COMPANY RESEARCH AND ANALYSIS REPORT

Nagaileben co., Ltd.

7447

Tokyo Stock Exchange First Section

22-Nov.-2017

FISCO Ltd. Analyst
Noboru Terashima

FISCO Ltd.
http://www.fisco.co.jp

Index

Summary — 01

1. Reached record-high net sales and operating profit in FY8/17 01
2. FY8/18 (forecast): Medical treatment fees and nursing care fees are expected to be revised, but the operating profit is forecast to increase 01
3. Actively returns profits to shareholders: From FY8/17, increased the annual dividend from ¥50 to ¥60 01

Company profile — 02

Business overview — 03

1. Sales breakdown 03
2. Sales channels and production status 04
3. Characteristics and strengths 04
4. Company policy (initiatives for CSR/ESG) 05

Results trends — 06

● Summary of the FY8/17 consolidated results 06

Business outlook — 12

● FY8/18 full-year outlook 12

Medium-to-long-term growth strategy — 16

1. Mid-term Management Plan 16
2. Future business strategies: The supporting tailwind will continue for the time being 16

Shareholder return policy — 17

Summary

Both net sales and operating profit achieved record highs in FY8/17

Nagaileben co., Ltd. <7447> (hereafter, also "the Company") is the leading manufacturer of medical gowns in Japan, with a domestic market share of over 60%. The Company boasts high profit margins and a solid financial condition.

1. Reached record-high net sales and operating profit in FY8/17

In the consolidated results for FY8/17 announced by the Company, net sales increased 2.9% year on year (YoY) to ¥17,017mn, operating profit rose 5.9% to ¥5,242mn, recurring profit increased 8.2% to ¥5,340mn, and net profit attributable to the owners of the parent company increased 12.6% to ¥3,673mn. Net sales and operating profit achieved record highs. Even with the negative impact of increased production cost due to depreciation of the yen and rising processing charges, the gross profit margin reached 47.5% thanks to the larger sales volume of high value-added products and the rise in the overseas production ratio.

2. FY8/18 (forecast): Medical treatment fees and nursing care fees are expected to be revised, but the operating profit is forecast to increase

The forecasts for the full-year consolidated earnings for FY8/18 are for net sales to increase 2.8% YoY to ¥17,500mn, operating profit to rise 2.5% to ¥5,373mn, recurring profit to climb 2.0% to ¥5,448mn, and net profit attributable to the owners of the parent company to increase 1.8% to ¥3,739mn. Medical treatment fees and nursing care fees are expected to be revised in the spring of 2018, and the Company is aiming to expand sales, particularly of its mainstay healthcare wear products. It is also forecasting that it will absorb the higher costs by the continuing rise in the overseas production ratio and other means, to maintain the increase in operating profit.

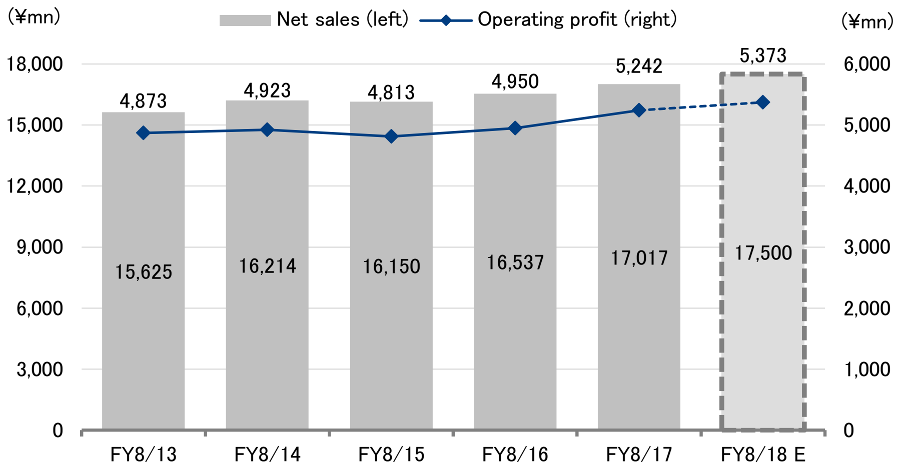
3. Actively returns profits to shareholders: From FY8/17, increased the annual dividend from ¥50 to ¥60

Based on the results in the previous fiscal year (FY8/17), the Company announced that it had rolled over the targets up to that time and set new medium-term management targets for FY8/20, of net sales of ¥18,500mn and operating profit of ¥5,600mn. It would seem to be aiming to achieve these targets through expanding overseas production and strengthening high-end products that have significant profit margins. The Company is also actively returning profits to shareholders. It has pledged a dividend payout ratio of above 50% (on a non-consolidated basis) and in FY8/17, it increased the annual dividend from the ¥50 up to that time to ¥60. It has also declared that it will flexibly buy back its own shares, and its approach toward returning profits to shareholders would seem worthy of praise.

Key Points

- Net sales and operating profit exceeded forecasts to achieve record highs in FY8/17
- Mid-term Management Plan target aims for operating profit of ¥5,600mn in FY8/20
- Increased the annual dividend to ¥60 and is actively returning profits to shareholders, including by buying back its owns shares

Trends in net sales and operating profit (consolidated)



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

Company profile

Leading manufacturer of medical gowns with a domestic market share of over 60%

Nagaileben is a specialist manufacturer of medical gowns for nurses, doctors, patients and others. Established in 1915 as Nagai Shoten, the Company has a rich history. Since then, it has expanded its operations nationally to become a leading domestic manufacturer with a share of over 60% of the market for medical gowns for nurses.

