TOKAI Holdings
3167 Tokyo Stock Exchange
First Section

5-Jul.-16

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at the end of this document.

FISCO Ltd. Analyst
Yuzuru Sato

Total Life Concierge Accelerating Implementation of Growth Strategies

Based in Shizuoka Prefecture, Japan, TOKAI Holdings Corporation <3167> (hereafter, also “the Company”) engages in two main businesses, “energy and lifestyle-related services”, primarily the provision of liquefied petroleum gas (LPG), and “information and telecommunications services”. Aiming to become a “Total Life Concierge” (TLC), a company offering a complete range of services for everyday life, the Company started the three-year medium-term business plan, called Innovation Plan 2016 “Growing,” in FY3/15 that contains initiatives for strengthening the profitability of its businesses and is on track to largely achieving initial goals. The next medium-term plan focuses on “implementing growth strategies” and seeks to accelerate the growth pace through further improvement of group synergies.

The Company reported ¥180,940mn in net sales (-3.5% y-o-y) and ¥8,245mn in operating profit (-8.4%) as FY3/16 consolidated results. Reduction of sales prices in the gas business accompanying a drop in the procurement price weakened sales by ¥10,300mn. Additionally, the Company spent ¥3bn on sales promotion costs and other upfront costs related to expanding sales in the Hikari collaboration* business, putting pressure on profits. However, profits still beat period-start guidance because the procurement price in the gas business fell by more than expected and the Company moved forward in enhancing overall business efficiency.

* In March 2015, the Company began selling the @ T COM Hikari service and the TNC Hikari service, which bundle the Company’s ISP service with NTT’s fiber-optic cables for these services.

The Company presented FY3/17 guidance for ¥187,100mn in net sales (+3.4% y-o-y), restoring a gain for the first time in three years, and ¥12,560mn in operating profit (+52.3%), setting a new high for the first time in five years. The projected ¥4,340mn y-o-y rise in operating profit factors in income gains of ¥2,280mn for Hikari collaboration and ¥1,130mn for the Aqua business. It also includes an ¥800mn decline in goodwill amortization costs. The Company projects a rise in group customer volume from the end of FY3/16 of 47,000 contracts to 2,604,000 contracts, primarily from CATV and gas businesses. This is just over twice as many net additions as in the previous year. While income improvement in the Aqua business is a risk, we think the procurement price assumption for LP gas of $370/ton is fairly conservative in light of the current level ($325/ton in May) and expect upside in the gas business to sufficiently cover any shortfall in the Aqua business.

For shareholder returns, the Company raised the dividend per share by ¥2 y-o-y to ¥14 in FY3/16 and implemented share buybacks and other measures. These actions put the gross payout ratio at 100%. The Company aims to sharply increase the dividend by ¥8 to ¥22 with a goal of 40% for the dividend payout ratio in FY3/17. It also intends to continue reviewing share buybacks targeting healthier capital efficiency. It has been improving the content of shareholder gifts too and deserves notice as a company with an aggressive stance toward shareholder returns.

Check Point

- Expecting steep sales and profit increases in FY3/17 and all-time high profits
- Steady advances with the medium-term business plan, starting to formulate the next plan
- Aggressive shareholder returns with consecutive dividend hikes, shareholder gifts, and share buybacks

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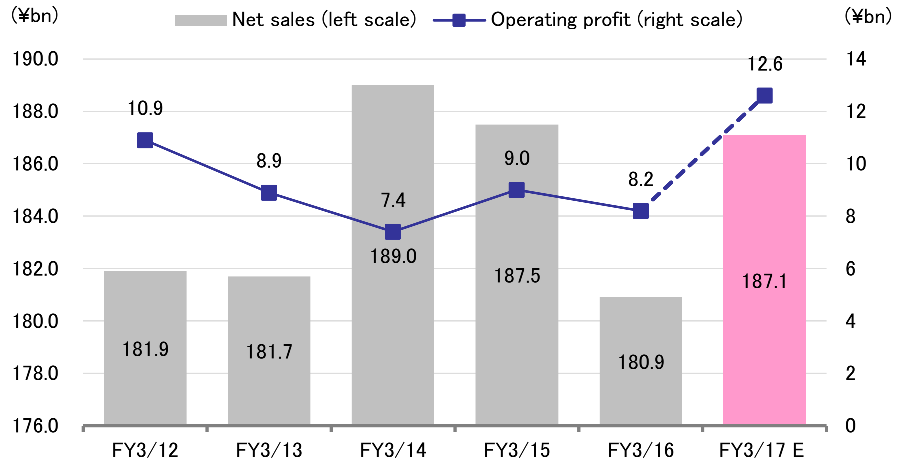
Business Performance Trends



Results Trends

Posted lower sales and profits due to external environment factors in FY3/16, though steadily increased customer volume

(1) Review of FY3/16 results

In FY3/16 consolidated results, net sales dropped 3.5% y-o-y to ¥180,940mn, operating profit fell 8.4% to ¥8,245mn, recurring profit dropped 4.7% to ¥8,150mn, and net profit attributable to owners of parent was down 12.1% to ¥3,458mn. The Company reported sales and profit declines. Reduction of sales prices accompanying a drop in the gas procurement price weakened sales (for a ¥10,300mn setback). Additionally, the Company spent ¥3bn on sales promotion costs and other upfront costs related to the Hikari collaboration business, putting pressure on profits. However, profit did not fall by much because of an increase in group-wide customer volume and time lag in lowering gas prices. The FY3/16 results also surpassed guidance targets.

While total group-wide customer volume at the end of FY3/16 missed the target (2,611,000 contracts) with an increase of 20,000 contracts from the end of the previous year to 2,558,000 contracts at year-end, we think the restoration of upward trends in CATV and gas and oil businesses that had stalled over the past few years is worth noting. Member volume for the TLC Membership Service, which strengthens contact with customers and offers benefits, expanded at a healthy pace with an increase of 96,000 contracts to 491,000 contracts.

