COMPANY RESEARCH AND ANALYSIS REPORT

# Trust Tech Inc.

## 2154

Tokyo Stock Exchange First Section

16-Apr.-2019

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# Summary

## Healthy advances in domestic and overseas businesses, expecting early attainment of ¥10bn in operating profit with further pick-up in the growth pace

Trust Tech Inc. <2154> (hereafter, also “the Company”) is a staffing company that mainly dispatches engineers and manufacturing staff and handles subcontracting for development, design, and production. Its core strength is dispatching/subcontracting engineers, and Trust Tech stands out among listed companies in the technology staffing industry with its aggressive pursuit of overseas opportunities.

**1. Posted large sales and profit increases again in 1H FY6/19**

The Company posted large sales and profit increases again in 1H FY6/19 with ¥40,246mn in net sales (+35.6% YoY) and ¥3,112mn in operating profit (+40.8%). Sales rose substantially on continued strong growth in domestic engineering field supported by robust demand and consolidated additions by two UK-based subsidiaries in the overseas field. In profits, the Company sustained top-level profitability in Japan both in engineering and manufacturing fields and reached an operating profit on healthy progress by the UK subsidiaries in the overseas field.

**2. Aiming for early realization of mid-term business plan goals via a beneficial cycle of “human resource recruitment ⇨ profit expansion ⇨ better terms ⇨ …” and “region x business field” strategy**

The Company is currently implementing its three-year rolling mid-term business plan that covers FY6/19 to FY6/21. The plan targets continuation of 20% annual growth rates in net sales and operating profit continuing along existing paths of "region" and "field" growth. The Company has medium-term goal of ¥10bn in operating profit and hopes to attain it ahead of time during the current mid-term business plan period. While recruitment of human resources is a key factor that influences growth, the Company is making smooth progress hiring people, including the prospect of over 950 new university graduates joining in April 2019. It is also putting efforts into better terms for employees in order enhance recruitment and raise the retention rate. We think it has put in place a beneficial cycle of “human resource recruitment ⇨ profit expansion ⇨ better terms ⇨ …”

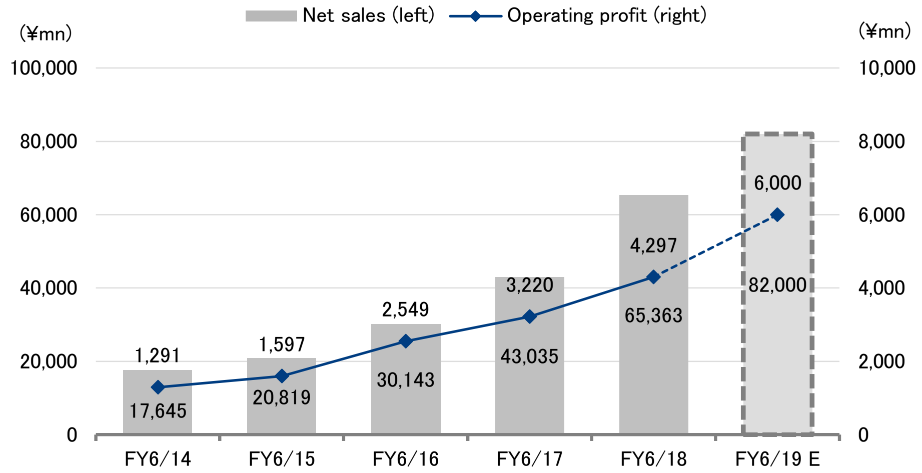
**3. Possibility of the growing presence of the overseas field becoming a major medium-term engine, focus on Asian initiatives too**

The overseas field has mainly pursued opportunities in developed countries with mature staffing markets, and the Company acquired three subsidiaries in the UK thus far as a result. This policy remains intact. The Company remains ready to aggressively engage in M&A deals that are available in EU countries, the US, and other markets. Meanwhile, it is steadily ramping up staffing business in Asia too. The Company has two joint ventures in China that conduct staffing business, and these entities are developing smoothly. In 2019, it invested in a major Vietnam-based staffing company and thereby created a foothold in Vietnam’s staffing market. We expect involvement in a more substantive manner in subsequent activities and see transformation of Asia into a profit source.

