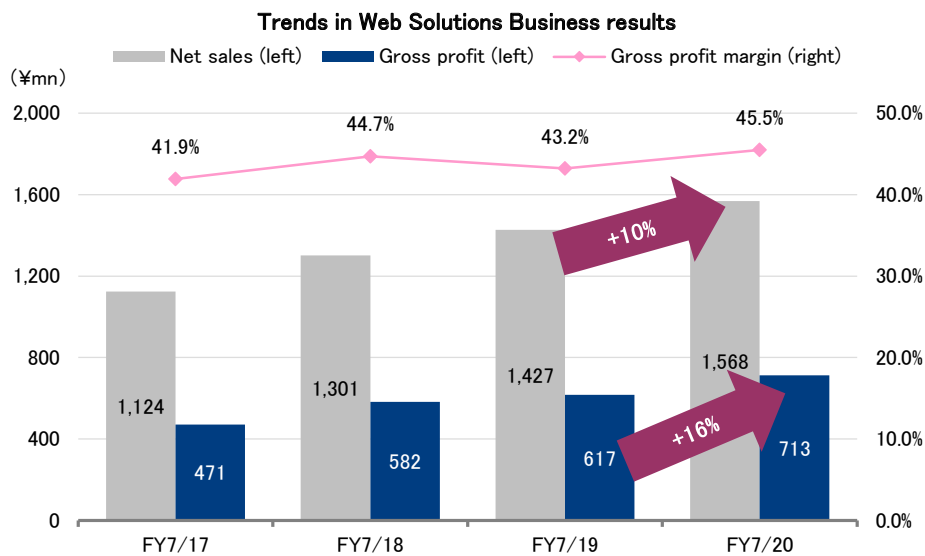


Source: Prepared by FISCO from the Company's results overview

Results trends

(2) Web Solutions Business

The Web Solutions Business reported ¥1,568mn in net sales (up 10% YoY), including the CROSS Business at ¥1,040mn (up 16%) and the Other Web Business at ¥527mn (down 1%), and ¥713mn in gross profit (up 16%), including the CROSS Business at ¥569mn (up 23%) and the Other Web Business at ¥143mn (down 6%). Sales sustained double-digit growth as gains in CROSS MALL and CROSS POINT more than offset decline related to exiting @VAL service business. The CROSS Business's gross profit margin rose 2.7ppt to 54.7%, and the Web Solutions Business's gross profit margin was 45.5%.



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

3. Financial conditions and management indicators

In financial standing, total assets increased ¥938mn YoY to ¥7,585mn and total liabilities rose ¥76mn to ¥3,871mn at end-FY7/20. In total assets, cash and cash equivalents increased. In liabilities, borrowings decreased. Total net assets were up ¥862mn to ¥3,713mn due to increased retained earnings. The equity ratio rose by 6.1ppt to 49.0%. FISCO thinks the Company has sound financial standing based on these results.

Results trends

Main management indicators

	(¥mn)				
	FY7/16	FY7/17	FY7/18	FY7/19	FY7/20
Net sales	7,896	8,621	9,412	10,522	12,679
Cost of sales	4,894	5,291	5,519	6,099	7,014
Gross profit	3,001	3,329	3,892	4,422	5,664
Gross profit margin	38.0%	38.6%	41.4%	42.0%	44.7%
SG&A expenses	2,625	2,897	3,366	3,471	3,964
SG&A expenses ratio	33.2%	33.6%	35.8%	33.0%	31.3%
Operating profit	376	432	526	951	1,700
Operating profit margin	4.8%	5.0%	5.6%	9.0%	13.4%
Non-operating profit	17	28	24	25	23
Non-operating expenses	2	4	4	3	8
Ordinary profit	392	455	546	972	1,715
Ordinary profit margin	5.0%	5.3%	5.8%	9.2%	13.5%
Extraordinary income	80	-	-	2	-
Extraordinary losses	0	0	0	0	2
Profit before income taxes	472	455	545	975	1,713
Total income taxes	224	155	208	354	523
Profit attributable to owners of parent	247	299	336	621	1,189
Profit attributable to owners of parent margin	3.1%	3.5%	3.6%	5.9%	9.4%
Comprehensive income	142	370	355	654	1,175
Total assets	4,981	5,565	5,719	6,646	7,585
(Current assets)	3,485	4,076	3,936	4,409	4,993
(Non-current assets)	1,495	1,488	1,783	2,236	2,591
Total liabilities	3,083	3,410	3,321	3,794	3,871
(Current liabilities)	1,593	1,798	1,781	2,335	2,366
(Non-current liabilities)	1,490	1,611	1,539	1,459	1,505
Total net assets	1,897	2,155	2,397	2,851	3,713
(Shareholders' equity)	2,018	2,205	2,429	2,850	3,727
Share capital	354	354	354	354	354
Total number of outstanding shares at period end excluding treasury stock (shares)	25,046,856	25,046,856	25,042,576	25,042,528	25,037,434
Net income per share (yen)	9.89	11.98	13.45	24.81	47.55
Net assets per share (yen)	75.77	86.06	95.74	113.87	148.33
Dividend per share (yen)	4.50	4.50	5.00	8.00	15.00
Equity ratio	38.1%	38.7%	41.9%	42.9%	49.0%
Cash flows from operating activities	519	920	217	1,006	2,088
Cash flows from investing activities	-601	-287	-451	-600	-587
Cash flows from financing activities	627	-21	-332	-420	-663
Cash and cash equivalents at end of period	1,326	1,938	1,371	1,356	2,194