FY3/16 Consolidated Results

(unit: ¥mn)

	FY3/15		FY3/16				
	Results	Ratio to sales	Plan	Results	Ratio to sales	YoY change	Versus guidance
Net sales	187,511	-	192,200	180,940	-	-3.5%	-5.9%
Cost of sales	118,579	63.2%	-	111,127	61.4%	-6.3%	-
SG&A expenses	59,928	32.0%	-	61,566	34.0%	2.7%	-
Operating profit	9,003	4.8%	7,760	8,245	4.6%	-8.4%	6.3%
Recurring profit	8,549	4.6%	7,410	8,150	4.5%	-4.7%	10.0%
Net profit attributable to owners of parent	3,934	2.1%	3,240	3,458	1.9%	-12.1%	6.7%

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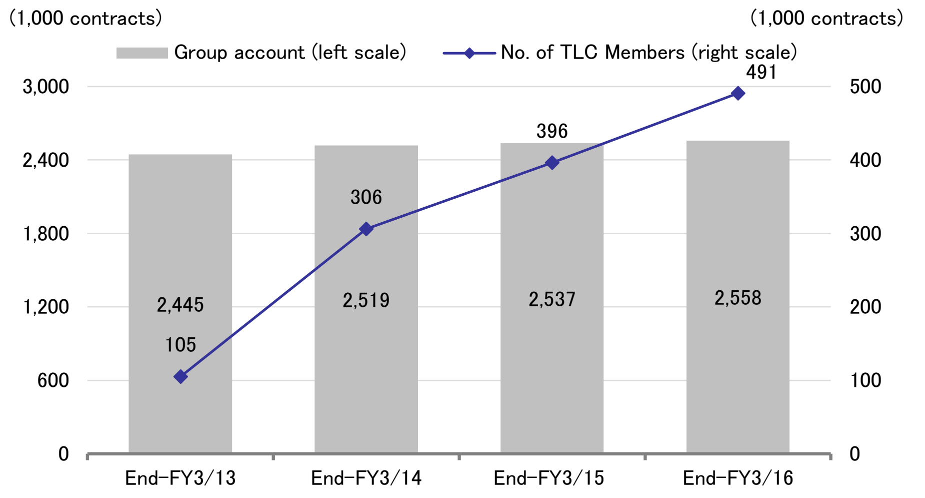
Group Number of Service Contracts



Healthy sales growth for Information and Communications, promoting further customer acquisition by allocating sales promotion costs

(2) Business segment trends

Below we review income trends by individual segments.

Net Sales Trends by Business Segment

(unit: ¥bn)

	FY3/15	FY3/16			
	Results	Initial plan	Results	YoY change	Versus guidance
Gas and Petroleum	93.1	86.1	80.7	-13.2%	-5.4
Information and Communications Services	40.1	47.2	44.2	10.3%	-3.0
CATV	24.4	24.8	24.6	1.0%	-0.2
Construction and Real Estate	20.0	22.7	21.0	4.8%	-1.7
Aqua	5.0	5.8	5.5	10.7%	-0.3
Other Businesses and Adjustments	5.0	5.5	4.9	-2.2%	-0.6
Total	187.5	192.2	180.9	-3.5%	-11.3

Operating Profit Trends by Business Segment

(unit: ¥bn)

	FY3/15	FY3/16			
	Results	Initial plan	Results	YoY change	Versus guidance
Gas and Petroleum	7.7	7.9	9.0	+1.3	+1.1
Information and Communications Services	5.0	2.7	2.3	-2.6	-0.4
CATV	1.7	1.8	2.0	+0.3	+0.2
Construction and Real Estate	1.0	1.4	1.3	+0.2	-0.1
Aqua	-1.3	-1.0	-1.1	+0.2	-0.1
Other Businesses and Adjustments	-5.0	-5.1	-5.2	-0.2	-0.1
Total	9.0	7.8	8.2	-0.8	+0.4

Note: Values prior to allocating indirect costs and other expenses

Customer Numbers by Services

(unit: 1,000 contracts)

	End-FY3/15	End-FY3/16			
	Results	Initial plan	Results	YoY change	Versus guidance
Gas (LP gas, city gas)	626	639	634	+8	-5
Information and telecommunications (fixed line and Wi-Fi)	864	881	852	-12	-29
(Hikari collaboration)	4	320	219	+215	-101
Information and telecommunications (mobile)	235	240	236	+1	-4
CATV	690	712	710	+20	-2
Aqua	130	146	133	+3	-13
Security	18	18	18	-0	±0
Total	2,537	2,611	2,558	+20	-53