History

1915	Founded business specializing in medical gowns in Kanda-Jinbocho in Tokyo, Japan, as Nagai Shoten, privately owned by Koji Nagai.
1950	Liquidated Tokyo Eisei Hakui Co. Ltd. Koji Nagai and Tatsuro Sawanobori jointly established Nagai Shoten Co. Ltd.
1969	Established a subsidiary, Nagai Hakui Kogyo Co. Ltd., in Akita Prefecture to expand the medical gowns manufacturing division. Tatsuro Sawanobori was appointed President. Shifted focus of manufacturing and sales business specialization from multi-purpose white gowns to medical gowns.
1977	Built second product center in Kameido, Tokyo. Established a partnership with a US company, G.D. Searle & Company, and established Japan Surgical Apparel Co. Ltd. in Hiroshima to expand sales of new surgical apparel products for hospitals.
1978	Established technology partnerships with Angelica Corp (US) and Toray Industries, Inc. Developed and released medical gowns made with a new fabric for leasing.
1980	Changed name to Nagai Co. Ltd. Opened a sales office in Takamatsu, Kagawa Prefecture. Concluded a license agreement with designer Kansai Yamamoto.
1982	Concluded a license agreement with designer Yukiko Hanai.
1988	Established Emit Co. Ltd. as a spin-off from Nagai Co. Ltd. Thereafter, the two companies exchanged their names, with Emit Co. Ltd. becoming a group management company, and Nagai Co. Ltd. becoming a group headquarters for sales.
1989	Newly built Nagai Luminous, a manufacturing plant for high-grade products, in Akita Prefecture. Started overseas production toward the global division of labor.
1994	Changed name from Nagai Co. Ltd. to Nagaileben Co. Ltd. Built a new logistics center in Akita Prefecture.
1995	Started over-the-counter trading of the Company's stock. Started development and sales of a second pillar product to respond to the aging of society. Vice President Ichiro Sawanobori appointed President.
1996	Concluded a license agreement with French designer Andre Courreges.
1999	Opened a sales office in Nagoya, Aichi Prefecture. Concluded a license agreement with designer Atsuro Tayama.
2001	Listed on the Second Section of Tokyo Stock Exchange.
2002	Established a technology partnership with Standard Textile Company, Inc. (US) and Toray Industries, Inc. for surgical textiles. Raised the status of the Nagoya sales office to a branch.
2004	Acquired ISO 9001. Listed on the First Section of Tokyo Stock Exchange. Absorbed Hokkaido Nagai Co. Ltd. and established the Hokkaido branch.
2005	Acquired ISO 14001. Concluded a license agreement with designer Keita Maruyama.
2006	Concluded a brand agreement with designer Minako Yokomori.
2014	Relocated to a new head office building in Kajicho, Chiyoda Ward, Tokyo.
2015	Held ceremony to commemorate its 100th anniversary.

Source: Prepared by FISCO from Company materials

Business overview

Focusing on expanding sales of high value-added, advanced-function products

1. Sales breakdown

All of the Company's products are medical gowns and related products. The contribution to sales by item (FY8/17) is 58.4% from healthcare wear, 15.7% from doctors' wear, 3.3% from utility wear, 10.5% from patient wear, 9.6% from surgical wear, 1.2% from shoes, and 1.3% from other products. Healthcare wear consists mainly of products for nurses, and utility wear consists of aprons, cardigans, and other items worn as outer garments. Profit margins for each item do not vary significantly, but the profit margins of purchased products, such as shoes and other products, are relatively lower.

In terms of each region's contribution to sales (FY8/17), eastern Japan accounts for 52.9%, western Japan 35.7%, central Japan 10.3%, and overseas 1.1%. While coverage is nationwide, sales in western Japan and overseas remain low, indicating the potential for future expansion.

The product categories were changed from FY8/17. The Company's own brand of high-priced products, together with the products previously in the DC brand, became the "high-end products" category, and products that up to that time were called advanced-function products have been redefined and categorized as "high value-added products." The name of the standard-function products category was changed to "value-added products," while the mass-produced products category has been left unchanged.

In the new categories, the percentages of total net sales by product (FY8/17) are 7.0% from high-end products, 50.6% from high value-added products, 37.3% from value-added products, and 5.1% from mass-produced products. On looking at the approximate price-band classifications in nurse wear, mass-produced products are less than ¥5,000, value-added products are ¥5,000 to ¥7,500, high value-added products are ¥7,500 to ¥10,000, and high-end products are more than ¥10,000. The tendency is for the higher the price, the greater the profit margin, so the Company is focusing on expanding sales of high-end products and high value-added products.

2. Sales channels and production status

The Company's end users include nurses and doctors, with the purchasers of the products mainly being medical facilities such as hospitals, nursing care facilities, and other such facilities. However, the Company does not conduct direct sales, with 100% of sales being agency sales via medical equipment wholesalers that sell to these medical and other facilities. As a result, sales expenses are kept down, but the Company is still able to understand customers' needs as the sales staff is constantly in contact with large hospitals and other facilities.

In most cases up until recently, medical gowns were laundered within the hospitals by the hospitals themselves, but in recent years they have been switching to leasing alongside the spread in laundry outsourcing. The lease term is typically four years. Because this generates lease switching demand every four years, it seems to stably support the Company's earnings. However, the lease renewal cycle does not necessarily occur in the same time period as the previous time and there are cases of it being slightly before or after, so sometimes a slight shifting occurs for the net sales (YoY) for each quarter.

Looking at the Company's production structure, based on FY8/17 performance, internal production and at partner plants constitute an aggregate of 98.7% (50.6% domestically and 48.1% overseas), with purchased products accounting for 1.3%. Overseas production predominantly takes place in Indonesia, Vietnam, and China, but the Company owns no plants and the goods are produced at the plants of its local partners, which mitigates investment risk and reduces costs.

3. Characteristics and strengths

The Company is a specialized manufacturer of medical gowns, and one of its strengths is that it has in place an integrated system to undertake every aspect of this business, from planning through to raw material procurement, manufacturing, and sales. In its product planning, it can accurately understand customer needs and reflect them in its products. Specifically, the Company sells products that are easy to work in while incorporating anti-static, antibacterial, and other functions, as well as featuring excellent designs, and they have earned excellent reputations among their users. At the same time, it deals directly with major synthetics manufacturers and textiles traders, including Toray Industries, Inc. <3402>, with which it is jointly developing materials, so it is able to secure optimal materials and products at low costs while selling them at appropriate margins.

Furthermore, in addition to its large number of affiliated plants, the Company has the necessary financial resources to be able to constantly maintain product item inventories that extend into the thousands of varieties, while also being able to swiftly respond to a broad range of user needs, including for made-to-order products, through a rapid production and sales system (the quick response system) that delivers the desired product on the specified day. This has also helped to earn it the strong trust of its customers. On the sales side, it has a network of close to 1,000 agents nationwide, and while its sales capabilities are robust, the Company itself keeps down its sales expenses as much as possible.

