

TOKAI Holdings Corporation

3167

Tokyo Stock Exchange First Section

1-Jul.-2020

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Index

Summary	01
1. FY3/20 results	01
2. Outlook for FY3/21	01
3. Key measures for FY3/21	02
4. Shareholder return policy	02
Business overview	03
1. Gas and petroleum business	04
2. Information and communications services business	05
3. CATV business	05
4. Building and real estate business	05
5. Aqua business	06
6. Other businesses	06
Result trends	06
1. In FY3/20, achieved record highs for the second consecutive fiscal period	06
2. Progress for the M&A strategy	08
3. Trends by business segment	10
4. Financial position	13
Outlook	14
1. Outlook for FY3/21 consolidated performance	14
2. Key measures	15
3. Net sales outlook by segment	18
Shareholder return policy	20
Information security measures	21

TOKAI Holdings Corporation
3167 Tokyo Stock Exchange First Section

1-Jul.-2020

<https://www.tokaiholdings.co.jp/english/ir/>

Summary

In FY3/21, is working to expand the customer base and aiming to achieve record-high results for the third consecutive period

Based in Shizuoka Prefecture, TOKAI Holdings <3167> (hereafter, also “the Company”) is a comprehensive lifestyle-infrastructure company that is developing “energy and lifestyle-related services,” primarily the provision of liquefied petroleum gas (LP gas), and “information and communications services.” In addition to realizing the Total Life Concierge (comprehensive services for living) concept*1, from FY3/19 it has started measures for a new theme, ABCIR+S*2, and it is aiming to take a further leap forward while advancing an M&A strategy.

*1 Total Life Concierge concept: a vision that aims to improve customer satisfaction by providing comprehensive and detailed support for customers’ comfortable lifestyles through the various services provided by the TOKAI Group.

*2 ABCIR+S: the TOKAI Group’s strategy for technological innovation. It is the acronym of AI (A), Big Data (B), Cloud (C), IoT (I), Robotics (R), and Smart Phone (S), and the Group will focus on creating and developing new services related to them.

1. FY3/20 results

In the FY3/20 consolidated results, net sales increased 2.3% year-on-year (YoY) to ¥195,952mn and operating profit rose 8.9% to ¥14,224mn, which were new record highs for the second consecutive period. The main factors behind the higher sales and profits were that the number of continuous-transaction customers in the Group steadily grew, including due to the effects of M&A, rising from 2,902,000 customers at the start of the period to 3,003,000 customers, and also from the progress made in accumulating monthly-billing revenue, the effects of reducing purchasing costs in the gas business, and that earnings were strong in the corporate information and communication services business and in the building and real estate business.

2. Outlook for FY3/21

The outlook for the FY3/21 consolidated results is for higher sales for the third consecutive fiscal period and record high profits for the fourth consecutive period, with net sales to increase 4.8% YoY to ¥205,300mn and operating profit to rise 5.5% to ¥15,000mn. In addition to finishing the medium-term management plan Innovation Plan 2020 “JUMP” (IP20) as the plan’s final fiscal year, the Company intends to focus on increasing the number of continuous-transaction customers to build the foundation for growth for the next period and onwards. It is aiming to grow customer numbers by 102,000 on the end of the previous fiscal period to 3,105,000 customers. In addition to the continuous increase in customers in the LP gas, CATV, and Aqua businesses, the forecast is for a slight increase in customer numbers in the consumer information and communication services business, in which customers have been decreasing in the last few years, through expanding the sales channels. For profits, it is anticipated that factors such as the effects of the higher sales and the reduction in purchasing costs in the gas business will cover for the increases in customer-acquisition costs and in depreciation and amortization costs due to the growth in capital investment. It seems that impact of COVID-19 will be minimal, as the Company’s mainstay business is lifestyle infrastructure services. But depending on how the situation develops in the future, it may affect some of its corporate services.

Summary

3. Key measures for FY3/21

The Company has three key measures for FY3/21; progressing M&A, implementing ABCIR+S, and deepening TLC. For M&A, it is continuing to progress investigations of investment projects with a total value of at least ¥100bn, which is leading to conclusions of contracts. For implementing ABCIR+S, it will make a fully-fledged start to marketing activities that utilize the D-sapiens DMP (Data Management Platform) that it has developed in-house. First, in the Aqua business, it will progress measures to use customer behavior to discover at an early stage signs of contract cancellations in order to prevent these cancellations, and then to use this measure in other services, and to improve sales efficiency and to strengthen marketing. For the deepening of TLC, toward maximizing customers' LTV (lifetime value), it intends to raise the contract rate for multiple services* from 18.8% at the end of the previous period to more than 20%. As the policy for this, it is looking into providing new services that will be useful for customers' lives. Specifically, it has started working on creating a services business in the field of health and preventative medicine, and we shall be paying attention to developments in the future.

| * Contract rate for multiple services = (total number of service contracts ÷ number of customers) - 1 |

4. Shareholder return policy

There has been no change to the policy of continuously and stably returning profits to shareholders. The forecast dividend per share for FY3/21 is ¥28.0 (dividend payout ratio, 43.3%), which is unchanged from the previous fiscal year. Going forward, the Company intends to pay dividends while observing profit trends and financing needs, with a benchmark dividend payout ratio of 40% to 50%. Also, at the end of March and the end of September, it presents one gift to shareholders from among several possible choices, such as an Aqua product, a QUO card, and points for a TLC member service worth ¥1,000. When including the gifts to shareholders in an estimate of the total investment yield per share unit from the current share price level (closing price of ¥985 on May 21, 2020), it is in the range of 3.9% to 7.0%*.

| * In the case of selecting either a QUO card or an Aqua product as the shareholder gift |

Key Points

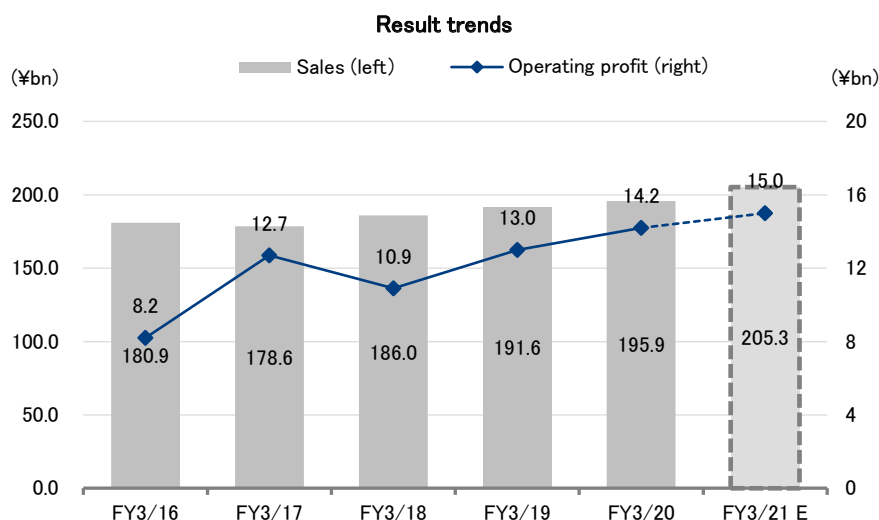
- With the number of continuous-transaction customers, which is the foundation of earnings, exceeding 3 million, the Company achieved record-high results for the second consecutive period in FY3/20
- Working on progressing M&A, implementing ABCIR+S, and deepening TLC as its key measures
- Strengthening measures toward increasing the number of customers in the mainstay businesses, and corporate information and communication services continue to perform well

TOKAI Holdings Corporation
3167 Tokyo Stock Exchange First Section

1-Jul.-2020

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Summary



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

Business overview

Provides various lifestyle-infrastructure services, including LP gas, Internet, and CATV services, toward realizing its management vision of the Total Life Concierge concept

Based in Shizuoka Prefecture, Japan, the Company is expanding its two main businesses, “energy and lifestyle-related services,” primarily the provision of liquefied petroleum (LP) gas, and “information and communications services,” and it is aiming to achieve its management vision of being a “Total Life Concierge” (TLC). It provides a complete range of services for everyday life under a one contract, one stop, and one call-center model and while deepening its connections with its customers, their local communities, society, and the global environment, it is striving to enrich people’s lives and to contribute to the development of local communities and to the conservation of the global environment, and also to a grow as a comprehensive provider of life services that represents Japan.