Note: Values per share retroactively revised for 2-for-1 stock splits on August 1, 2018 and November 1, 2019 respectively.

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

■ Outlook

Projects temporary declines in sales and profit in FY7/21 based on the end of special demand, though there is the possibility of improvement

1. FY7/21 outlook

In FY7/21 consolidated results outlook, the Company targets ¥12,350mn in net sales (down 2.6% YoY), ¥1,200mn in operating profit (down 29.4%), ¥1,226mn in ordinary profit (down 28.5%), and ¥784mn in profit attributable to owners of parent (down 34.0%). Additionally, in 1H FY7/21 consolidated results outlook, it targets ¥6,467mn in net sales (down 7.1% YoY), ¥792mn in operating profit (down 35.4%), ¥802mn in ordinary profit (down 34.9%), and ¥521mn in profit attributable to owners of parent (down 35.7%).

FY7/21 outlook

	FY7/20		FY7/21 (E)			
	1H	Full year	1H	Change (%)	Full year	Change (%)
Net sales	6,957	12,679	6,467	-7.1%	12,350	-2.6%
Operating profit	1,226	1,700	792	-35.4%	1,200	-29.4%
Ordinary profit	1,232	1,715	802	-34.9%	1,226	-28.5%
Profit attributable to owners of parent	809	1,189	521	-35.7%	784	-34.0%
Net income per share (yen)	32.37	47.55	20.81	-	31.35	-

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

The Company projects lower sales and profits in 1H and the full year mainly because of non-recurrence of special demand from the consumption tax hike and introduction of a reduced tax rate and completion of Windows 7 support in the previous fiscal year. While there is no change in sales growth on a basis excluding special demand considering heightened customer DX needs, the Company sees this as a period of building up orders for FY7/22 because of temporary delay in orders on curtailment of face-to-face sales in April and May under the state of emergency declaration in response to the COVID-19 outbreak. In expenses, the Company is factoring in increase in personnel costs driven by employee additions in 2H (new graduates being hired in spring 2021) and increase in headquarter rent accompanying contract renewal.

Impact of the COVID-19 outbreak, meanwhile, has been limited, and inquiries appear to be healthy again with resumption of face-to-face sales activities from June. At the quarterly level, the Company expects restoration of positive sales growth (YoY) in 4Q. FISCO thinks the Company has modest earnings upside room because of possible declines in budgeted business trip costs and socializing costs depending on the COVID-19 situation.

2. Priority measures

Due to likely increase in DX needs for operation standardization and streamlining and pick-up in IT investments utilizing subsidies as impacts of the COVID-19 outbreak, the Company intends to promote recruitment of new customers using the web, customer development in a new channel by holding webinars, expanded sales of Aladdin EC, the BtoB EC and web orders reception and placement system that eliminates fax services, wider sales of CROSS MALL integrated management software for operating multiple EC sites, reinforcement of package software features, and improvement in SE productivity with customized part templates.

Outlook

Furthermore, the Company plans to continue implementing telework internally (sustained reduction of the company attendance rate by 30%) for the rest of this year. It hopes that this initiative will lead to standardizing web meetings and cutbacks in traveling time.