As a result, the Company's share of the domestic market for medical gowns for nurses exceeds 60%, and it maintains a firm position as the leading medical gown manufacturer in Japan. Additionally, it is maintaining profitability with a gross profit margin of 47.5% (actual results for FY8/17). The fact that it is both highly profitable and has a high market share demonstrates that most of its customers are satisfied with its products and services, which is the Company's greatest strength.

By concentrating its business resources in the niche market of medical gowns, the Company can efficiently manage every aspect of its business, from planning through to manufacturing and sales. Moreover, although it is a niche market, there remains room for further development, as the Company has relatively low shares of the peripheral markets for patient wear, surgical wear, and other items. The Company has explicitly stated that the medical gown business could grow for some time and that it will take active steps to develop the peripheral markets.

4. Company policy (initiatives for CSR/ESG)

The Company commemorated its centennial in 2015, by cultivating a corporate culture called Nagaism that is focused on realizing interpersonal harmony, generating profits, and contributing to society. It has undertaken the following specific initiatives for CSR/ESG.

(1) Expanding women's roles: Supporting industries led by women

The Company's products are for women working on the frontlines at hospitals and nursing care facilities, and its production facilities have many women involved in sewing work. The Company's business operations create many opportunities to expand the roles of women from a variety of life stages, which connects to supporting working women.

(2) Contributing to communities

a) Contributing to communities through production sites

The Company is creating employment and contributing to regional economies through its production operations in Akita Prefecture in Japan, in Dalian in China, and also in Indonesia, Vietnam, and elsewhere overseas.

b) Medical kids project

This project started from the idea of deepening interaction between hospitals and local communities and enabling children to attend hospitals or undergo hospitalization with ease of mind. Child-sized medical gowns resembling those worn by doctors and nurses are lent to hospitals and a Miffy character makes hospital visits.

(3) Contributing to customers: Opened the ITONA® gallery, an oasis for nurses

The ITONA® gallery, Japan's first communication space for nurses, was opened in 2015 to celebrate the centenary of foundation and as a gesture of gratitude to nurses, the Company's main customers.

(4) Social contribution

a) Promotion of the employment of disabled persons

The Company actively employs people with disabilities and was awarded by the Ministry of Health, Labour and Welfare in September 2016 as an outstanding business in terms of contribution to the employment and promotion of people with disabilities.

b) Disaster support activities

Monetary donations, provision of medical gowns and presentation of wheelchairs and other items has been made through nursing associations or the Japanese Red Cross Society following the outbreak of SARS and natural disasters including the Indonesian earthquake, the Great Hanshin Earthquake, the Great East Japan Earthquake and the Kumamoto earthquakes.

(5) Environmental initiatives

The Company secured ISO 14001 certification in 2005. Cutting wastage from raw materials is reused for roofing processing and other purposes. The Company has also developed and sells COMPELPAK, a reusable product for use on surgical front lines. By converting to a reusable product instead of the disposable type that had been used until now, it enables medical waste to be reduced and contributes to solving environmental problems.

Results trends

Net sales and operating profit achieved record highs in FY8/17

● Summary of the FY8/17 consolidated results

(1) Profit-and-loss conditions

In the consolidated results for FY8/17, net sales increased 2.9% YoY to ¥17,017mn, operating profit rose 5.9% to ¥5,242mn, recurring profit rose 8.2% to ¥5,340mn, and net profit attributable to the owners of the parent company climbed 12.6% to ¥3,673mn. Net sales and operating profit achieved record highs. The gross profit margin reached 47.5% thanks to increased sales of high value-added products, further shift toward overseas production, absorbing increased costs caused by depreciation of the yen and rising processing charges.

Summary of the FY8/17 consolidated results

(¥mn)

	FY8/16		FY8/17			
	Amount	% of total	Amount	% of total	Change	YoY
Net sales	16,537	100.0	17,017	100.0	479	2.9
Gross profit	7,735	46.8	8,086	47.5	350	4.5
SG&A expenses	2,784	16.9	2,843	16.7	59	2.1
Operating profit	4,950	29.9	5,242	30.8	291	5.9
Recurring profit	4,937	29.9	5,340	31.4	402	8.2
Net profit attributable to the owners of the parent company	3,262	19.7	3,673	21.6	411	12.6

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

The market environment and the industry environment were generally stable, as had been initially forecast. In this environment, the Company secured renewal demand for its mainstay healthcare wear, while patient wear and surgical wear—peripheral markets being focused on—were steady, exceeding the forecast to reach record-high net sales.

The gross profit margin improved 0.7 of a percentage point YoY to 47.5% (46.8% in the previous fiscal year). Gross profit rose ¥350mn, with the main factors being an increase of ¥415mn due to the higher sales and a decrease of ¥64mn because of production factors. Breaking down these production factors, it decreased ¥48mn from the higher processing charges and ¥73mn from the effects of the exchange rate on cost prices (FY8/16, ¥99.8/dollar→FY8/17, ¥104.0/dollar), but increased ¥52mn from the rise in the overseas production ratio (FY8/16, 47.4%→FY8/17, 48.1%). On the other hand, there were no special factors in SG&A expenses and they increased only slightly, up 2.1% to ¥2,843mn, which was basically in line with the initial forecast. As a result, operating profit grew 5.9% YoY and achieved a record high.

Recurring profit increased 8.2% YoY, increased more than in operating profit, but this was mainly due to the effects of foreign exchange gains and losses in non-operating profit and expenses (a gain of ¥44mn in FY8/17, compared to a loss of ¥70mn in previous year). In extraordinary profit and loss, there were no major fluctuations or unexpected events, but the corporate tax amount decreased following the lowering of the tax rate, so net profit attributable to the owners of the parent company increased 12.6% YoY. Taken as a whole, the results can be said to be favorable and greater than expected.

a) Net sales by item

In net sales by item, healthcare wear increased 2.8% YoY to ¥9,940mn, doctors' wear rose 1.0% to ¥2,681mn, utility wear decreased 7.4% to ¥557mn, patient wear climbed 10.7% to ¥1,786mn, surgical wear increased 3.8% to ¥1,634mn, shoes decreased 0.8% to ¥203mn, and other products increased 0.3% to ¥214mn.