The Company currently discloses information on six business segments; the gas and petroleum business, the information and communications services business, the CATV business, the building and real estate business, the Aqua business, and other businesses. Looking at the sales structure by segment for FY3/20 results, the Company’s original business, the gas and petroleum business accounted for 39.9% of sales, the information and communications services business for 26.4%, and the CATV business for 16.0%. These three mainstay businesses accounted for over 80% of sales. The details by business segment are as follows.

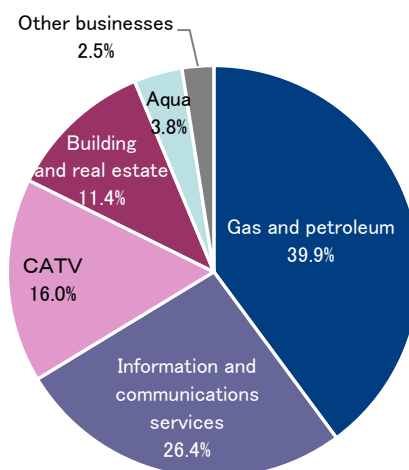
TOKAI Holdings Corporation
3167 Tokyo Stock Exchange First Section

1-Jul.-2020

<https://www.tokaiholdings.co.jp/english/ir/>

Business overview

Sales composition by business segment (FY3/20)



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

1. Gas and petroleum business

In this business, 83% of net sales are provided by the LP gas business and 17% by the city gas business. The mainstay LP gas business is developed by TOKAI Corporation, primarily for homes and businesses. The service areas are mainly in the Shizuoka and Kanto regions, but since 2015 it has also gradually expanded into other areas including the south Tohoku, Chubu/Tokai, Chugoku, and Kyushu areas. As of the end of March 2020, it had 652,000 contracts, and in direct sales, it ranked third after Iwatani Corporation <8088> and Nippon Gas <8174>. In terms of market share, it is the leader in Shizuoka, its home territory, with around 20%, while it has a share of just under 10% in the highly competitive Kanto region, putting it in second place. As there are approximately 20 million households nationwide that use LP gas, its nationwide market share is still at the level of around 3%, and going forward there remains room for it to grow its share, including by expanding sales areas and conducting M&A. There are many LP gas companies in Japan, approximately 17,000 companies, including medium, small, and micro companies. Going forward, consolidation will likely progress through major capital players in this industry.

In the city gas business, TOKAI GAS CORPORATION supplies city gas in Yaizu City, Fujieda City, and Shimada City in Shizuoka Prefecture. In addition, it acquired the city gas businesses operated by the respective local governments of Shimonita Town, Gunma Prefecture, in April 2019, and of Nikaho City, Akita Prefecture, in April 2020, and it has started supplying city gas in these areas. The number of contracts was 61,000 at the end of March 2020 including the 5,000 contracts from Nikaho City. There are approximately 198 operators (general gas pipeline operator) nationwide in the city gas market, but with the exception of the four largest companies, most are (privately- and publicly-operated) small- to medium-sized operators with limited service areas. Following the liberalization of the retail city gas market in April 2017, the Company has been implementing a strategy of increasing customer numbers by bringing operators in various regions into the Group through M&A.

2. Information and communications services business

The information and communications services business, which is conducted by TOKAI Communications Corporation, is comprised of the consumer ISP (Internet service provider) business and mobile business (sales of mobile phones), and a business to provide communication lines, data center services, cloud system development and consigned systems development for corporations. Looking at the percentages of total net sales for FY3/20 results, the consumer business contributed 55% and the corporate business 45%.

The ISP business provides the “@ T COM” service for the nationwide service area and the TOKAI Network Club (TNC) service for the Shizuoka Prefecture service area, and it has the leading share within Shizuoka Prefecture of approximately 19%. In addition, from February 2015 it launched the Hikari Collaboration service (@TCOM Hikari and TNC Hikari services), in which it receives wholesale provision of optical lines from NTT <9432> and provides its own optical (hikari) Internet connection service. As of the end of March 2020, the Company had 389,000 customers using its existing ISP service and 324,000 customers using its Hikari Collaboration service and customers are shifting toward Hikari Collaboration in the past few years. The two services have a total of 713,000 customers. This number has steadily declined from 864,000 as of the end of March 2015, immediately after the Hikari Collaboration service was launched. This decline has occurred because customers have been leaving the service at a faster pace than new customers can be enrolled, as major mobile phone carriers conduct sales of service bundles at discounted prices, including mobile phone fees, making use of NTT’s wholesale optical line business.

The mobile business operates 12 mobile phone stores, mainly within Shizuoka Prefecture, as a sales agency of Softbank Corp <9434>, and as of the end of March 2020, it had 212,000 customers. Also, in February 2017 the Company began sales of LIBMO, which is a low-cost mobile service, as an MVNO business*. The number of LIBMO customers had steadily increased to 48,000 at the end of March 2020. It also operates four iCracked Store stores, which provides iPhone repair services.

* MVNO (Mobile Virtual Network Operator): Operators who provide services by borrowing other companies’ wireless communication infrastructure, such as for mobile phones.

3.CATV business

In the CATV business, the Company has gradually expanded the service area through its M&A strategy. It provides services in Tokyo and six prefectures: Shizuoka, Kanagawa, Chiba, Nagano, Okayama and Miyagi. Currently, the CATV business is undertaken by ten Group companies. As of the end of March 2020, the number of customers stood at 862,000 for broadcasting services and 292,000 for communications services, bringing the total to 1,154,000 customers. In the CATV industry, the J:COM (Jupiter Telecommunications Co., Ltd.) Group holds a market share of just over 50% based on the number of subscribing households. The second-largest CATV company and smaller players have market shares in the single digits and are locked in a tight race for market share. The Company has around 3% of shares, and its strategy is to continue increasing its market share through proactive M&As going forward.

4. Building and real estate business

In this business, TOKAI Corporation engages in the construction and design of detached housing, multi-dwelling housing, stores, and office buildings. It also provides a building management service, sells home facilities and equipment, provides a security service (classified in the gas and petroleum business), operates insurance agencies (classified in other businesses), and develops and trades real estate. In addition, TOKAI Corporation and Tokai Gas Corporation are developing a renovation business. The Company has also made a consolidated subsidiary of Nissan Tri Star Construction Inc., a comprehensive construction company based in Gifu Prefecture, in September 2019.