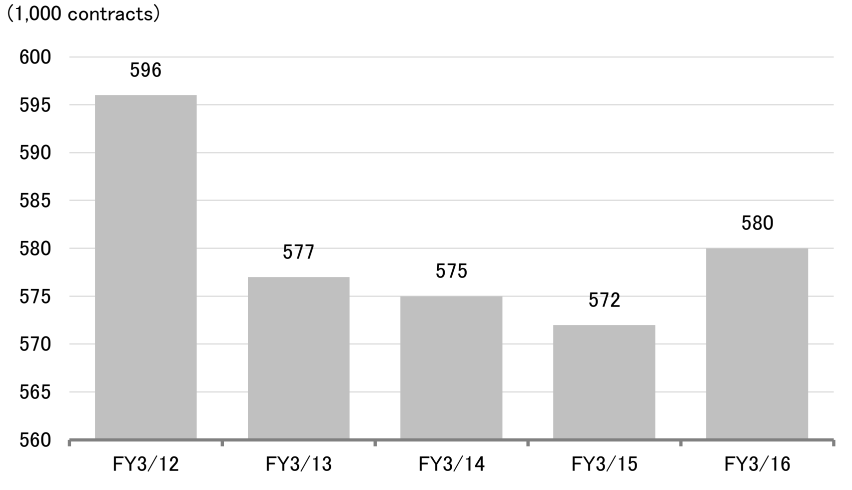
○Gas and Petroleum business

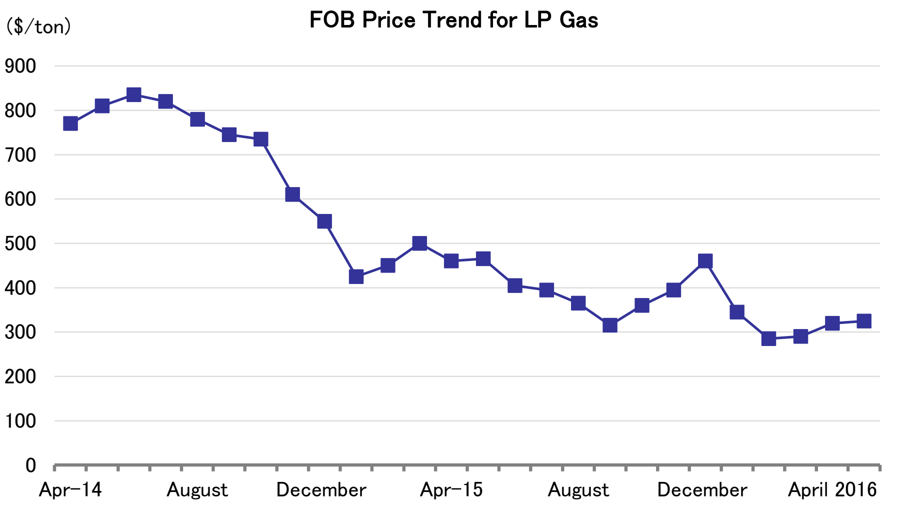
In the Gas and Petroleum business, sales dropped 13.2% to ¥80,700mn and operating profit rose by ¥1,300mn to ¥9,000mn. Customer numbers in the mainstay LP gas business climbed for the first time in seven years with an increase of 8,000 contracts to 580,000 contracts, thanks to expansion of sales coverage to southern Tohoku and Aichi areas and success in ongoing efforts to prevent churn, and were roughly unchanged in the city gas business at 54,000 contracts. While sales volumes stayed at flat levels y-o-y because of the warm winter impact, the Company incurred a setback in sales of ¥10,300mn due to lowered sales prices (11.1%) accompanying the decline in procurement prices.

The decline in unit costs related cheaper procurement prices provided the bulk of the increase in operating profit. The Company's average procurement price per ton of LP gas fell 37% to ¥47,829 in FY3/16, from FY3/15's ¥75,790, due to the CP price drop. Higher marketing costs related to expansion of sales areas, meanwhile, largely offset the profit boost from reduction of indirect costs from improving business efficiency.

Compared to period-start guidance, sales missed by ¥5,400mn due to a shortfall of 5,000 contracts in customer volume and lower sales prices, but operating profit overshot by ¥1,100mn mainly on a drop in the procurement price.

Trends in LP Gas Customer Numbers





Source: Japan LP Gas Association, FOB price (contract price from Saudi Arabia to import firms)

○Information and Communications Services business

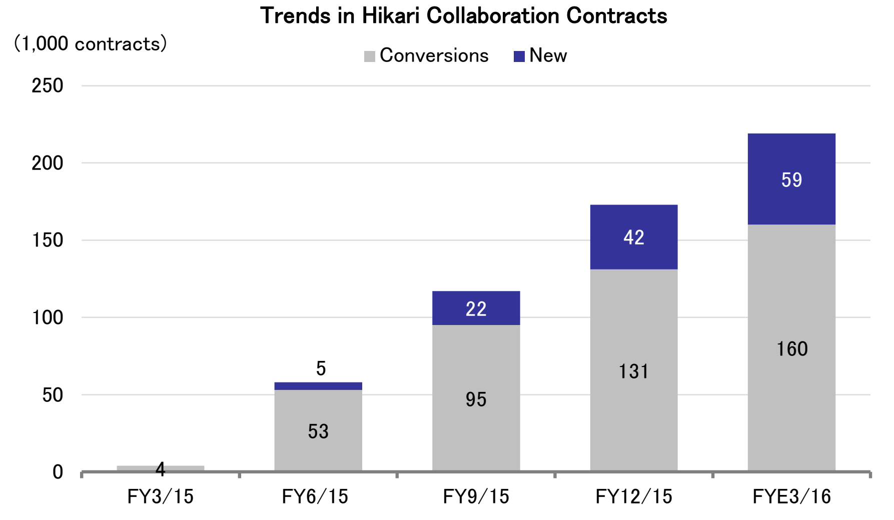
The Information and Communications Services business posted ¥44,200mn in sales (+10.3% y-o-y) and ¥2,300mn in operating profit (-¥2,600mn).

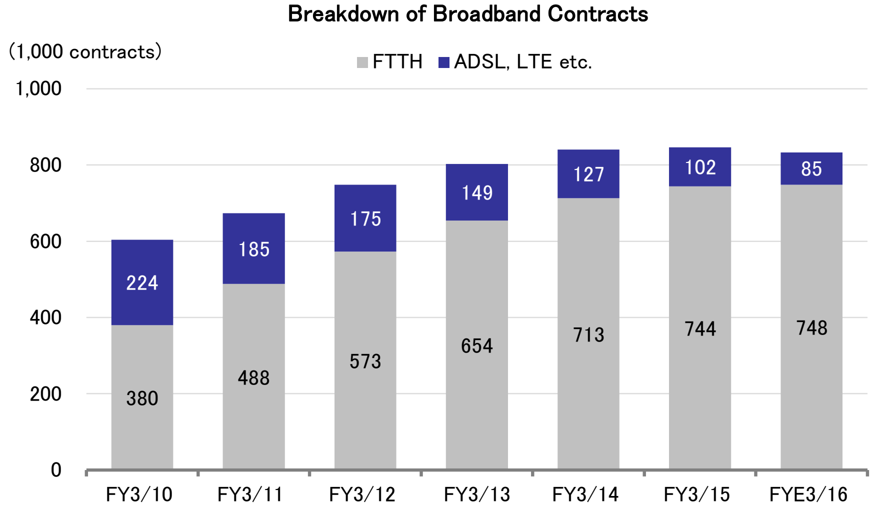
In the broadband business, the Company focused on conversions to @T.COM Hikari and TNC Hikari that utilize Hikari collaboration that started in FY3/15 and new customer recruitment. Customer volume amounted to 219,000 contracts based on 160,000 contracts for customers converting from existing services (27.8% conversion rate) and 59,000 contracts from acquiring new customers. We think the Company performed well in customer recruitment, despite missing the period-start target (260,000 conversions and 60,000 new acquisitions) amid tougher competition with new entrants, including major mobile carriers. While Hikari collaboration contributed to higher sales because it adds the optical communications line usage fee to the service fee, aggressive spending on sales promotion costs weakened profit by ¥2,800mn.

Total broadband customer volume fell for the first time with a decline of 13,000 contracts from the end of the previous fiscal year to 833,000 contracts, despite a rise of 4,000 contracts to 748,000 contracts for FTTH service, due to a drop of 17,000 contracts for ADSL and other services.