In social contribution activities, the Company was a sponsor of MOVE FES. 2019 held on December 22, 2019. This is an event by WITH ALS General Incorporated Association that promotes awareness of amyotrophic lateral sclerosis (ALS), a designated intractable disease. The Company intends to continue to actively promote corporate social responsibility (CSR).

■ Medium-term growth strategy

Medium-term growth direction aimed at being the leading company in DX assistance is unchanged

1. New three-year medium-term management plan

The Company delayed disclosure of goals for the new three-year medium-term management plan (FY7/21-FY7/23; rolling plan updated once a year) because of higher uncertainty with the COVID-19 outbreak. It intends to disclose goals once it is possible to calculate estimates after conducting a necessary review of the likely impact of the COVID-19 outbreak. Goals for FY7/22 in the plan disclosed on September 6, 2019 were ¥13,200mn in net sales, ¥2,000mn in operating profit, ¥2,026mn in ordinary profit, and ¥1,338mn in profit attributable to owners of parent.

2. Growth strategies

Despite delaying disclosure of new goals, as medium-term growth strategies, it calls for (1) building a robust income foundation through stable growth in the System Solutions Business (2) cultivating the Web Solutions Business as a second major income source, and (3) entering the field of new business operation systems that incorporate new technologies. The Company promotes a unique CROSS-OVER Synergy strategy and aims to build highly profitable operations through organic coupling of proprietary services and products that incorporate new technologies and provision of total solution packages with high added value to the market.

(1) Building a robust income foundation through stable growth in the System Solutions Business

The Company is accelerating reinforcement of various industry package products, expansion of its customer base in five specialization industries (apparel and fashion, food, medical equipment, screw and metal parts, steel and non-ferrous industry), opening new sales locations and widening commercial zone areas, and development of the ERP market and BtoB EC market. In customer segment expansion, while wholesale business had been the main segment previously, it is pursuing additions of manufacturing, import, and retail customers in the five specialization industries utilizing functions and know-how cultivated in industry-specific standard package development for the Aladdin Office mission-critical operation management system.

(2) Cultivating the Web Solutions Business as a second major income source

The Company intends to promote reinforcement of back-side assistance for the BtoB EC market through development of next-generation cloud services and formulation of a new fee plan.

Medium-term growth strategy

(3) Entering the field of new business operation systems that incorporate new technologies

The Company plans to promote development of services utilizing blockchain and artificial intelligence (AI).

3. Aims to be a leading company in DX assistance

The Company also wants to be a leading company in DX assistance and intends to promote development of next-generation cloud services and other services using blockchain technology and AI technology.

(1) Utilizing blockchain technology through a capital and business alliance with Sivira

The Company invested in Sivira and formed a capital and business alliance in June 2017. Utilizing Sivira's proprietary blockchain technology Broof, it is jointly enhancing security in cloud services, opening up inventory data, and planning, developing, and selling an open platform that extends across companies, stores, and services. In August 2017, it started operation of Sivira's proprietary blockchain technology Broof in the CROSS Series, its operation management cloud service.

(2) Next-generation cloud R&D office I'LL Matsue Laboratory

The Company opened I'LL Matsue Laboratory in Matsue (Shimane Prefecture) as a next-generation cloud R&D office and began full-fledged operations in October 2017. Part of the lab is also available as "IT interaction space." Matsue is a "sacred city" for engineers as a city promoting use of "Ruby," the first programming language developed in Japan approved as an international standard. The Company aims to achieve high quality more efficiently in development of the next-generation version of existing cloud service "CROSS SERIES" by uniformly adopting Ruby, a programming language known for its simplicity and high productivity and flexibility, as the development language.

(3) Actively investing in R&D for services utilizing AI

Anticipated trends in the market environment are growing IT investments toward realizing DX, rising IT investments in ERP and other products as part of promoting workstyle reforms (boosting productivity), expansion of the EC market, and expansion of blockchain, AI, and other new technology markets. The Company is promoting R&D activities for data analysis and automated operations utilizing AI in operation system areas as an initiative to boost competitiveness in this market environment. It also plans to build a proprietary CROSS-OVER platform that incorporates know-how cultivated in mission-critical systems and cloud services and further accelerate mutual collaboration between mission-critical systems and cloud services.