5. Aqua business

In the Aqua business (bottled water home delivery business), TOKAI launched the Delicious Water Home Delivery returnable (using returnable bottles) service in 2007 in Shizuoka Prefecture, and since 2011, it has been providing its water product Ulunom as a one-way (using disposable bottles) service in areas other than Shizuoka Prefecture. It has two bottle manufacturing plants within Shizuoka Prefecture for Mt. Fuji natural water (production capacity of approximately 180,000 bottles), and at the end of March 2020, it had 161,000 customers. At the end of 2019, the number of customers in the industry as a whole was 4.14 million, so the Company's share is around the 4% level (approximately 50% share in Shizuoka Prefecture).

6. Other businesses

Other businesses include a nursing care business operated by TOKAI LIFE PLUS CORPORATION, a wedding ceremony business by TOKAI City Service Corporation, and a shipbuilding and repairs business by Tokaizosen-unyū Corporation. The Company launched the nursing care business in 2011, and as of March 2020, it operated six day-service facilities, a short-stay facility, and a paid-for nursing home in Shizuoka Prefecture. In addition, it has opened two care plan centers. For its wedding ceremony business, it operates one facility in Shizuoka Prefecture.

Result trends

With the number of continuous-transaction customers, which is the foundation of earnings, exceeding 3 million, the Company achieved record-high results for the second consecutive period in FY3/20

1. In FY3/20, achieved record highs for the second consecutive fiscal period

In the FY3/20 consolidated results, net sales increased 2.3% YoY to ¥195,952mn, operating profit increased 8.9% to ¥14,224mn, recurring profit rose 9.2% to ¥14,479mn, and net income attributable to owners of the parent climbed 6.0% to ¥8,241mn. Net sales increased for the third consecutive fiscal period, while each profit item also increased for the second consecutive fiscal period achieving record highs in both sales and profits. In comparison to the initial Company forecasts also, net sales and every profit item were basically as forecast.

FY3/20 consolidated results

	FY3/19		Forecast	FY3/20			
	Results	% of sales		Results	% of sales	YoY change	Vs. plan
Net sales	191,600	-	200,800	195,952	-	2.3%	-2.4%
Cost of sales	115,441	60.3%	-	116,662	59.5%	1.1%	-
SG&A expenses	63,101	32.9%	-	65,065	33.2%	3.1%	-
Operating profit	13,057	6.8%	14,170	14,224	7.3%	8.9%	0.4%
Recurring profit	13,259	6.9%	14,040	14,479	7.4%	9.2%	3.1%
Net income attributable to owners of the parent	7,772	4.1%	8,230	8,241	4.2%	6.0%	0.1%

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

TOKAI Holdings Corporation | 1-Jul.-2020
3167 Tokyo Stock Exchange First Section | <https://www.tokaiholdings.co.jp/english/ir/>

Result trends

Net sales increased mainly due to the rise in monthly-billing income alongside the increase in the number of continuous-transaction customers, and also as the corporate information and communication services business continued to perform strongly and from the effects of the M&A in the building and real estate business. The number of continuous-transaction customers steadily increased, up by 101,000 on the end of the previous fiscal period to 3,003,000 customers. Of this number, 65,000 customers were added due to the M&A (60,000 in the CATV business and 5,000 in the city gas business). Looking by business, customer numbers increased in the mainstay gas business and in the CATV and Aqua businesses, which covered for the decrease in consumer information and communication services.

Customer numbers by key services

	FY3/17	FY3/18	FY3/19	FY3/20	YoY change
(thousand)					
Gas	642	661	684	713	29
LP gas	588	606	628	652	24
City gas	54	55	56	61	5
Information and communication services	1,061	1,044	1,004	973	-31
Existing ISP and related services	527	465	419	389	-30
Hikari Collaboration	299	323	327	324	-3
LIBMO	2	29	41	48	7
Mobile	233	227	217	212	-5
CATV	733	1,032	1,063	1,154	91
Broadcasting services	508	775	789	862	73
Communication services	225	257	274	292	18
Aqua	135	146	156	161	5
Security	17	17	17	16	-1
Total	2,564	2,876	2,902	3,003	101
(Number of TLC members)	586	699	805	896	91
(Percentage of TLC members)	22.9%	24.3%	27.7%	29.8%	2.1pt

Note: The number of customers below a thousand is rounded to the nearest thousand. Information and communication services and CATV both offer communication services, so total figures avoid duplication.
Source: Prepared by FISCO from the Company's results briefing materials

Looking at the factors causing operating profit to increase and decrease, the increase factors were ¥2.4bn from the rise in the number of customers, ¥200mn from the MVNO business, ¥200mn from the decline in customer acquisition and maintenance costs, and ¥500mn from the reduction in purchasing costs in the gas business. These absorbed the decrease factors, including ¥600mn from the decline in profits in the communication broadband business (the Hikari Collaboration and existing ISP and related services), ¥1.1bn from the increase in system-strengthening costs, and ¥400mn from other factors, and therefore profits increased. As a provision for a litigation loss of ¥1,161mn* was recorded as an extraordinary loss, the increase rate of net income attributable to owners of the parent was slightly less than the increase rate of recurring profit.

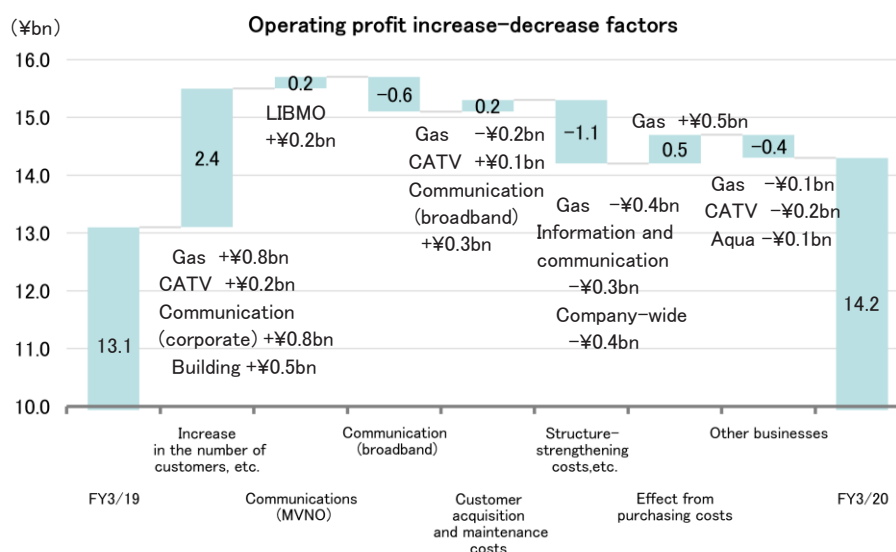
* With consolidated subsidiary TOKAI Communications as the plaintiff (and the counterclaim defendant), and Hitachi Solutions, Ltd., as the defendant (and the counterclaim plaintiff), these companies have initiated a claim for damages and a counterclaim for damages against each other. TOKAI Communications won the case in the district court, but the ruling was reversed at the Tokyo High Court on January 16, 2020, and it lost the case. Therefore, a provision was recorded in preparation for when the ruling is determined. The Company has appealed the ruling to the Supreme Court.

TOKAI Holdings Corporation
3167 Tokyo Stock Exchange First Section

1-Jul.-2020

<https://www.tokaiholdings.co.jp/english/ir/>

Result trends



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

In FY3/20, completed five M&A and entered-into two alliances

2. Progress for the M&A strategy

In the medium-term management plan (IP20), which it started in FY3/18, the Company is working on “progressing M&A” as one of its basic strategies. In FY3/20, it completed 5 M&A and entered-into 2 alliances. The specific achievements are as follows.