In the mainstay healthcare wear, orders trended favorably for the new high value-added products and sales grew steadily, particularly in eastern Japan. In doctors' wear, sales conditions have been difficult for mass-produced products, but sales still increased YoY thanks to the strong performance of high-end products. Sales fell in utility wear, in which the trend of the transition from individual supply to common goods is continuing, but this decrease was within the expected range and is not a particular cause for concern. Moreover, as its monetary contribution is small, the impact of this decrease on the overall results was negligible.

In the peripheral markets, which have come to be focused on in recent years, sales continued to grow significantly in patient wear due to the market's favorable reception to the Company's value-added products. This is occurring against the backdrop of market expansion from the spreading use of hospitalization sets. Higher sales were also secured in surgical wear, driven by the performance of COMPELPAK. As the sales amount of shoes and other products are small, their impact on the overall results was negligible.

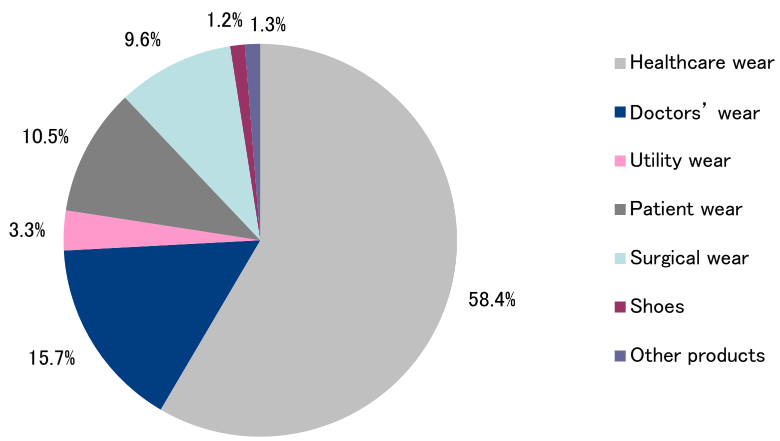
Net sales by item

(¥mn, %)

	FY8/16		FY8/17	
	Amount	YoY	Amount	YoY
Healthcare wear	9,674	2.6	9,940	2.8
Doctors' wear	2,654	2.0	2,681	1.0
Utility wear	601	-10.3	557	-7.4
Patient wear	1,613	11.1	1,786	10.7
Surgical wear	1,574	0.9	1,634	3.8
Shoes	204	-3.1	203	-0.8
Other products	213	-3.9	214	0.3
Total	16,537	2.4	17,017	2.9

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

Net sales by item (FY8/17)



Source: Prepared by FISCO from Company materials

b) Net sales by region

By region, in eastern Japan, net sales increased 5.5% YoY to ¥9,007mn; in central Japan, they grew 2.3% to ¥1,756mn; in western Japan, they decreased 0.2% to ¥6,068mn; and overseas, they fell 8.2% to ¥184mn. The positive performance in eastern Japan was because, in addition to steady orders for renewal projects, the Company acquired new projects and also from the effects of the growth in sales of patient wear, and this region drove the overall increase in sales. The scale of the central Japan market is small so its results are greatly affected by the number of projects, but it still secured higher sales YoY. The result in western Japan was a reaction to the previous fiscal year, in which there was special demand for large-scale projects, but sales were still maintained at practically the same level YoY, including from steady orders for renewal projects and an increase in market share by acquiring new projects. The scale of overseas sales is still small, and they also declined as a reaction to the previous fiscal year, in which there were deliveries to large-scale hospitals.

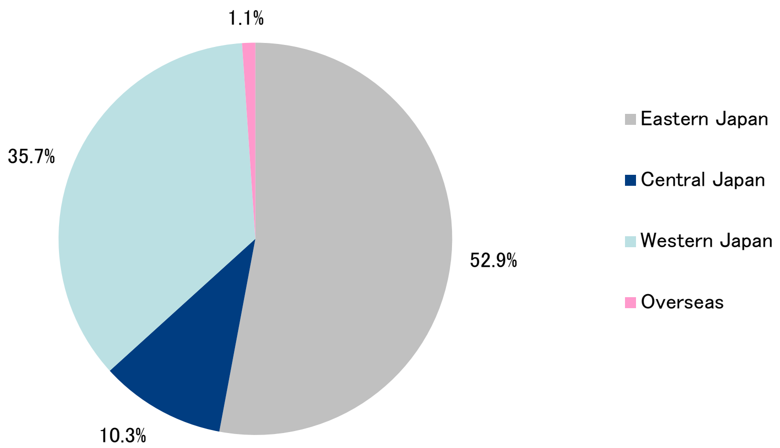
Net sales by region

(¥mn, %)

	FY8/16		FY8/17	
	Amount	YoY	Amount	YoY
Eastern Japan	8,539	2.2	9,007	5.5
Central Japan	1,717	-3.2	1,756	2.3
Western Japan	6,080	4.1	6,068	-0.2
Overseas	200	14.1	184	-8.2
Total	16,537	2.4	17,017	2.9

Source: Prepared by FISCO from Company materials

Net sales by region (FY8/17)



Source: Prepared by FISCO from Company materials

c) Net sales by product

By product, for high-end products, net sales increased 7.9% YoY to ¥1,191mn; for high value-added products, they grew 3.3% to ¥8,612mn; for value-added products, they rose 2.3% to ¥6,343mn; and for mass-produced products, they decreased 3.1% to ¥869mn. In high-end products, despite the slump in sales for the DC brand, an increase in sales was secured for high-end products as a whole, driven by the performance of the Company's own brand of high-priced products. Sales also steadily increased of high value-added products, which is the market's volume zone and where the Company is focusing most on expanding sales, while sales also grew of general value-added products. Sales of mass-produced products slumped, but their sales scale is small and it is not a market that the Company is especially focusing on, so this result is not a particular cause for concern.