**Key Points**

- Aims to sustain strong growth by expanding regionally and in business fields; headed for the early achievement of ¥10bn in operating profit
- Hopes to continue robust growth and high profitability by aggressively hiring engineers and implementing measures to enhance engineer value
- Entering Vietnam's staffing business following China and Indonesia

Results trend




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

# Company profile

## Currently sustaining robust growth with multiple acquisitions in Japan and abroad

### 1. History

Sanei Shoji Inc. and others established Kyousei Sangyou Inc. (Trust Tech's predecessor) in 1997 as a special subsidiary based on the Act on Employment Promotion etc. of Persons with Disabilities. Amuse Capital acquired all of the company's shares and changed its name to Trust Works Sanei Inc. in 2004 and also expanded business scope to dispatching services (specified worker dispatching business) and other areas. Trust Works Sanei acquired all shares in former Trust Tech Inc., which was a company under Amuse Capital, in 2005 and entered the engineer dispatching business. It merged with former Trust Tech in 2008 and changed its name to Trust Tech Inc., completing the foundation of current operations.

Trust Tech subsequently pursued M&A deals to broaden its business scope, including rapid acquisitions as subsidiaries of PLM (now, consolidated subsidiary TTM Inc.) in 2009, International Dispatching Human Resources Limited (now, consolidated subsidiary HKTT Limited) in 2010, and Freedom Co., Ltd. (now, TRUST NEXT SOLUTIONS Inc.) and Kanamoto Engineering (changed its name to Trial but was absorbed into Trust Tech in October 2016) in 2015. It acquired UK-based dispatching firm MTrec Liimited as a subsidiary in August 2016, giving it a foothold to promote full-fledged overseas initiatives, and then purchased UK-based Gap Personnel Holdings Limited (GAP) as a subsidiary in December 2017 (this deal involved direct acquisition of holding-company 1998 Holdings Limited). It also acquired FUSIONi Co., Ltd. as a subsidiary in March 2017 (renamed as Trust iPowers Inc. in January 2018) as part of broadening business scope to IT and software. The Company acquired UK-based Quattro Group Holdings Limited as the third entity in this country in August 2018.

## Pursuing three main fields - engineer dispatching, manufacturing staff dispatching, and overseas business

### 2. Business overview

Trust Tech has had two main business domains – the engineering field, which covers engineer dispatches and the development and design subcontracting, and manufacturing field, which handles manufacturing subcontracting and dispatching of manufacturing workers to production lines. It switched to three business segments from FY6/17 with the addition of an overseas field to cover overseas business. Trust Tech's overall income consists of these three reporting segments plus other income from special subsidiary Trust Tech With Inc. (renamed from Kyousei Sangyou Inc. in March 2017) that handles employment for disabled persons and from real estate leasing business.

The corporate group consists for Trust Tech and consolidated subsidiaries TTM Inc., TRUST NEXT SOLUTIONS and Trust iPowers in Japan. As business fields, Trust Tech, TRUST NEXT SOLUTIONS and Trust iPowers handle engineering while TTM runs the manufacturing.

Overseas initiatives started with the acquisition of a Hong Kong-based company, which provides engineering recruitment and other services, in June 2016. Since then, the Company has rapidly expanded business scope by setting up sites in Asia, with emphasis on China, and simultaneously making acquisitions in the UK. Overseas field sales are rising above the ¥30bn range due to major acquisitions in the UK of MTrec in August 2016, GAP in December 2017, and Quattro Group in August 2018. In January 2019, it purchased shares of L&A Investment Corporation (LAI) acquiring a 44.42% stake, which owns one of Vietnam's largest staffing companies.

Overview of Trust Tech group companies

| Business segment | Company name | Business content | Equity stake | Comment |
|---|---|---|---|---|
| Engineering field | Trust Tech Inc. | Provides dispatching, subcontracting, outsourcing, and recruitment services in the engineering field | - | |
| | TRUST NEXT SOLUTIONS Inc. | Provides control-related software development, design assistance, and testing | 100% | Acquired as a subsidiary in July 2015, merged with the group and changed the company name in April 2018 |
| | Trust iPowers Inc. | Provides dispatching and outsourcing services in the ICT field | 100% | Acquired as a subsidiary in March 2017, changed the company name in January 2018 |
| Manufacturing field | TTM Inc. | Provides subcontracting and dispatching services in the manufacturing field | 100% | |
| Other | Trust Tech With Inc. | Provides an environment for disabled people to engage with others as members of society | 100% | Formerly Kyousei Sangyou Inc. |
| Overseas field | MTrec Limited | Handles dispatching and recruitment business | 83% | Acquired shares in August 2016 |
| | PT.TRUST TECH ENGINEERING SERVICE INDONESIA | Personnel placement | 100% | Established in September 2016 |
| | Shan Dong Trust Bridge Human Resources Inc. | Dispatching, subcontracting and personnel placement | 49% | Established in October 2016 |
| | Trust Tech Human Business Consulting Shanghai Inc. | Personnel placement | 100% | Established in July 2017 |
| | Guangzhou Trust Dianmi Human Resources Inc. | Dispatching, subcontracting and personnel placement | 49% | Established in June 2017, began business in January 2018 |
| | Gap Personnel Holdings Limited | Dispatching and personnel placement | 75% | Acquired shares in December 2017 |
| | Quattro Group Holdings Limited | Dispatching and personnel placement | 75% | Acquired shares in August 2018 |
| | L&A INVESTMENT CORPORATION (LAI) | Handles staffing, staff introductions, and executive searches | 44.42% | Acquired shares on January 23, 2019, treated as an equity-method affiliate |