(1) City gas business

In March 2019, the Company acquired the first refusal rights to acquire the gas business (5,000 customers) operated by Nikaho City, Akita Prefecture. It concluded the contract for it in May of the same year and took-over the business from April 2020. This was its second M&A in the city gas business and the first time that the Group has entered-into Akita Prefecture. Going forward, the aim is to provide not only city gas, but also a variety of lifestyle-related services in accordance with its TLC vision, and to expand the scope of the city gas business while contributing to enriching the lives of its customers.

As a model case of a new alliance with a community-based company, in April 2019 in Isesaki City, Gunma Prefecture, the Company acquired the shares of Isesaki Gas Co., Ltd., which conducts a city gas business, and made it an equity method affiliate, and the two companies then concluded a capital and business alliance agreement in August of the same year. In Gunma Prefecture, the Company is already conducting an LP gas business in Maebashi City and Ota City, while it started a city gas business in Shimonita Town in April of the same year. Isesaki Gas conducts an LP gas business through a subsidiary, and going forward, the Company intends to promote the mutual usage of services and to pursue the benefits of alliances with community-based companies by mutually sharing management resources and expertise. Specifically, it is anticipated that costs will be reduced through sharing their LP gas distribution networks, and that the Company will provide its lifestyle-related services to the approximately 11,000 Isesaki Gas customers.

TOKAI Holdings Corporation
3167 Tokyo Stock Exchange First Section

1-Jul.-2020

<https://www.tokaiholdings.co.jp/english/ir/>

Result trends

Moreover, in October 2019, the Company established T&T Energy Co., Ltd., jointly with TEPCO Energy Partner, Inc. (investment ratio, 50.0%) as a joint venture. Leveraging TEPCO Energy Partner's strength of "expertise in the city gas retail business, starting with its ability to procure gas" and the Company's strength of "a sales network in the Tokai area," the joint venture is conducting a city gas business in the Tokai area (Aichi, Gifu, and Mie). In the Tokai area, TOHO GAS Co., Ltd. <9533> provides city gas to 2.32 million household customers and the Company is aiming to gradually acquire customers in this market. Also, in the future, the Company plans to investigate providing various lifestyle-related services, including electricity, and expanding the sales area outside of the three prefectures.

(2) CATV business

In October 2019, the Company acquired the CATV business (3,000 customers) of Shioya Limited, whose service-provision area is one part of eastern Shizuoka Prefecture. It has started transmitting regional community channels, which are one of the features of the Company, and providing high speed communication services through FTTH and 4K/8K broadcasting, while it has also started providing various lifestyle-related services through the TLC concept.

Also, at the end of March 2020, the Company acquired 87.9% of the shares of Sendai CATV Co., Ltd., which provides services to 57,000 customers in Sendai City and Natori City in Miyagi Prefecture, and it made it a consolidated subsidiary. With Sendai City, which is a government-ordinance designated city, as the base, in the future the policy is to expand the business foundation in the Tohoku area by not only increasing the sophistication of services through investing in converting to fiber optics for CATV, but also by providing lifestyle-related services, including Internet, LP gas, and home water delivery services.

(3) Building and real estate business

In September 2019, the Company made a consolidated subsidiary of Nissan Tri Star Construction Inc., a comprehensive construction company in Gifu Prefecture. Nissan Tri Star Construction has an extensive track record, mainly in civil engineering, as a company with more than 50 years of history since its foundation. In the future, the Company intends to utilize Nissan Tri Star Construction's technologies and expertise to expand its business domain as a comprehensive construction business to Shizuoka Prefecture and the Kanto region, in addition to the three Tokai prefectures. However, securing and training human resources is an issue, and it seems that for the time frame, this business will be developed with a view to the medium- to long-term.

(4) Information and communication services business

In July 2019, the Company made a consolidated subsidiary of AM's Brain Inc., which has its head office in Okayama Prefecture and whose businesses include outsourced software development and systems operations and maintenance. The objective of making it a subsidiary is to strengthen the development structure in the western Japan area in order to respond to the strong demand for systems development. The Company has a data center in Okayama Prefecture, so synergies are expected in the future.

Result trends

Results were driven by higher earnings in the LP gas business and the corporate information and communication services business

3. Trends by business segment

Net sales by segment

	FY3/17	FY3/18	FY3/19	FY3/20	YoY
(¥mn)					
Gas and petroleum	73,344	76,073	77,977	78,154	0.2%
Information and communication services	49,508	50,894	51,234	51,753	1.0%
CATV	25,396	28,386	30,511	31,385	2.9%
Building and real estate	19,511	19,807	20,090	22,383	11.4%
Aqua	5,762	6,200	7,004	7,416	5.9%
Other businesses	5,108	4,706	4,781	4,858	1.6%
Total	178,631	186,069	191,600	195,952	2.3%

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

Operating profit by segment

	FY3/17	FY3/18	FY3/19	FY3/20	YoY
(¥mn)					
Gas and petroleum	9,161	7,364	6,815	7,452	9.3%
Information and communication services	4,213	3,174	3,827	4,226	10.4%
CATV	2,752	3,554	4,953	5,024	1.4%
Building and real estate	1,098	1,330	1,615	2,116	31.0%
Aqua	298	246	762	674	-11.5%
Other businesses and adjustments	-4,775	-4,699	-4,916	-5,271	-
Total	12,750	10,971	13,057	14,224	8.9%

*Values are prior to allocating indirect costs and other expenses

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

(1) Gas and petroleum business

In the gas and petroleum business, net sales increased 0.2% YoY to ¥78,154mn, and operating profit before the allocation of indirect costs and other costs (the calculation method is different to that in the financial results; same below in this section) increased 9.3% to ¥7,452mn. Net sales increased for the third consecutive period, and operating profit increased for the first time in four periods. In the last few years, profits have continued to decline, including due to the rise in purchasing costs and the reduction in the volume of gas consumed per household due to the warmer temperatures. But profits increased in this period, mainly because the average temperature was the same as in the previous year and as the volume of gas sold to households increased alongside the rise in the number of customers, and also as progress was made in reducing purchasing costs.

Within the above results, in the LP gas business, net sales decreased slightly YoY, down 0.5% to ¥65,235mn. Progress was made in acquiring customers in both existing areas and new areas, and the number of customers increased by 23,000 on the end of the previous fiscal period (up 7,000 in existing areas and up 15,000 in new areas) to 652,000 customers. In addition, the sales volume increased 4% YoY and the average sales unit price rose slightly. However, profits were reduced by the fall in industrial and wholesale sales prices, linked to the fall in purchasing prices. But the part that sales prices fell was absorbed by the reduction in purchasing costs, so this had no impact on profits. The number of contracts was below the Company's forecast (684,000 contracts) due to delays in acquisitions in commercial areas, but it is making steady progressing in acquiring customers in new areas, including Tsu City, Mie Prefecture, which the Company newly entered in April 2019.

TOKAI Holdings Corporation
3167 Tokyo Stock Exchange First Section

1-Jul.-2020

<https://www.tokaiholdings.co.jp/english/ir/>

Result trends

In the city gas business, net sales increased 4.1% YoY to ¥12,919mn. Sales unit prices decreased due to the system to adjust raw-materials costs, but net sales still increased, mainly because in April, the Company newly started operating a business in Shimonita Town, Gunma Prefecture (approximately 1,000 customers), which was a sales-increase factor of around 2%, and also due to an increase in equipment sales. In Shimonita Town, it has started providing the Company Group's various services and has acquired approximately 100 contracts as the total for electricity, home water delivery, LIBMO, ISP, and other services. It seems that the Company expects sales per customer to increase by a maximum of 2.5 times through proposing to them multiple Group products. The number of customers at the end of the period was 61,000 customers, including from the addition of the previously mentioned 5,000 customers in Nikaho City, Akita Prefecture.