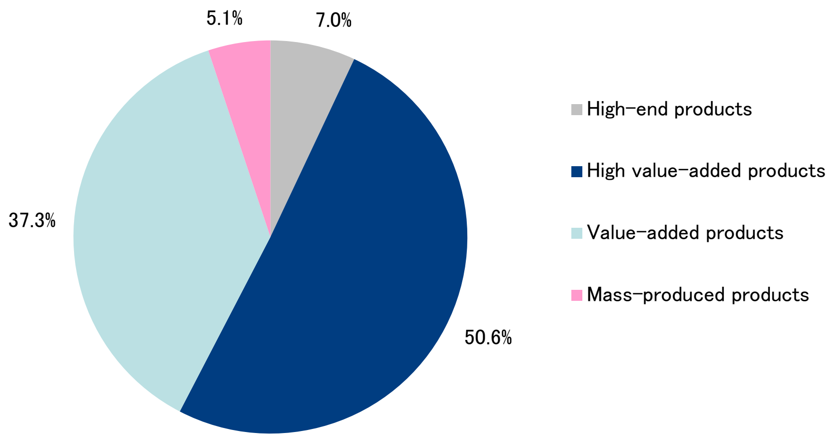
Net sales by product

(¥mn, %)

	FY8/16		FY8/17	
	Amount	YoY	Amount	YoY
High-end products	1,104	0.9	1,191	7.9
High value-added products	8,336	6.3	8,612	3.3
Value-added products	6,199	-0.9	6,343	2.3
Mass-produced products	896	-6.6	869	-3.1
Total	16,537	2.4	17,017	2.9

Source: Prepared by FISCO from Company materials

Net sales by product (FY8/17)



Source: Prepared by FISCO from Company materials

The financial position is solid, with cash at the end of the period of ¥22.7bn and a shareholders' equity ratio of 89.2%

(2) Financial position

The Company's financial position continues to be stable. Total assets at the end of FY8/17 were ¥40,951mn, up ¥2,093mn compared to the end of the previous fiscal year. Current assets were ¥32,325mn, an increase of ¥3,242mn, with the main factors being increases in cash and deposits of ¥3,257mn, a decrease in notes and accounts receivable of ¥922mn and a decrease in inventories of ¥36mn. Fixed assets were ¥8,626mn, down ¥1,148mn, primarily due to a decrease of ¥925mn in investments and other assets accompanying the transfer of long-term deposits to current assets.

Total liabilities were ¥4,405mn, up ¥50mn compared to the end of the previous fiscal year. The main factors included a decrease in notes and accounts payable of ¥132mn and a decrease in income tax payable of ¥57mn. Net assets were ¥36,545mn, an increase of ¥2,043mn. This was mainly due to an increase in retained earnings of ¥2,011mn following the recording of net profit. As a result of these factors, the equity ratio at the end of FY8/17 was 89.2%, increasing 0.4 of a percentage point from the previous year-end.

Summary of the consolidated balance sheet

(¥mn)

	End of FY8/16	End of FY8/17	Change
Cash and deposits	19,504	22,762	3,257
Notes and accounts receivable	4,866	3,944	-922
Inventories	4,348	4,311	-36
Current assets, total	29,083	32,325	3,242
Tangible fixed assets	7,476	7,256	-219
Intangible fixed assets	57	54	-3
Investments and other assets	2,240	1,315	-925
Fixed assets, total	9,774	8,626	-1,148
Total assets	38,857	40,951	2,093
Notes and accounts payable	1,561	1,428	-132
Income taxes payable	1,149	1,091	-57
Total liabilities	4,355	4,405	50
Retained earnings	34,978	36,989	2,011
Treasury shares	-4,902	-4,902	-
Net assets, total	34,501	36,545	2,043
Net liabilities and net assets	38,857	40,951	2,093

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

(3) Cash flow conditions

In FY8/17, cash flow provided by operating activities was ¥3,979mn. The main income items were the recording of net income before income taxes of ¥5,341mn, depreciation and amortization of ¥311mn, and a decrease in notes and accounts receivable of ¥116mn, while the main expenditure items included a decrease in accounts payable of ¥132mn. Cash flow used in investing activities was ¥4,389mn, which was primarily due to the acquisition of tangible fixed assets of ¥102mn and fixed deposits (net) of ¥4,400mn. Cash flow used in financing activities was ¥1,662mn, with the main item being ¥1,662mn for dividend payout. As a result, cash and cash equivalents during the fiscal period declined ¥2,042mn, and the balance of cash and cash equivalents at the end of the fiscal period was ¥4,662mn. The Company does not have any interest-bearing debt, and in addition, it holds ¥4,902mn of treasury stock (4,989,551 stocks). Therefore, as before it has an abundance of cash on hand.

Summary of the consolidated cash flow statement

(¥mn)

	FY8/16	FY8/17
Cash flow from operating activities	3,565	3,979
Net income before income taxes	4,934	5,341
Depreciation and amortization	331	311
Change in notes and accounts receivable-trade	-180	116
Change in inventory assets	-148	36
Change to accounts payable	162	-132
Cash flow from investing activities	-1,997	-4,389
Acquisition of tangible fixed assets	-151	-102
Change in fixed deposits (net)	-2,000	-4,400
Cash flow from financing activities	-3,324	-1,662
Dividend payout	-3,324	-1,662
Change to cash and cash equivalents	-1,787	-2,042
Balance of cash and cash equivalents at period end	6,704	4,662

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

Business outlook

Higher profits are forecast in FY8/18 also, with record highs expected

● FY8/18 full-year outlook

(1) Outlook of profit and loss

The Company's forecasts for the full-year consolidated result for FY8/18 are for net sales to increase 2.8% YoY to ¥17,500mn, operating profit to rise 2.5% to ¥5,373mn, recurring profit to climb 2.0% to ¥5,448mn, and net profit attributable to the owners of the parent company to increase 1.8% to ¥3,739mn. The assumptions for the full fiscal year forecasts are described below, but the Company is forecasting that the gross profit margin will fall slightly and the exchange rate is expected to be less than favorable, so it can be said that these are fairly firm forecast values.

FY8/18 consolidated earnings outlook

(¥mn, %)

	FY8/17		FY8/18 forecast			
	Amount	% of total	Amount	% of total	Change	YoY
Net sales	17,017	100.0	17,500	100.0	483	2.8
Gross profit	8,086	47.5	8,260	47.2	174	2.2
SG&A expenses	2,843	16.7	2,886	16.5	43	1.5
Operating profit	5,242	30.8	5,373	30.7	131	2.5
Recurring profit	5,340	31.4	5,448	31.1	108	2.0
Net profit attributable to the owners of the parent company	3,673	21.6	3,739	21.4	66	1.8

Source: Prepared by FISCO from Company materials

The Company is forecasting that the gross profit margin will fall slightly YoY to 47.2% (47.5% in FY8/17). Gross profit is expected to climb ¥174mn, with the positive factors forecast to be increases of ¥221mn from higher sales, and ¥53mn from the rise in the overseas production ratio (FY8/17 48.1%→FY8/18 48.8%), and the negative factors being ¥15mn from the effects of the higher processing charges, etc., and ¥106mn from the effects of the exchange rate (FY8/17 ¥104/dollar→FY8/18 ¥110/dollar) on costs. However, with regards to the exchange rate, it has already reserved a rate for practically the entire 1H of ¥108 to ¥109, so the actual average rate may be lower than ¥110.