Corporate data communications service achieved double-digit sales and profit gains (y-o-y) thanks to robust demand against a backdrop of market expansion for cloud services. System development business, meanwhile, slightly eased.

Compared to period-start guidance, the Company had shortfalls of ¥3,000mn in sales and ¥400mn in operating profit mainly due to customer volume coming in below expectations by 101,000 contracts for Hikari collaboration.

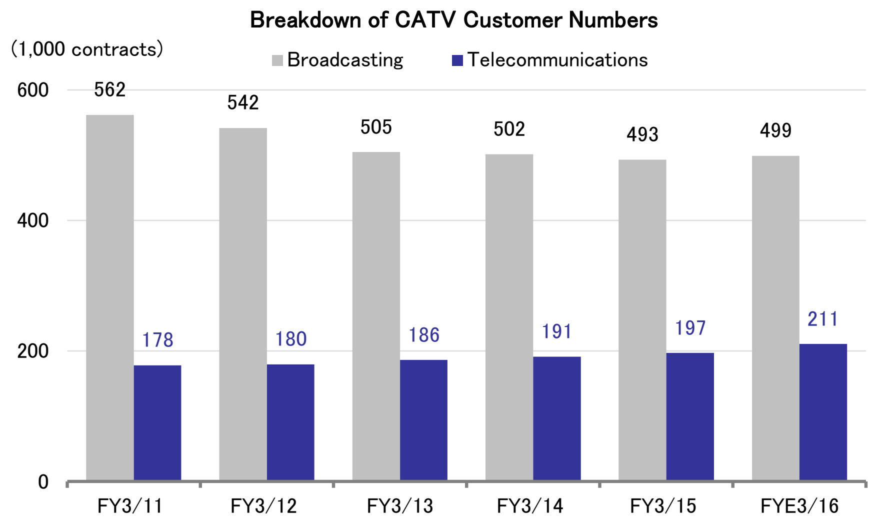




○CATV Business

The CATV business recorded ¥24,600mn in sales (+1.0% y-o-y) and ¥2,000mn in operating profit (+¥300mn). Customer volume increased by 20,000 contracts from the end of the previous fiscal year to 710,000 contracts thanks to bundling discounts for broadcast and communications services, the launch of bundling discounts with smartphones through collaboration with multiple mobile carriers, focus on bulk sales to multi-household dwellings, and use of churn prevention measures through an improved customer center. We think the first increase in five years for broadcast service with a gain of 6,000 contracts to 499,000 contracts deserves attention. Communications service also had a healthy increase of 14,000 contracts to 211,000 contracts. Profit moved upward, even with higher customer acquisition costs and costs related to bolstering the customer center, thanks to the sales-increase effect and lower depreciation costs.

Compared to period-start guidance, sales undershot by ¥200mn because of 2,000 fewer contracts than anticipated, but operating profit exceeded the target by ¥200mn.



Higher sales and small loss in the Aqua business, sales and profit gains for the Construction and Real Estate business

○Aqua business

The Aqua business booked ¥5,500mn in sales (+10.7% y-o-y) and a ¥1,100mn operating loss (vs. a ¥1,300mn loss in FY3/15). Customer contracts rose by 3,000 contracts from the end of the previous fiscal year to 133,000 contracts, owing to expansion of operating scope in Kansai, Hokuriku, and Tohoku areas during FY3/16, in addition to existing main markets in Shizuoka and Kanto areas, and this growth provided a lift to sales. While SG&A expenses climbed by ¥300mn y-o-y to ¥3,800mn, mainly because of marketing costs to acquire customers, the segment narrowed its operating loss by ¥200mn due to extra gross profit driven by higher sales. However, the addition pace to customer numbers was slower than anticipated in guidance, and this segment missed period-start targets by ¥300mn in sales and ¥100mn in operating profit.

○Real Estate and Construction business

The Construction and Real Estate business booked ¥21,000mn in sales (+4.8% y-o-y) and ¥1,300mn in operating profit (+¥200mn). Sales and profits improved thanks to gains in home sales, new store building projects, and building management support.

○Other Businesses and Adjustments

The Other businesses and adjustments segment incurred a 2.2% drop in sales to ¥4,900mn and a wider operating profit at ¥5,200mn (vs. ¥5,000mn a year earlier). Wedding ceremony sales declined because closure of one site in March 2015 shrunk operations to two sites. Nursing case business, however, posted higher sales owing to full-year contributions from four sites opening in FY3/15 (putting the total network at seven sites) and an increase in usage numbers. Shipbuilding business also reported stronger sales, despite a drop in the number of repaired vessels, because of an increase in repair work per vessel.

Results Outlook

Expecting steep sales and profit increases in FY3/17 and all-time high profits

(1) Forecasts for FY3/17

The Company's FY3/17 consolidated outlook calls for ¥187,100mn in sales (+3.4% y-o-y), ¥12,560mn in operating profit (+52.3%), ¥11,830mn in recurring profit (+45.1%), and ¥6,240mn in net profit attributable to owners of parent (+80.4%). The Company projects steep profit increases to all-time highs for all items. It also expects to achieve profit goals presented in the three-year medium-term plan that started in FY3/15 (Innovation Plan 2016 "Growing").

FY3/17 Consolidated Results Outlook

(unit: ¥mn)

	FY3/16		FY3/17		
	Results	Ratio to sales	Plan	Ratio to sales	YoY change
Net sales	180,940	-	187,100	-	3.4%
Operating profit	8,245	4.6%	12,560	6.7%	52.3%
Recurring profit	8,150	4.5%	11,830	6.3%	45.1%
Extraordinary profit	-1,714	-0.9%	-	-	-
Net profit attributable to owners of parent	3,458	1.9%	6,240	3.3%	80.4%

The Company factors in an increase of 47,000 contracts y-o-y from the end of FY3/16 to 2,604,000 contracts, primarily driven by the mainstay Gas and Petroleum business and CATV business. It projects a return to a sales increase for the first time in three years, despite the prospect of an ongoing decline in gas business sales due to continuation of sales price reductions, because of rising contract volumes in Hikari collaboration, CATV, and Aqua businesses. The Company also expects profit lifts of ¥3,400mn from improved income in Hikari collaboration and Aqua businesses and ¥800mn in lower goodwill amortization costs. The plan assumes flat profits besides these additions, and we see a reasonable chance of earnings upside if Hikari collaboration and Aqua businesses proceed on track with guidance. The larger projected rate of increase in net profit attributable to owners of parent, meanwhile, stems from a rebound after heavy recognition of fixed asset disposal losses, impairment losses, and other extraordinary losses in FY3/16 and a decline in the effective tax rate.