Looking at the factors causing operating profit to increase and decrease, the increase factors were ¥800mn from the rise in the number of customers and ¥500mn from the reduction in purchasing costs, which absorbed the decrease factors, of ¥200mn from the rise in customer acquisition and maintenance costs and ¥400mn from the increase in system-strengthening costs.

(2) Information and communication services business

In the information and communications services business, net sales increased 1.0% YoY to ¥51,753mn and operating profit rose 10.4% to ¥4,226mn. Net sales increased for the tenth consecutive period, while operating profit rose for the second consecutive period. A situation is continuing in which the strong performance of the corporate business is covering for the decreases in the consumer business.

In the consumer business, net sales decreased 7.2% YoY to ¥28,606mn. This was mainly because, due to the intensification of competition with the major mobile carriers, the number of customers for ISP services decreased by 34,000 on the end of the previous fiscal period to 713,000 customers (customer numbers have continued to trend downward since peaking at 864,000 customers in FY3/15). Breaking this down, the number of customers for existing ISP and related services was down 30,000 on the end of the previous fiscal period to 389,000 customers and for Hikari Collaboration was also down 3,000 to 324,000 customers, which was the first decrease since this service was started. In addition to the intensification of competition, this was because customer-acquisition costs were kept down. However, the number has been maintained within a range of 324,000 customers since the 2Q. Other than these businesses, in the mobile (mobile phone sales agencies) business, customer numbers decreased by 5,000 to 212,000 customers, while for the low-cost mobile service LIBMO, they increased 7,000 to 48,000 customers.

In the consumer business, operating profit decreased by around 20% YoY or by approximately ¥500mn in monetary terms. Looking at the increase and decrease factors, the increase factors were ¥200mn from the higher profits in LIBMO and ¥300mn from the reduction in customer acquisition and maintenance costs, but these increases were exceeded by the decrease factors, of ¥600mn from the fall in the number of customers for ISP and related services and ¥300mn for the increase in systems-strengthening costs and other costs, and therefore profits declined. The systems-strengthening costs included the costs of relocating the mobile shops (relocation of three shops from roadside locations to within large shopping centers). The aim of these relocations is to improve the profitability of the stores through providing various services including LIBMO and the Hikari Collaboration services, as well as offering iPhone repair services as joint facilities with the iCracked Store in addition to smartphone sales.

Result trends

Conversely, the corporate business performed strongly, with net sales increasing 13.3% YoY to ¥23,147mn. This was mainly because companies are working on digital transformation and in this situation, an increasing number of them are introducing Cloud services, so systems builds for the Amazon Web Service and Cloud connection line contracts maintained their high double-digit growth. The excellent sales were also because of the continued strong orders for outsourced systems development. It seems that profits increased by approximately 40% YoY or around ¥1bn in monetary terms, due to the effects of the higher sales.

(3) CATV business

In the CATV business, net sales increased 2.9% YoY to ¥31,385mn and operating profit rose 1.4% to ¥5,024mn. Net sales increased for the seventh consecutive period and operating profit rose for the fifth consecutive period, and the results were new record highs. In addition to discount services for subscribing to a broadcast and communication set and a discounted smartphone set through a collaboration with a major mobile carrier, the Company is acquiring new customers through various measures, including strengthening the creation of programs on community channels based in local communities, while it also worked to prevent contract cancellations. As a result of these efforts, sales and profits increased.

The number of customers at the end of the period had steadily increased, up 73,000 on the end of the previous fiscal period to 862,000 customers for broadcasting services, and up 18,000 to 292,000 customers for communication services. Within these increases, 60,000 customers were from the effects of the M&A, with 3,000 customers added from the acquisition of Shioya's business in October 2019 and 57,000 customers added from Sendai CATV being made a subsidiary at the end of March 2020. Sendai CATV's results were not included in the FY3/20 results and it will contribute from FY3/21. In its FY3/19 results, it recorded net sales of ¥1,037mn and operating profit of ¥66mn.

Looking at the factors causing operating profit to increase and decrease, the increase factors were ¥200mn from the rise in the number of customers and ¥100mn from the reduction in customer acquisition and maintenance costs, which absorbed the decrease factor, of ¥200mn from an increase in other costs.

(4) Building and real estate business

In the building and real estate business, net sales increased 11.4% YoY to ¥22,383mn and operating profit rose 31.0% to ¥2,116mn. So sales and profits increased by double digits, for higher sales and profits for the fourth consecutive period and also new record high results. The addition of the results of Nissan Tri Star Construction, which was made a subsidiary in September 2019, was a factor adding approximately ¥1.6bn to net sales and around ¥200mn to operating profit. But the higher sales and profits was also due to the performance of the existing business, including increases in equipment sales and in orders for renovations and other services.

(5) Aqua business

In the Aqua business, net sales increased 5.9% YoY to ¥7,416mn and operating profit decreased 11.5% to ¥674mn. Profits increased significantly because the Company worked actively to acquire customers at large-scale commercial facilities, etc., and the number of customers was up 5,000 from the end of the previous fiscal year to 161,000 customers. So although sales continued to increase, profits decreased.

TOKAI Holdings Corporation
3167 Tokyo Stock Exchange First Section

1-Jul.-2020

<https://www.tokaiholdings.co.jp/english/ir/>

Result trends

(6) Other business and adjustments

In other businesses, net sales increased 1.6% YoY to ¥4,858mn. Breaking this down, in the nursing care business, sales continued to trend upward, rising 15.6% to ¥1,243mn, due to the increase in the number of facility users. But in the shipbuilding and repairs business, they decreased 2.6% to ¥1,480mn because of the fall in the volume of ship repair work, while in the wedding ceremony business, they declined 8.0% to ¥1,359mn, mainly because special events and banquets were cancelled and wedding ceremonies were postponed due to concerns about the COVID-19 outbreak. The segment's operating loss, including internal adjustments, increased slightly YoY to ¥5,271mn (compared to a loss of ¥4,916mn in the same period in the previous fiscal year), mainly because of an increase in Company-wide shared costs.

Targeting an equity ratio on the 30% level, intends to continue to actively invest, including in M&A

4. Financial position

Looking at the financial condition at the end of FY3/20, total assets were up ¥2,366mn on the end of the previous fiscal year to ¥169,972mn. This was mainly because although investment securities under investments and other assets decreased ¥1,647mn, mainly due to the decline in the valuation difference on investment securities, there were increases in accounts receivable-trade of ¥1,060mn due to the acquisition of new consolidated subsidiaries, property, plant, and equipment of ¥1,322mn, deferred tax assets of ¥1,700mn, and cash and deposits of ¥465mn.

Total liabilities were up ¥278mn on the end of the previous fiscal period to ¥103,989mn, as while interest-bearing debt decreased ¥2,331mn, within current liabilities, others increased ¥1,362mn and the provision for a litigation loss rose ¥1,161mn. Total net assets increased ¥2,088mn on the end of the previous fiscal period to ¥65,982mn. This was because the main decrease factors, including dividend payments of ¥3,678mn and a valuation difference on available-for-sale securities of ¥1,283mn, were exceeded by the recording of net income attributable to owners of the parent of ¥8,241mn.