4. Medium-term growth momentum unchanged as a trend

Market conditions are healthy, and customer volume is increasing. Profit margin is rising too on improved quality and productivity and expansion of recurring-type business. FISCO hence thinks medium-term growth momentum targeting a position as a DX assistance leader is unchanged, despite the prospect of sales and profit declines in FY7/21 on one-time impact from non-recurrence of special demand.

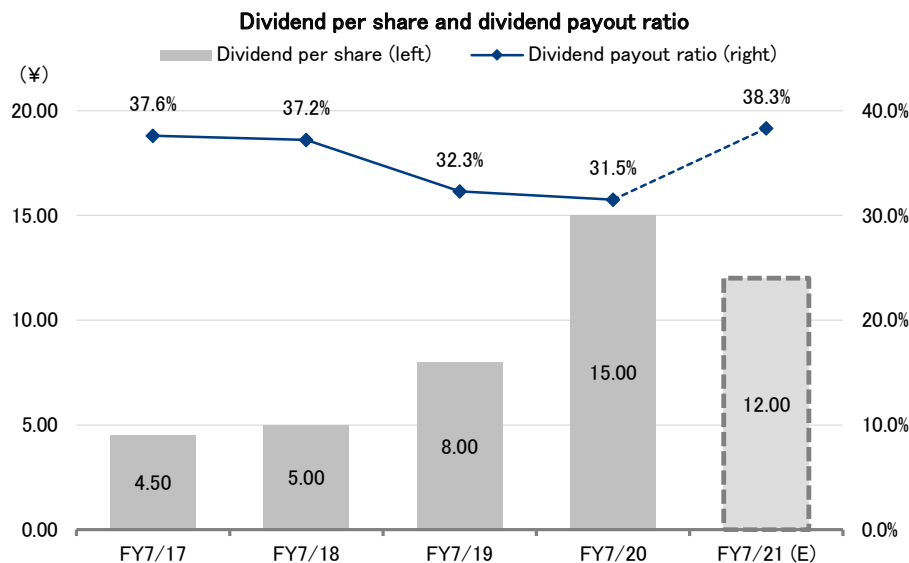
Shareholder return policy

Targets dividend payout ratio in the 30% range and a stable dividend

The Company's basic policy is to pay a dividend based on results while comprehensively considering things like management and the balance between retained earnings for maintaining and strengthening its competitiveness in the industry and return on equity (ROE) when allocating profits. The Company targets a dividend payout ratio in the 30% range and a stable dividend.

Based on the Company's basic policy, it intends to pay an annual dividend of ¥15.00 per share in FY7/20 (¥7.00 interim, ¥8.00 year-end). Taking into account a 2-for-1 stock split on November 1, 2019 and retroactively calculating the annual dividend of ¥16.00 per share in FY7/19 as ¥8.00 per share, the dividend for FY7/20 increased by ¥7.00 per share for a payout ratio of 31.5%.

The Company forecasts an annual dividend per share of ¥12.00 (¥6.00 interim, ¥6.00) for FY7/21, ¥3.00 lower YoY, for a dividend payout ratio of 38.3%. It can be expected to increase dividends and improve shareholder returns in conjunction with expanded earnings.



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

■ Information security

Amid concerns about large-scale cyberattacks and rising interest in corporate information security measures, the Company views information security and information protection as one of its most important management issues. In its provision of services that assist management operations at customers as part of efforts to strengthen management and sales foundations, the Company defines internal rules related to information system operation and handling of confidential information and promotes information security measures.

In September 2016, the Company obtained international standard ISO27001 certification for its information security management system (ISMS). It also has a dedicated department related to information security within the company, issues warnings to all employees utilizing the internal portal site, and rigorously manages the internal firewall.



Disclaimer

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

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

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

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

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

The intellectual property rights, including the copyrights to the main text hereof, the data and the like, belong to FISCO, and any revision, reprocessing, reproduction, transmission, distribution or the like of this report and any duplicate hereof without the permission of FISCO is strictly prohibited.

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

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

■ For inquiry, please contact: ■

FISCO Ltd.

5-11-9 Minami Aoyama, Minato-ku, Tokyo, Japan 107-0062

Phone: 03-5774-2443 (Financial information Dept.)

Email: support@fisco.co.jp