SG&A expenses are forecast to be ¥2,886mn (up 1.5% YoY), which was an increase accompanying an expansion of sales rather than an increase for a special reason. Therefore, operating profit is expected to be ¥5,373mn, which will once again be a record high. In addition, if a higher-than-expected gross profit margin is achieved, operating profit will highly likely be revised upward. Moreover, the forecast assumes that the effects of the exchange rate on costs in non-operating profit will be zero, and both recurring profit and net profit attributable to the owners of the parent company are expected to increase YoY.

a) Net sales forecasts by item

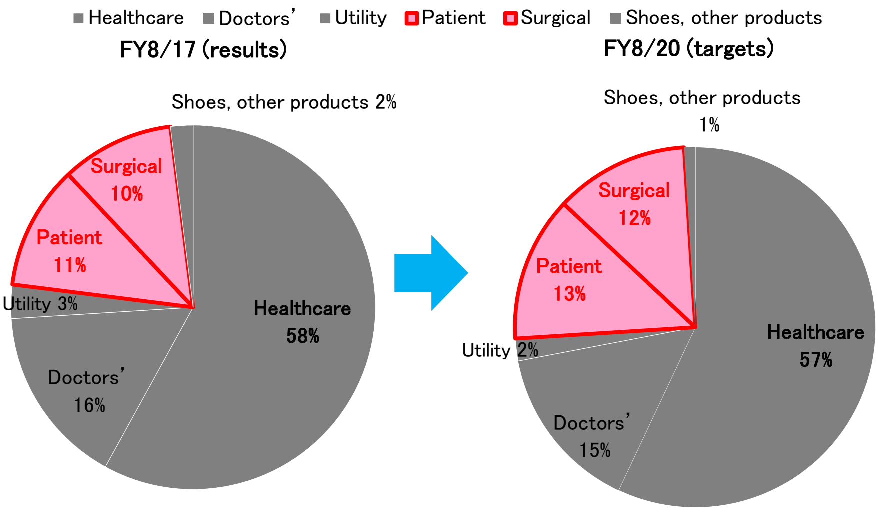
Net sales forecasts by item

(¥mn, %)

	FY8/17		FY8/18 forecast	
	Amount	YoY	Amount	YoY
Healthcare wear	9,940	2.8	10,210	2.7
Doctors' wear	2,681	1.0	2,750	2.6
Utility wear	557	-7.4	510	-8.5
Patient wear	1,786	10.7	1,920	7.5
Surgical wear	1,634	3.8	1,700	4.0
Shoes	203	-0.8	200	-1.5
Other products	214	0.3	210	-2.0
Total	17,017	2.9	17,500	2.8

Source: Prepared by FISCO from Company materials

Targeted net sales percentage by item



Source: Prepared by FISCO from Company materials

In net sales by item, healthcare wear is forecast to be ¥10,210mn (up 2.7% YoY), doctors' wear ¥2,750mn (up 2.6%), utility wear ¥510mn (down 8.5%), patient wear ¥1,920mn (up 7.5%), surgical wear ¥1,700mn (up 4.0%), shoes ¥200mn (down 1.5%), and other products ¥210mn (down 2.0%).

In healthcare wear, the revitalization of the market from the launch of the new high value-added products and the resulting steady increase in sales are expected to continue. In doctors' wear, conditions will be severe for mass-produced products, but the forecast is for high-end products to perform strongly and for results to trend stably. The utility wear market is shrinking and sales are expected to continue to decrease. For patient wear, the Company is forecasting that the major increase in sales will continue from the effects of new products, against the backdrop of the strong growth in demand in this market. Higher sales are also expected in surgical wear from eliminating the cap at the COMPELPAK laundry sterilization plant and through developing new customers.

b) Forecasts for net sales by region

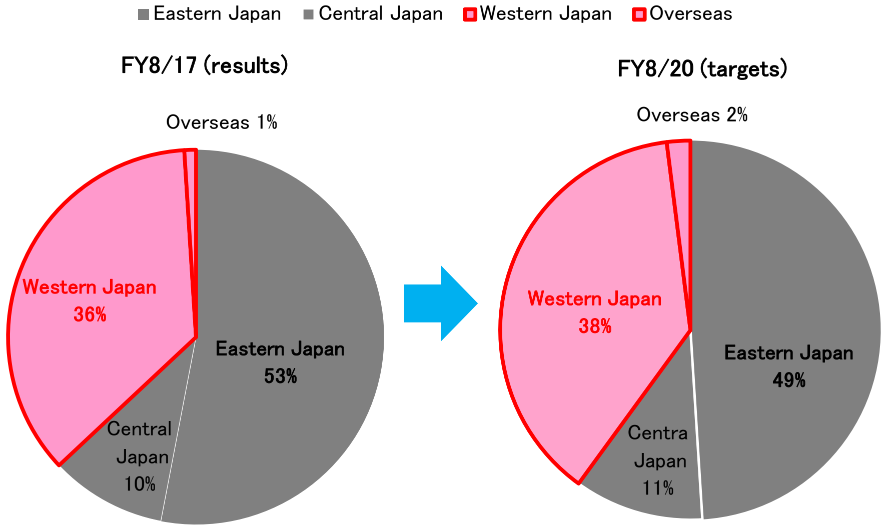
Forecasts for net sales by region

(¥mn, %)

	FY8/17		FY8/18 forecast	
	Amount	YoY	Amount	YoY
Eastern Japan	9,007	5.5	9,190	2.0
Central Japan	1,756	2.3	1,810	3.0
Western Japan	6,068	-0.2	6,300	3.8
Overseas	184	-8.2	200	8.4
Total	17,017	2.9	17,500	2.8

Source: Prepared by FISCO from Company materials

Targeted net sales percentages by region



Source: Prepared by FISCO from Company materials

The forecasts for net sales by region are ¥9,190mn in eastern Japan (up 2.0% YoY), ¥1,810mn in central Japan (up 3.0%), ¥6,300mn in western Japan (up 3.8%), and ¥200mn overseas (up 8.4%).