The equity ratio, which indicates financial soundness, rose from 37.4% at the end of the previous fiscal year to 38.0%, while the interest-bearing debt/EBITDA ratio fell from 1.80 to 1.63 times, and in such ways, the Company's financial soundness is steadily improving. It is currently progressing the medium-term management plan, in which it sets out the policy of actively investing in growth, including for M&A, and the Company intends to keep the equity ratio at around the 30% level while continuing to invest for the time being.

Looking at the cash flow conditions, cash flow from operating activities was ¥22,535mn, cash flow from investing activities was ¥12,131mn, and the free cash flow was ¥10,403mn, so the Company continues to generate stable cash flows. It used the free cash including for dividend payments of ¥3,678mn and to repay interest-bearing debt, which improved its financial position.

TOKAI Holdings Corporation
3167 Tokyo Stock Exchange First Section

1-Jul.-2020

<https://www.tokaiholdings.co.jp/english/ir/>

Result trends

Consolidated balance sheets

	FY3/17	FY3/18	FY3/19	FY3/20	Change
Total assets	161,112	165,993	167,606	169,972	2,366
(Cash and deposits)	3,239	3,143	4,164	4,629	465
Total liabilities	104,665	104,543	103,711	103,989	278
(Interest-bearing debt)	54,137	50,980	50,604	48,273	-2,331
Net assets	56,446	61,450	63,894	65,982	2,088
EBITDA	28,392	26,318	28,148	29,651	1,503
Interest-bearing debt/EBITDA rate (times)	1.91	1.94	1.80	1.63	-0.17
Equity ratio	34.5%	36.3%	37.4%	38.0%	0.6pt

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

Cash flow conditions

	FY3/17	FY3/18	FY3/19	FY3/20
Cash flows from operating activities	26,692	20,909	21,605	22,535
Cash flows from investing activities	-10,985	-11,488	-12,443	-12,131
Free cash flow	15,706	9,421	9,161	10,403
Cash flow from financing activities	-16,643	-9,527	-8,147	-10,375
Cash and cash equivalents	3,111	3,004	4,018	4,046

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

Outlook

The impact of COVID-19 outbreak is minimal and the outlook for the FY3/21 results is for record highs for the third consecutive period

1. Outlook for FY3/21 consolidated performance

For the FY3/21 consolidated results, the Company is forecasting higher sales and profits once again, with net sales to increase 4.8% YoY to ¥205,300mn, operating profit to rise 5.5% to ¥15,000mn, recurring profit to grow 2.7% to ¥14,870mn, and net income attributable to owners of the parent to climb 2.7% to ¥8,460mn. In addition to completing the IP20 medium-term management plan, FY3/21 is positioned as an important one in order to work to establish the foundations for the next medium-term management plan. The Company is aiming to grow sales and to enhance the earnings base by continuing to increase the number of continuous-transaction customers (the forecast is for an increase of 110,000 on the end of the previous fiscal period to 3.11 million customers), which is thought will lead to the growth of the Group in the medium- to long-term.

Looking by business segment, sales are expected to increase in every business segment, while the outlook is that profits will also continue to rise in the mainstay businesses, centered on the gas business. New M&A projects that are still at the negotiating stage have not been incorporated into the results forecasts. Also, while it is possible that the COVID-19 outbreak will have a partial impact on some businesses, including the corporate information and communication services and the building and real estate business, at FISCO, we think it will have practically no effect on the mainstay businesses of lifestyle services, which include the gas, CATV, and Internet services.

TOKAI Holdings Corporation
3167 Tokyo Stock Exchange First Section

1-Jul.-2020
<https://www.tokaiholdings.co.jp/english/ir/>

Outlook

Outlook for FY3/21

(¥mn)

	FY3/20		FY3/21		YoY
	Results	% of sales	Forecast	% of sales	
Net sales	195,952	-	205,300	-	4.8%
Operating profit	14,224	7.3%	15,000	7.3%	5.5%
Recurring profit	14,479	7.4%	14,870	7.2%	2.7%
Net income attributable to owners of the parent	8,241	4.2%	8,460	4.1%	2.7%
Net income per share (¥)	62.93		64.60		

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

Working on progressing M&A, implementing ABCIR+S, and deepening TLC as its key measures

2. Key measures

The Company has set three themes as the key measures for FY3/21; progressing M&A, implementing ABCIR+S, and deepening TLC.

(1) Progressing M&A

In the medium-term management plan IP20, which was started in FY3/18, improving the topline by “progressing M&A” was set as one priority strategy, and the Company has progressed negotiations while looking at a total investment amount of ¥100bn. In terms of the results up FY3/20, it has completed 9 M&A and entered-into 2 alliances by investing a total amount of ¥8,629mn, from which it has realized net sales of ¥7,677mn, operating profit of ¥555mn, and the addition of 350,000 continuous-transaction customers.

Currently also, it is investigating in-house or progressing negotiations with the other party for 26 M&A projects worth a total of ¥102.9bn. Whether or not it will be able to invest ¥100bn during the period of the current medium-term management plan will depend on the market environment and the state of negotiations with the other parties. But its policy is to continue to progress M&A during the period of the next medium-term management plan as well.

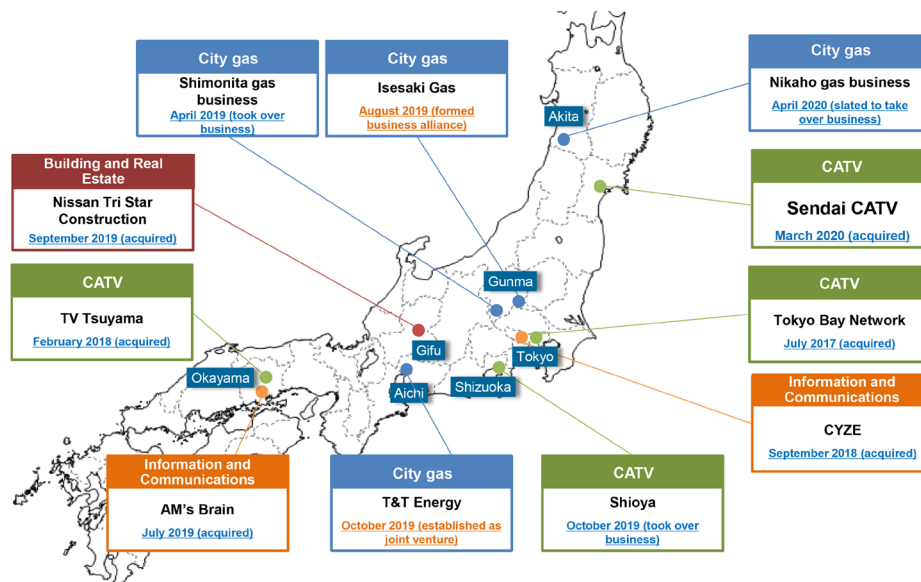
TOKAI Holdings Corporation
3167 Tokyo Stock Exchange First Section

1-Jul.-2020

<https://www.tokaiholdings.co.jp/english/ir/>

Outlook

Achievements from the Company's M&A strategy



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

Track record of M&A and alliances

Business	Number of companies	Investment amount	Net sales	Operating profit	Number of customers
City gas	4	1,953	622	41	6
CATV	4	3,997	4,624	265	344
Information and communication services	2	655	385	52	-
Building and real estate	1	2,024	2,046	197	-
Total	11	8,629	7,677	555	350

Note: The figures for net sales and operating profit include the contributions from the city gas business of Akita Prefecture, Nikaho City, and Sendai CATV from FY3/21 onwards