Sales by Business Segment

(unit: ¥bn)

	FY3/15	FY3/16		FY3/17	
	Results	Results	YoY change	Plan	YoY change
Gas and Petroleum	93.1	80.7	-13.2%	75.9	-6.0%
Information and Communications Services	40.1	44.2	10.3%	51.8	17.1%
CATV	24.4	24.6	1.0%	25.4	3.1%
Construction and Real Estate	20.0	21.0	4.8%	22.5	7.2%
Aqua	5.0	5.5	10.7%	5.8	6.4%
Other Businesses and Adjustments	5.0	4.9	-2.2%	5.7	16.9%
Total	187.5	180.9	-3.5%	187.1	3.4%

Operating Profit by Segment

(unit: ¥bn)

	FY3/15	FY3/16		FY3/17	
	Results	Results	YoY change	Initial plan	YoY change
Gas and Petroleum	7.7	9.0	+1.3	9.0	+0
Information and Communications Services	5.0	2.3	-2.6	4.2	+1.9
CATV	1.7	2.0	+0.3	2.4	+0.4
Construction and Real Estate	1.0	1.3	+0.2	1.5	+0.2
Aqua	-1.3	-1.1	+0.2	0	+1.1
Other Businesses and Adjustments	-5.0	-5.2	-0.2	-4.6	+0.6
Total	9.0	8.2	-0.8	12.6	+4.3

Note: the figures are prior to the allocation of indirect expenses

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Customer Numbers by Services

(unit; 1,000 contracts)

	End-FY3/15	End-FY3/16		End-FY3/17	
	Results	Results	Change from the previous year-end	Plan	Change from the previous year-end
Gas (LP gas, city gas)	626	634	+8	650	+16
Information and telecommunications (fixed line and Wi-Fi)	864	852	-12	857	+4
(Hikari collaboration)	4	219	+215	357	+138
Information and telecommunications (mobile)	235	236	+1	237	+1
CATV	690	710	+20	730	+20
Aqua	130	133	+3	138	+4
Security	18	18	-0	18	+0
Total	2,537	2,558	+20	2,604	+46

Information and Communications Services driving sales growth, aiming for higher sales in all businesses other than Gas and Petroleum

(2) Outlook by business segment

○**Gas and Petroleum**

The FY3/17 segment guidance calls for ¥75,900mn in sales (-6.0% y-o-y) and roughly flat operating profit. It assumes a faster pace of customer contract growth to an increase of 16,200 contracts by adding more new contracts through customer acquisition in existing operating areas and broadening operating areas. The Company entered Aichi prefecture and Miyagi prefecture and other parts of southern Tohoku in FY3/16 and plans to widen operations to Mie and Gifu prefectures in FY3/17.

The plan projects a decline in sales, even with expansion of customer volume, because of a lingering impact from fee reductions. Yet it envisions flat earnings due to an ongoing decline in procurement prices too. The outlook assumes a $370/ton contract price, and this works out to a roughly 8% decline on a yen-converted basis (at a ¥119/$ forex rate). We see substantial upside room for earnings in light of May values being below the plan view at a $325/ton contract price and ¥109/$ rate.

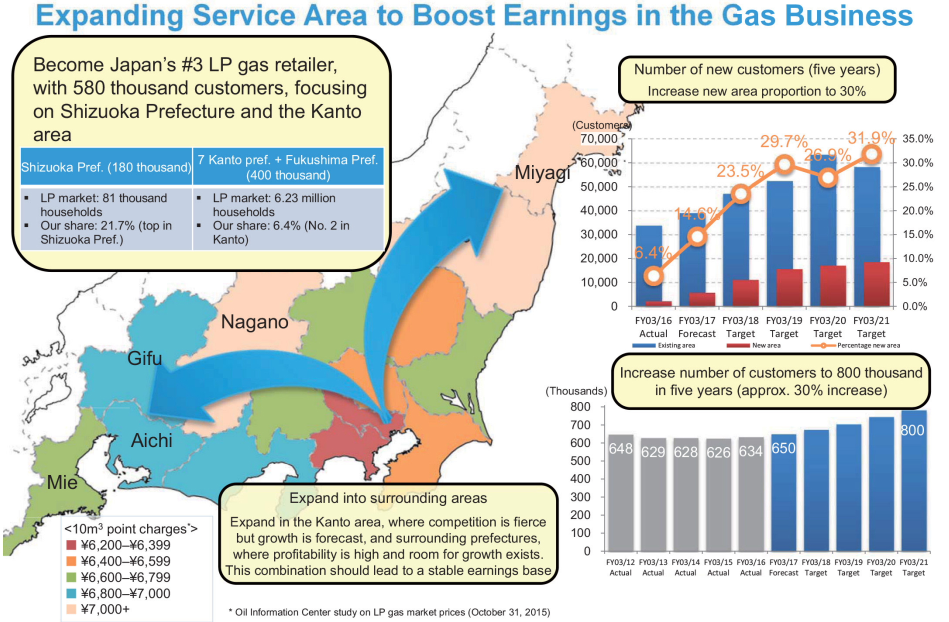
While higher marketing costs and personnel expenses related to bolstering sales activities in new areas are likely to add about ¥500mn to expenses, the Company should be capable of offsetting this impact with improved business efficiency and other curtailment of indirect costs.

The LP gas industry has many smaller operators, but we expect growing dominance by major operators. Our view takes into account likely weeding out of smaller operators from the standpoint of price competitiveness amid advances in sales liberalization for communications, electricity, and other living infrastructure services and related toughening of customer acquisition competition through bundled sales. The Company intends to enter Nagano and Toyama prefectures, where its group CATV firms operate, too from FY3/18 as part of this process.

The Company aims to raise the ratio of acquisitions in new operating areas to about 30% of total new customer acquisitions by FY3/21. It also plans to expand shares in existing areas and increase the total number of gas business customers to 800,000 contracts by FY3/21, including 70,000 from new areas.

While customer numbers had stalled in the gas business in recent years, we expect the Company to convert this segment into a growth business by lifting total customer volume.