In eastern Japan, the Company expects sales to continue to increase from securing demand for renewal projects by proposing new high value-added products. In central Japan and western Japan, the Company is aiming to achieve sales growth YoY by focusing on increasing market share through strengthening sales promotions. Overseas results will be affected by exchange rates, but the Company plans to utilize its name recognition and focus on expanding sales. The plan is to increase sales in every region and to achieve record highs for net sales.

c) Net sales forecasts by product

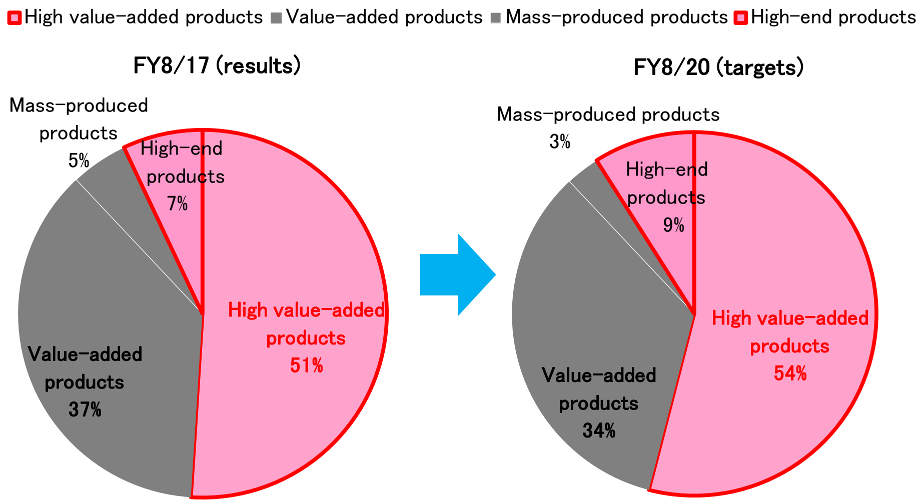
Net sales forecasts by product

(¥mn, %)

	FY8/17		FY8/18 forecast	
	Amount	YoY	Amount	YoY
High-end products	1,191	7.9	1,280	7.4
High value-added products	8,612	3.3	8,980	4.3
Value-added products	6,343	2.3	6,400	0.9
Mass-produced products	869	-3.1	840	-3.4
Total	17,017	2.9	17,500	2.8

Source: Prepared by FISCO from Company materials

Targeted net sales percentages by product



Source: Prepared by FISCO from Company materials

The net sales forecasts by product are ¥1,280mn for high-end products (up 7.4% YoY), ¥8,980mn for high value-added products (up 4.3%), ¥6,400mn for value-added products (up 0.9%), and ¥840mn for mass-produced products (down 3.4%).

In high-end products, conditions are severe for the DC brand, but the Company's luxury brands, including 4D+ and Beads Berry, are performing strongly, so the forecast for high-end products as a whole is for sales to increase. The high value-added products have been favorably received by the market and their sales are trending favorably, and the Company plans to achieve even higher sales by continuing to promote its high value-added strategy. The forecast is for sales of mass-produced products to decline, but the plan is to transfer their customers to value-added products, including to the products of other companies.

Medium- to-long-term growth strategy

Mid-term plan targets for FY8/20 of operating profit of ¥5,600mn

1. Mid-term Management Plan

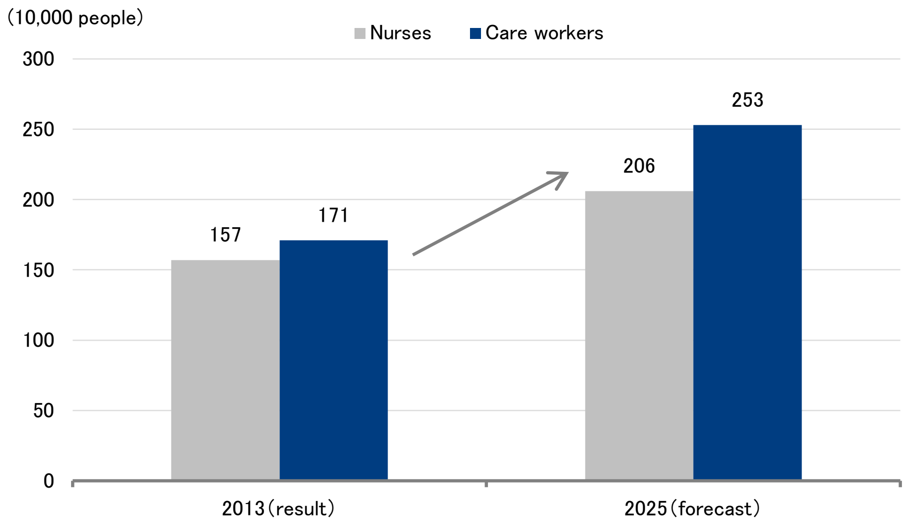
The Company initially announced targets for FY8/19 of net sales of ¥18,000mn and operating profit of ¥5,400mn in its Mid-term Management Plan. But based on the FY8/17 results, it has newly announced the plan's mid-term targets for FY8/20, of net sales of ¥18,500mn and operating profit of ¥5,600mn.

Plans to actively develop advanced-function, high value-added products

2. Future business strategies: The supporting tailwind will continue for the time being

The operating environment surrounding the Company should be favorable for some time. According to data released by the Ministry of Health, Labour and Welfare, the number of nurses in Japan is projected to increase from 1.57 million in 2013 to as many as 2.06 million in 2025. Moreover, the number of care workers is forecast to increase from 1.71 million in 2013 to 2.53 million in 2025. In this operating environment, the Company plans to achieve its medium-term growth by implementing the following strategies.