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

(2) Implementing ABCIR+S

Amid the spread of smartphones and the evolution of IT technologies like AI and IoT, the Company is incorporating these technologies into its services to increase their diversity and sophistication and to improve the loyalty of customers. At the same time, it is working on its ABCIR+S strategy to improve sales efficiency and to reduce customer acquisition and maintenance costs through introducing digital marketing technologies. ABCIR+S stands for AI (A), Big Data (B), Cloud (C), IoT (I), Robotics (R), and Smart Phone (S)

TOKAI Holdings Corporation
3167 Tokyo Stock Exchange First Section

1-Jul.-2020

<https://www.tokaiholdings.co.jp/english/ir/>

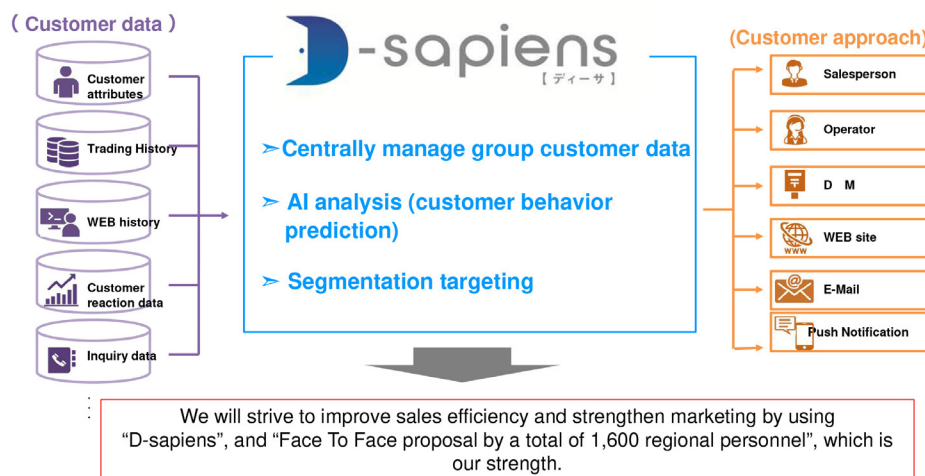
Outlook

In FY3/20, the Company completed the in-house development of D-sapiens, a DMP* that will be the basis for its ABCIR+S strategy. D-sapiens centrally manages customer data and uses AI to analyze customers' behavior histories (online history, transaction history, inquiry history, etc.), which makes it possible to predict with a high degree of accuracy customers' behavior patterns, such as to discover potential demand and signs of contract cancellations. Based on this prediction data, the Company will propose those services to customers that meet their needs on the optimal timing and using the optimal method, which will lead to acquisitions of new contracts. It is also expected to have the effect of preventing contract cancellations, as customers showing signs of cancelling a contract will be approached before they cancel. One of the Company's strengths is "face-to-face sales proposals through a total of 1,600 locally based sales personnel," and combining this strength with D-sapiens is expected to lead to improved sales efficiency and a reduction in customer acquisition and maintenance costs. As the first attempt, the Company started utilizing D-sapiens in the Aqua business in April 2020, and from 2H onwards after it has accumulated expertise, it plans to utilize it in LIBMO and other services as well.

* DMP refers to the platform for the integrated management and analysis of Big Data accumulated on the various servers on the Internet and log data for its own website, to ultimately realize the optimization of the action plan, including the distribution of advertisements.

D-sapiens – strengthening marketing through “Real”x“Digital” –

- Centrally manage customer data built up through communication with customers
- AI analysis accurately predicts customer behavior patterns such as “Uncovering potential demand” and “Price orientation and sign of cancellation”
- A customer approach that delivers the desired service at an appropriate distance according to the customer's lifestyle



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

(3) Deepening TLC

The Company intends to expand its customer base by realizing its TLC vision, which aims to provide comprehensive and detailed support for customers' comfortable lifestyles through the various services provided by the Group. As one strategy toward expanding the customer base, it is working to improve the contract rate for multiple services. By providing multiple services to a single customer, the aim is to reduce customer acquisition and maintenance costs, while it will also lead to a reduction in the contract-cancellation rate. At the time it set-out the TLC concept in 2011, the contract rate for multiple services was only around the 7% level, but by the end of FY3/20 it had risen to as high as 18.8%, and the target is for it to be above 20% by the end of FY3/21.

Outlook

To achieve this target, the Company has strengthened measures for CATV companies which previously had low contract rates for multiple services. The CATV companies have also been operating in regions in which the Group does not provide services, such as Nagano and Okayama. But in the future, the aim is to raise the contract rate for multiple services by also providing set plans, such as for the low-cost mobile service LIBMO.

Also, as a new measure, the Company is entering-into a new field. Specifically, it is considering providing healthcare services, including for health and preventive medicine. In April 2020, it newly established the Healthcare Business Planning Office and embarked on creating a fully-fledged business model. In order to realize all-generational social security reforms, health and preventive medicine was incorporated as an important policy within the Japanese government's Growth Strategy Execution Plan, which was created from a Cabinet resolution in June 2019. The policy for the future is to aim to promote the health of citizens as a whole by investing public funds and promoting the participation of private-sector companies, which will contribute to keeping down social security costs, including medical and nursing costs, which are increasing year by year.

The Company is currently considering starting a business for two areas, cancer and lifestyle-related diseases. For cancer, it envisages a genetic testing service, using genetic analysis techniques to determine the risk of developing cancer in the future and its early detection. Also, in the lifestyle-related diseases field, it anticipates services for a health-promotion program that utilizes technologies such as IoT and a smartphone app to improve lifestyle-related problems, and a program to maintain and strengthen bodily functions through evaluating scoring for cognitive strength and muscular strength. It plans to progress these services through alliances with other companies, and it hopes to announce some of them during FY3/21.

Looking from the perspective of health management, in March 2020 the Company announced that it has been selected for the first time as a Health Management Brand, a system implemented by the Ministry of Economy, Trade and Industry (METI) and the Tokyo Stock Exchange. The Health Management Brand designation indicates those companies that, among listed companies, are evaluated as considering the management perspective for their employees' health management and that are conducting strategic measures for it. In principle, one company per industry is elected, and as it began in 2015, this is the sixth time the selections have been made. The Company was also certified for the fourth consecutive year among the Excellent Health Management Corporations 2020 (large scale corporations sector) – White 500, which is jointly implemented by METI and Nippon Kenko Kaigi. Moreover, 1 Group company was newly certified in Excellent Health Management Corporations 2020 (large scale corporations sector), while 2 were newly certified in the Excellent Health Management Corporations 2020 (medium- and small-scale corporations sector), meaning that 15 Group companies are now certified. In such ways, the Group's companies can be highly evaluated for actively tackling health management.

Strengthening measures toward increasing the number of customers in the mainstay businesses, and corporate information and communication services continue to perform well

3. Net sales outlook by segment

The results forecasts for the main businesses are described below.

(1) Gas and petroleum business

For the gas and petroleum business, although sales unit prices will decline, this will be absorbed by the increase in the number of customers. So the outlook is that net sales will increase 2% YoY and that operating profit will rise 9% from the effects of the reduced purchasing costs

Outlook

In the LP gas business, the number of customers is expected to increase 51,000 on the end of the previous fiscal period to 703,000 customers. The Company will acquire customers in new areas and is working to acquire them in existing areas. Conversely, in the city gas business, the number of customers is set to remain unchanged on the end of the previous fiscal period at 61,000 customers. However, as the figure at the end of the previous period included the addition of 5,000 customers in Nikaho City, Akita Prefecture, for which a business was started from April 2020, in actuality, the number of customers will increase 9% YoY. As sales unit prices are falling, the forecast is that net sales will increase only slightly.