Expanding the Area of the LP Gas Business



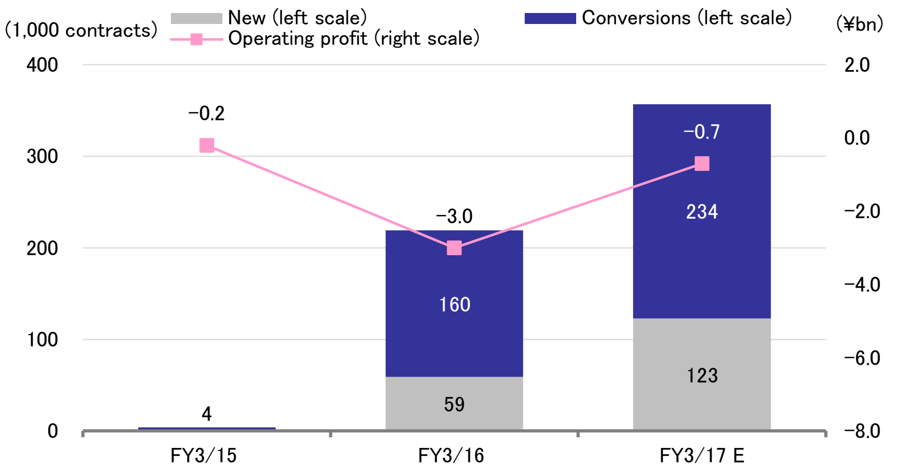
Source: Company briefing materials

○Information and Communications Services business

The FY3/17 segment guidance calls for ¥51,800mn in sales (+17.1% y-o-y) and ¥4,200mn in operating profit (+¥1,900mn). The bulk of the anticipated rise in sales comes from increasing Hikari collaboration customers, and this factor also adds ¥2,300mn to operating profit. The plan assumes gains in Hikari collaboration customers of 138,000 contracts from the end of FY3/16 to 357,000 contracts at the end of FY3/17, with conversions rising by 74,000 contracts to 234,000 contracts and new customers increasing by 64,000 contracts to 123,000 contracts. We think the Company is well within reach of the plan target considering the conservative outlook for a monthly average customer acquisition pace of 11,500 contracts, versus FY3/16's 17,900 contracts.

We expect profitability in Hikari collaboration service in FY3/18 with about ¥700mn if customer volume expands to 439,000 contracts. We forecast continuation of sales and profit increases in the 10% range in corporate data communications services based on likely continuation of a healthy market environment again in FY3/17.

Trends in Hikari Collaboration Contracts and Operating Profit



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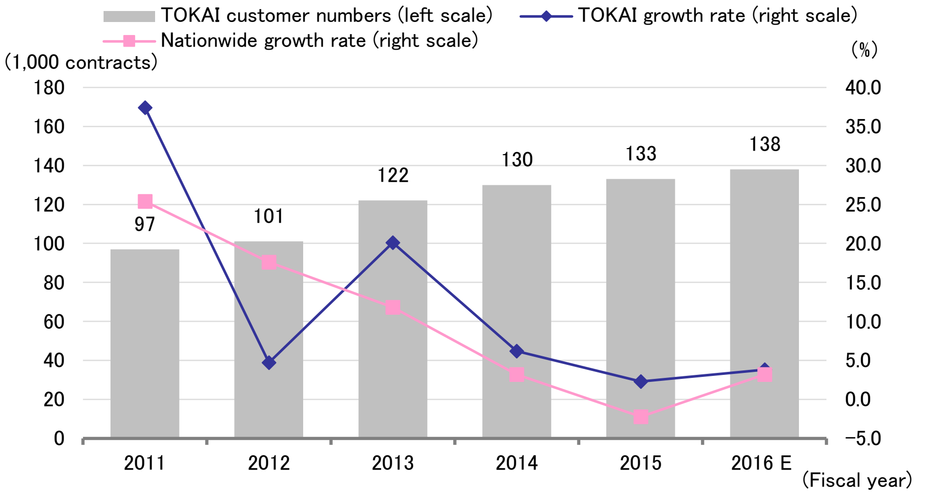
○**Aqua business**

The FY3/17 segment guidance projects a 6.4% y-o-y rise in sales and realization of a profit (vs. FY3/16's ¥1,100mn operating loss). The Company assumes an increase of 4,900 contracts in the customer base from the end of FY3/16. It plans to revise the sales strategy in order to reach a profit this fiscal year taking into account a slowdown in the customer expansion pace amid slower growth momentum in the water delivery market as a whole.

Specifically, it had been broadening operating areas to major regional cities in Kansai, Hokuriku, and Tohoku and aggressively holding customer acquisition fairs in order to recruit more customers through FY3/16, but its average customer acquisition cost increased and the cost recovery period lengthened. From FY3/17, however, it has revised the policy to implementing sales promotion activities focused on areas with high customer acquisition efficiency and is making revisions to the personnel structure. It also plans to reduce the number of sales promotion fairs by 25% from FY3/16's 8,800 times for the full year to 6,600 times in FY3/17.

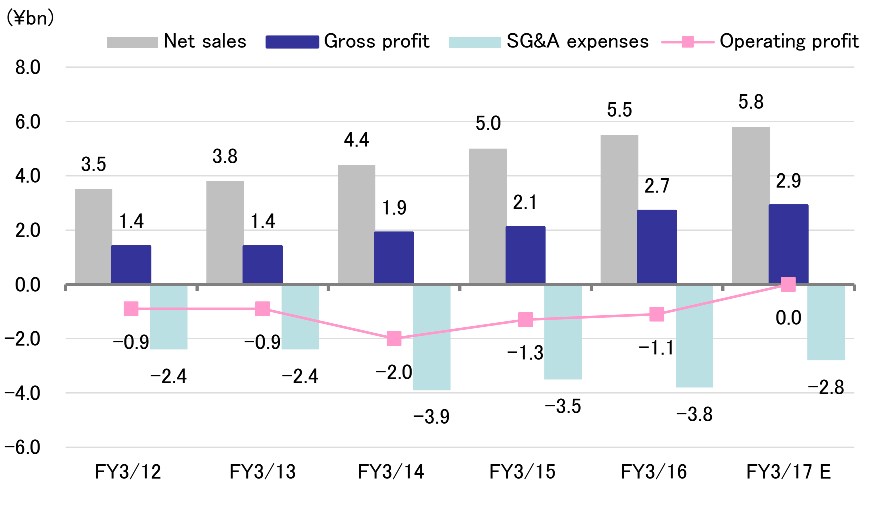
The main anticipated changes in operating profit are additions of ¥300mn from a rise in sales volume accompanying an increase in customer volume, ¥400mn from improved efficiency in customer acquisition fees, and ¥430mn from better efficiency in sales operations. We think a key point for reaching plan targets in FY3/17 is the extent to which the Company is capable of efficiently increasing customer volume.