Estimates of future demand for nurses and care workers



Source: Prepared by FISCO from Company materials

(1) Marketing strategy to boost sales

a) Aim to increase share by further uncovering demand in the core markets, including the current mainstay markets for nurses and care workers.

b) In addition to the existing mainstay healthcare wear products, further develop the peripheral markets, including patient wear and surgical wear.

c) Open up new markets (for individual use, etc.) by utilizing the Company's technological expertise in materials and apparel manufacturing, and its sales network.
d) Actively open up overseas markets (particularly Taiwan).

(2) Production strategy to ensure a stable supply
a) In the context of the tightening of the domestic labor market, respond to wage increases and further strengthen the production system.
b) Strengthen collaborations with materials manufacturers and trading companies, and improve new product development capabilities.
c) Further bolster the quick response system and the ability to respond rapidly to small-lot, multi-product orders.

(3) Strategy toward stable profitability
a) Further promote the shift from domestic production to overseas production.
b) Actively utilize special tax measures, including EPA and FTA.
c) Secure business profitability through strategy of heightened added value.

Shareholder return policy

The Company has pledged a dividend payout ratio (on a non-consolidated basis) of above 50%, raised the dividend from ¥50 to ¥60

The Company's equity ratio reached 89.2% at the end of FY8/17, and it is financially stable. Additionally, considering the Company's business conditions, it seems highly unlikely that its profits will rapidly deteriorate, so continued stable earnings are expected. As a result, if its distribution of earnings outside the Company (particularly dividend payments) is low, profits will accumulate in shareholders' equity each year, and return on equity (ROE) will decline; which is to say, capital efficiency will decline. But in addition to paying dividends commensurate with the growth in profits, the Company actively and comprehensively returns profits to shareholders, including through share buybacks, and as a result has maintained a high ROE (10.3% in FY8/17).

The Company will thus maintain a stable financial position while pursuing solid shareholder returns. In FY8/15, it supplemented the regular dividend of ¥50 per share with an additional ¥50 per share to commemorate its centennial. This raised the total annual dividend to ¥100 per share, for a non-consolidated payout ratio of 107.5%. It also spent ¥1,500mn in repurchasing 1 million shares during the fiscal year, raising the total return ratio (non-consolidated basis) to 153.8%. In FY8/16, it paid an annual dividend of ¥50 for a dividend payout ratio of 52.5% on a non-consolidated basis.

The Company has pledged a dividend payout ratio of above 50% on a non-consolidated basis. In the previous fiscal year (FY8/17), it increased the annual dividend from ¥50 to ¥60, and it is also forecasting an annual dividend of ¥60 for FY8/18, which is currently underway. It may further increase the dividend if profits exceed their forecasts.

Trends in the dividend payout ratio and the total return ratio

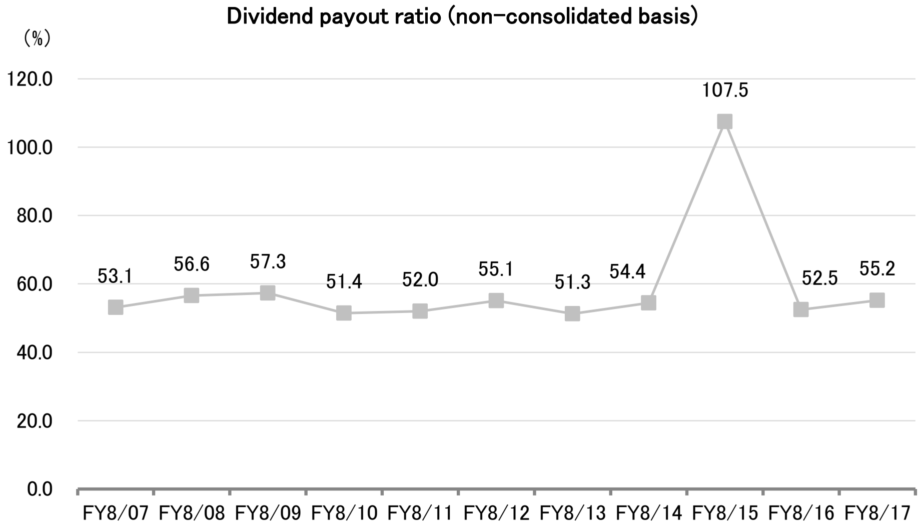
(¥mn, %)

	Total dividend amount	Share buybacks	Dividend payout ratio*	Total returns ratio*
FY8/01	475	0	27.4	27.4
FY8/02	475	0	29.3	29.3
FY8/03	530	1,697	29.7	124.6
FY8/04	744	0	36.5	36.5
FY8/05	1,117	0	56.9	56.9
FY8/06	1,117	0	53.4	53.4
FY8/07	1,117	0	53.1	53.1
FY8/08	1,083	1,077	56.6	111.2
FY8/09	1,040	1,220	57.3	122.2
FY8/10	1,127	0	51.4	51.4
FY8/11	1,205	226	52.0	61.7
FY8/12	1,205	0	55.1	55.1
FY8/13	1,541	229	51.3	58.7
FY8/14	1,712	0	54.4	54.4
FY8/15	3,324	1,500	107.5	153.8
FY8/16	1,662	0	52.5	52.5
FY8/17	1,994	0	55.2	55.2

* On a non-consolidated basis

Source: Prepared by FISCO from Company materials

Dividend payout ratio (non-consolidated basis)



Source: Prepared by FISCO from Company materials

FISCO

Disclaimer

FISCO Ltd. (the terms “FISCO”, “we”, mean FISCO Ltd.) has legal agreements with the Tokyo Stock Exchange, the Osaka Exchange,and Nikkei Inc. as to the usage of stock price and index information. The trademark and value of the “JASDAQ INDEX” are the intellectual properties of the Tokyo Stock Exchange, and therefore all rights to them belong to the Tokyo Stock Exchange.

This report is based on information that we believe to be reliable, but we do not confirm or guarantee its accuracy, timeliness,or completeness, or the value of the securities issued by companies cited in this report. Regardless of purpose,investors should decide how to use this report and take full responsibility for such use. We shall not be liable for any result of its use. We provide this report solely for the purpose of information, not to induce investment or any other action.

This report was prepared at the request of its subject company using information provided by the company in interviews, but the entire content of the report, including suppositions and conclusions, is the result of our analysis. The content of this report is based on information that was current at the time the report was produced, but this information and the content of this report are subject to change without prior notice.

The final selection of investments and determination of appropriate prices for investment transactions are decisions for the recipients of this report.

FISCO Ltd.