(2) Information and communication services business

In the information and communication services business, the forecasts are for net sales to increase 2% and operating profit to rise 5%. Within these results, the outlook is that sales and profits in the consumer business will continue to decline, which will be covered by the growth of the corporate business.

The number of customers in the consumer business is expected to change direction and increase, up 2,000 on the end of the previous fiscal period to 975,000 customers. Breaking this down, they will decrease 21,000 for existing ISP and related services to 368,000 customers, they will increase 13,000 for the Hikari Collaboration to 337,000 customers, they will increase 15,000 for LIBMO to 63,000 customers, and they will decrease 5,000 for mobile to 207,000 customers. For the increase for Hikari Collaboration, the effects of set sales with other products, which were started on a trial basis in some stores in major consumer electronics retailers from the 4Q, have been confirmed, so customer numbers are expected to increase from this initiative being developed at all stores nationwide. For LIBMO also, the aim is to increase the number of contracts through conducting set sales with the Hikari Collaboration and strengthening online advertising. The outlook is that profits will decrease due to the effects of the lower sales and also the increase in customer-acquisition costs.

Conversely, in the corporate business, the outlook is for sales and profits to continue to increase from the growth in demand for network connection services and Cloud-system builds, which are benefiting from the growth of the Cloud services market, and also for outsourced systems development.

(3) CATV business, Aqua business and Building and real estate business

In the CATV business, the forecasts are for net sales to increase 6% YoY and operating profit to grow 2%. The plan* is for the number of customers to increase by 37,000 on the end of the previous fiscal period to 1,191,000 customers. Sales will increase approximately ¥2bn, but half of this amount will be from the contribution of Sendai CATV, which has newly been made a subsidiary, while the remaining half will be from customer acquisitions by the existing subsidiaries. If excluding Sendai CATV, the sales growth rate will be 3%, the same as in the previous fiscal year, so it would seem to be an achievable level. The main reason for the low operating profit growth rate is the increase in depreciation and amortization costs from the plan to strengthen the personnel structure. Currently, each subsidiary is investing in converting to fiber optics, and the capital investment amount is scheduled to increase from ¥5.3bn in the previous fiscal period to ¥6.7bn.

* The number of Sendai CATV customers was included in the result for FY3/20, so the increase in FY3/21 is only from new customer acquisitions by the various subsidiaries.

In the building and real estate business, the forecasts are for net sales to increase 15% YoY and operating profit to rise 4%. This is because, in addition to the contribution of the full fiscal year results of Nissan Tri Star Construction, in existing businesses as well, demand, which had cooled due to the impact of the consumption tax hike in the previous fiscal period, will recover. However, at FISCO, we think that orders for projects may be delayed due to the impact of the novel coronavirus, so there is a risk that sales will be below forecast.

Outlook

In the Aqua business, the forecasts are for net sales to increase 6% YoY, but for operating profit to continue to decrease. Through sales to large-scale commercial facilities and other facilities in the main cities, the number of customers will increase 11,000 on the end of the previous fiscal period to 172,000 customers. The net increase in the previous fiscal period was 5,000 customers, so the pace of the increase has slowed down. So in this fiscal period, the Company will focus on acquiring customers, and therefore it plans to increase customer-acquisition costs. During April and May, a situation continued in which sales promotions could not be implemented in commercial facilities because of the impact of COVID-19 outbreak, and depending on the situation in the future, it is possible that acquisitions of new customers will be less than forecast. However, this would be a positive factor for profits, as it means no customer-acquisition costs will be incurred.

Shareholder return policy

Annual return on investment of 4% to 7% from the gifts to shareholders and dividends

The Company returns profits to shareholders by paying dividends, presenting shareholders with gifts, and also purchasing treasury shares depending on conditions. Its basic policy is to continuously pay a stable dividend and it targets a dividend payout ratio of 40% to 50%. The FY3/21 dividend per share will be unchanged YoY at ¥28.0 (for a dividend payout ratio of 44.3%).

The Company presents gifts to shareholders at the end of March and September depending on the number of shares held. For each unit of shares (100 shares) held, shareholders can receive one of the following gifts: an Aqua product worth ¥2,050 (such as the Ulunom “Fuji-no-Tennensui Sarari” (natural water from Mt. Fuji), etc.), a QUO card worth ¥500, meal coupons worth ¥1,000, TLC Membership Service points worth ¥1,000, or a ¥2,100 discount on LIBMO usage fees (¥350 a month x 6 months). When including the gifts to shareholders in an estimate of the total investment yield per share unit from the current share price level (closing price of ¥985 on May 21, 2020), it is in the range of 3.9% to 7.0% (depending on the selection of either a QUO card or an Aqua product as the gift).

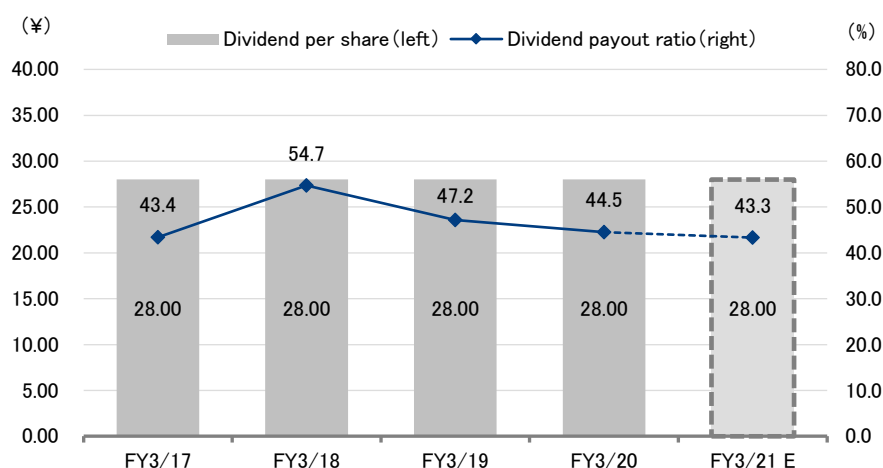
TOKAI Holdings Corporation
3167 Tokyo Stock Exchange First Section

1-Jul.-2020

<https://www.tokaiholdings.co.jp/english/ir/>

Shareholder return policy

Dividend per share and dividend payout ratio



Note: Including a commemorative dividend of ¥6 in FY3/17

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

Shareholder gifts

Shareholders on record at the end of March and September are presented with their choice of one of the following five type of gifts, as well as a 10% discount coupon for a standard wedding service at the Group's wedding halls, plus a discount of ¥100,000 and a dining certificate with 20% discount coupon (a book of 12 certificates) for the Beau Ciel and Aoi restaurants.

Shares held	100-299 shares	300-4,999 shares	Over 5,000 shares
Aqua product	¥2,050 worth	¥4,100 worth	¥8,200 worth
QUO card	¥500 worth	¥1,500 worth	¥2,500 worth
A Group restaurant dining certificate	¥1,000 worth	¥3,000 worth	¥5,000 worth
TLC Points	¥1,000 worth	¥2,000 worth	¥4,000 worth
LIMBO monthly usage fee	¥2,100 worth	¥5,100 worth	¥11,280 worth

Source: Prepared by FISCO from the Company website

Information security measures

In terms of information security measures, previously each Group company had separately managed the personal information held and conducted measures against system failures and cyber-attacks. Since FY3/18, the Company has also established a Group-wide expert committee in order to share information between all the Group companies and at the same time, to heighten awareness of its security measures.

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