Aqua Business Customer Numbers and Industry Growth Rate



Note: Nationwide growth rate prepared by the Japan Delivery Water & Server Association

Results Trends for the Aqua Business



○CATV business

The FY3/17 segment guidance projects sales and profit advances with a 3.1% y-o-y increase in sales to ¥25,400mn and a ¥400mn gain to ¥2,400mn in operating profit. This view assumes a rise in customer volume of 20,600 contracts from the end of FY3/16 to 730,000 contracts. The Company intends to continue striving to expand customer volume through bundling discounts and other sales promotion measures, bulk sales to multi-household dwellings, and churn prevention. It expects profit boosts from higher sales and an ongoing decline in depreciation costs from exhaustion of capital investments.

○Construction and Real Estate business

The FY3/17 segment guidance forecasts a 7.2% y-o-y rise in sales to ¥22,500mn and a ¥200mn increase in operating profit to ¥1,500mn. It factors in growing sales for equipment installation, home sales, and renovation businesses.

○Other Businesses and Adjustments

The FY3/17 segment guidance projects a 16.9% y-o-y increase in sales to ¥5,700mn and ¥600mn narrowing of the operating loss to ¥4,600mn. The Company expects a steep rise in sales for the nursing care business because of a higher utilization rate for its facilities and is aiming for the first-ever operating profit. Additionally, it forecasts higher FY3/17 sales and profits in the wedding ceremony business thanks to exhaustion of the negative impact from the site closure and a higher utilization rate for the existing sites.

Steady advances with the medium-term business plan, starting to formulate the next plan

(3) Likely to attain goals from the Innovation Plan 2016 "Growing" three-year medium-term plan and next-generation medium-term plan

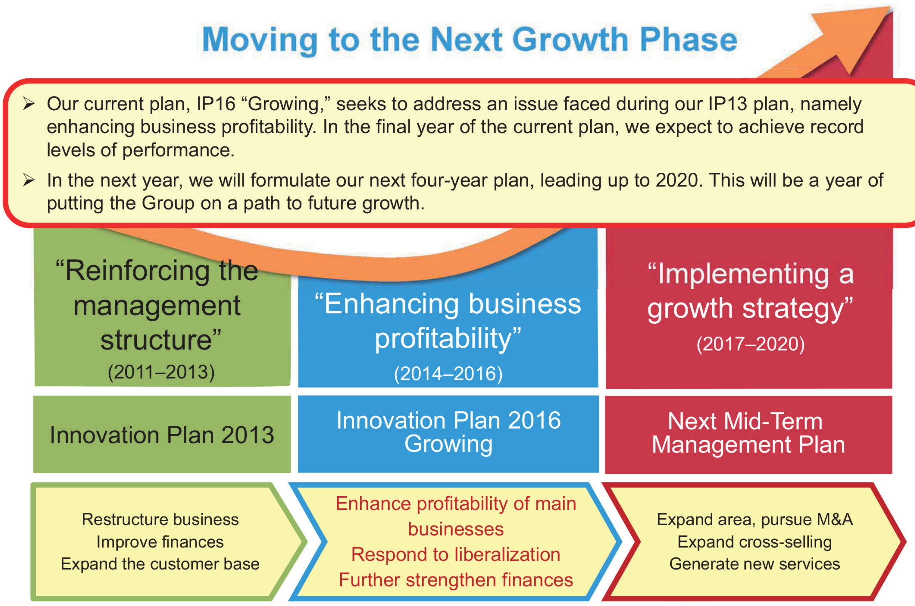
In June 2014, the Company announced its medium-term management plan, Innovation Plan 2016 "Growing" for the three years through FY3/17. This plan has three main objectives: continued sales growth and improved profitability by increasing the number of customers, continued improvements to the financial structure and stable management, and the delivery of steady and sustained returns to shareholders. TOKAI has steadily expanded earnings and improved financial standing under the plan. The plan's targets are 2.73mn group customer contracts, consolidated net sales of ¥209,500mn, operating profit of ¥12,600mn, interest-bearing debt of ¥64,700mn, and a 28.6% equity ratio. Based on earnings progress through FY3/16 and recent conditions, we expect slight shortfalls in customer numbers and net sales, but operating profit on track with the plan and a faster cutback pace in interest-bearing debt than anticipated. We think the equity ratio is also headed for the 30% range, surpassing the 28.6% target. We believe TOKAI is making smooth progress even though business conditions changed considerably from when it formulated the medium-term plan, including the decline in gas raw material prices and the start of Hikari collaboration service.

Medium-Term Business Plan's Business Goals and Attainment Prospects

	FY3/17 Initial plan	FY3/17 Current plan
Customer volume (10,000 contracts)	273	260
Net sales (¥bn)	209.5	187.1
Operating profit (¥bn)	12.6	12.6
EBITDA (¥bn)	28.7	28.3
Interest-bearing debt (¥bn)	64.7	62.2
Equity ratio	28.6%	30.8%

The Company aims to formulate the next medium-term business plan over the next year in light of this progress. We expect aggressive business initiatives in the next plan with a theme of "implementing growth strategies." Key points are "expansion of service areas and promoting M&A," "increased cross-selling," and "creation of new services."

Headed for the Next Growth Phase



Source: Company briefing materials

The "expansion of service areas and promoting M&A" covers broadening of service areas in the LP gas business mentioned above and review of area expansion opportunities utilizing M&A in the CATV business. The Company offers CATV service in five prefectures (Shizuoka, Chiba, Kanagawa, Nagano, and Okayama) currently. In this industry, Jupiter Telecommunications Co., Ltd., the top firm, holds a 50% market share, while most other CATV firms operate in specific regions. We think developments should be closely watched.

The "increased cross-selling" addresses an issue for the Company of needing to raise the contract rate for multiple services per customer. Only 7% of customers currently subscribe to multiple services out of the services provided by the TOKAI group. This means that the Company is not sufficiently capitalizing on its strength of supplying a wide range of living infrastructure services, such as gas, information and communications, CATV, and water delivery. TOKAI has been implementing measures to promote cross-selling, including discounted plans for multiple contracts and enhancement of the TLC Membership Service, but the results are not showing up in numbers yet. The Company thus created the TLC promotion organization in FY3/17 and intends to raise the cross-selling ratio with clear goals. It added electricity service to the menu from 2016, but contract volume is still very low. We will be closely monitoring these efforts because a higher cross-selling rate would raise profitability through prevention of customer churn and reduction of customer acquisition costs.

The "creation of new services" targets ramp-up of new businesses related to life events as a comprehensive living services company. The Company wants to cultivate services that offer strong affinity with existing businesses from among various living-related services that range from birth to education, medical care, insurance, and other areas as new businesses.

■ Financial Position and Shareholder Returns

Healthy progress improving financial standing through reduction of interest-bearing debt

(1) Financial position

Total assets at the end of March 2016 had decreased ¥5,400mn compared to the end of FY3/15 to ¥160,300mn. While current assets increased ¥2,200mn accompanying gains in cash and deposits and sales credits, non-current assets dropped ¥7,500mn. The decline consists of ¥3,900mn in tangible fixed assets, ¥1,800mn in assets related to retirement benefits, ¥1,700mn in goodwill, and ¥1,800mn in investment securities.

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TOKAI Holdings
3167 Tokyo Stock Exchange First Section

5-Jul.-16

Liabilities, meanwhile, decreased ¥3,900mn from the end of FY3/15 to ¥118,300mn. Interest-bearing debt fell ¥1,700mn, and lease debt declined ¥1,100mn. Net assets decreased ¥1,500mn from the end of FY3/15 to ¥42,000mn. Although the Company booked ¥3,500mn in net profit attributable to owners of parent, this amount was exceeded by ¥1,800mn to purchase treasury shares, ¥1,400mn for dividend payments, and ¥1,200mn declines each for the securities valuation difference and cumulative adjustment value related to retirement benefits.

In our review of TOKAI's business indicators, we think financial standing has steadily improved because of the decline in interest-bearing debt and profitability remains stable with operating margin holding in the 4% range. While ROE is currently in the upper single digits, we project an increase to the lower 10% range if FY3/17 earnings reach plan levels.

Consolidated Balance Sheet

(unit: ¥mn)

	End-FY3/13	End-FY3/14	End-FY3/15	End-FY3/16	Change
Current assets	40,351	40,606	35,959	38,117	2,157
(Cash and deposits)	4,235	3,182	2,861	4,077	1,216
Non-current assets	137,147	132,928	129,699	122,153	-7,546
(Goodwill)	12,632	10,241	8,270	6,589	-1,681
Total assets	177,642	173,620	165,702	160,303	-5,399
Total liabilities	143,631	135,291	122,234	118,332	-3,902
(Interest-bearing debt)	93,668	85,843	73,114	71,409	-1,705
Net assets	34,011	38,329	43,467	41,970	-1,496
Main performance indicators					
Equity ratio	18.6%	21.6%	25.7%	25.6%	
Interest-bearing debt ratio	283.0%	229.4%	171.9%	173.9%	
ROE (net profit ÷ capital)	10.4%	7.4%	9.9%	8.3%	
Operating margin	4.9%	3.9%	4.8%	4.6%	

Aggressive shareholder returns with consecutive dividend hikes, shareholder gifts, and share buybacks

(2) Shareholder return measures

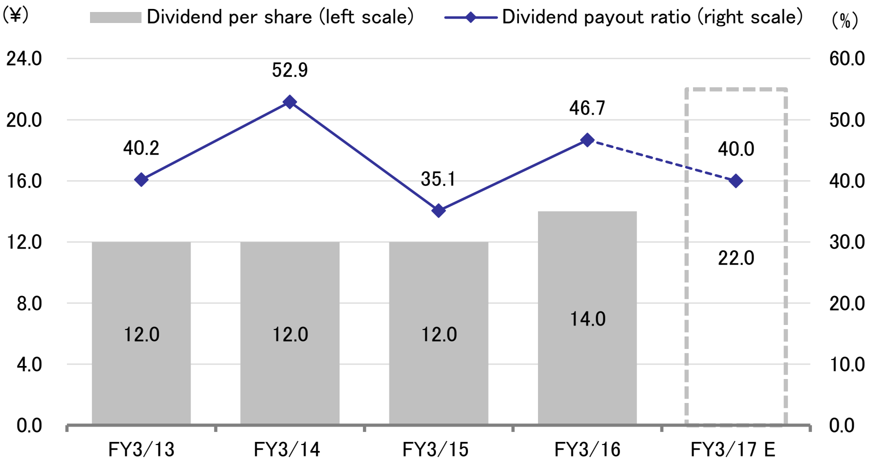
The Company pays dividends and has a shareholder gift program and also purchases treasury shares depending on conditions as shareholder return measures.

The Company sustains a stable dividend as its core policy and targets a 40% dividend payout ratio. It increased the dividend by ¥2 from the previous year to ¥14 in FY3/16 because earnings beat guidance, and this was the first dividend hike since becoming a holding company. It is planning a consecutive dividend hike in FY3/17 with an increase of ¥8 to ¥22 (40.0% dividend payout ratio) because of the prospect of a steep profit increase.

The Company also presents gifts to shareholders at the end of September and March. For each unit of shares (100 shares) held, shareholders can receive one of the following gifts: an Aqua product worth ¥1,900 (such as the Urunom "Fuji-no-Tennensui Sarari" (Mt. Fuji natural water), a QUO card worth ¥500, food coupons worth ¥1,000, or ¥1,000 worth of TLC Membership Service points. When including the gifts to shareholders in an estimate of the annual investment yield per unit from the current share price level (¥677 on May 30), it is in the range of 5% to 9% (depending on selection of a QUO card or an Aqua product as a gift).

The Company purchased 3.3mn treasury shares in FY3/16 and retired 15.52mn shares in November 2015. It also acquired 3.4mn shares that had been held by a subsidiary in March 2016. These steps reflect efforts to enhance shareholder value. We expect the Company to conduct further share buybacks from FY3/17 depending on conditions.

Dividend Per Share and Dividend Payout Ratio



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