Source: Prepared by FISCO from securities reports and press releases

## Securing engineers is the key to growth; accelerating the pace of mid-career and new university graduate hires and focusing on a higher retention rate with better terms

### 3. Income structure of the engineering field segment

In the engineering field segment, Trust Tech handles the dispatch, subcontracting, and outsourcing of its engineers for R&D, design, production technology, and other technology areas at customer companies. Actual business content can be largely divided into dispatching engineers and development, design, and other subcontracting, with about 80% dispatch of engineers and 20% is subcontracting. The outsourcing business mainly involves work conducted by the Company's engineers at customer facilities, and outsourcing development at its own facilities is rare.

Average prices are higher in the engineering field compared with those in the manufacturing field because of the added value of "engineers." Price difference results in the profitability gap between the two segments. While it might appear that subcontracting should be more profitable than dispatching service, dispatching delivers almost the same profitability in many cases because process step estimates, deadlines, and other aspects of subcontracting business often differ from the initial budget in actual implementation.

Growth in this field depends on the Company's ability to secure a large number of talented engineers. It is more important to find engineers than destinations in the current tight labor environment. Trust Tech had focused on acquiring human resources by hiring people with an existing career who can be immediately used on projects, ramped up mid-career recruitment for the year ending June 30, 2019. It has also been hiring new graduates more aggressively in the past few years; in addition to hiring around 500 graduates in April 2018, the Company is making progress on recruitment for this year as well with plans to hire around 750 new graduates in April 2019.

An important point along with hiring is boosting the engineer retention rate. Trust Tech is putting efforts into increasing the average dispatching price and improving compensation for engineers. Increase in the average price is often achieved through assignments to customers paying higher prices. Key points in accomplishing this are more precise understanding of individual engineer skills and market value and matching these features with suitable assignments. Trust Tech intends to place even stronger emphasis on talent management.

## Profitability is the top priority, strongly promoting efficient matching with locally-oriented hiring and sales activities

### 4. Income structure of the manufacturing field segment

The manufacturing field segment operates services that supply personnel for production lines at customer companies using its production line staff. It uses operation subcontracting (on-site subcontracting) and manufacturing staff dispatches as the two services formats. While sales ratios of subcontracting and dispatching fluctuate, the split appears to be roughly equal. In a comparison of subcontracting and staff dispatches for manufacturing, profitability should be higher for subcontracting because of leeway to raise margin by enhancing productivity with autonomous efforts. The reality, however, is profitability does not differ much because of stringent terms from the customer side.

Manufacturing services have a lower average fee than engineering, and sales vary more due to impact of changes in demand for manufactured products. Contract periods tend to be shorter as well. These attributes contribute to lower profitability in manufacturing services versus engineering.

Trust Tech is focusing on locally-oriented hiring and sales activities in order to enhance profitability in the manufacturing field. Dispatches of manufacturing personnel to remote locations involve moving and transfer expenses. This approach aims to curtail and reduce such costs. Japan has many corporate communities in automotive, electric equipment, and other fields in its regional cities. Effective matching via recruitment of workers and subcontracting and dispatching customers in such regional cities enhances the cost reduction efficiency. Trust Tech has been improving its profitability in the manufacturing field due to success in steadfast efforts with this type of regional focus; EBITDA margin reached 5.2% and operating margin was 5.1% in 1H FY6/19, arriving at a leading position in the industry.

Employee numbers in the manufacturing field segment has been in a range of 2,000 to 2,500 people up to now due to responses to changes in subcontracting and dispatching demand. Furthermore, manufacturing subcontracting and dispatching demand is rooted in efforts to lower labor costs at customer firms. Considering this background, Trust Tech enlists a mix of indefinite-term employees and limited-term employees in the manufacturing field to flexibly meet demand. Trust Tech sees shortages in manufacturing personnel in Japan as a structural issue and expects continued rise in demand in the medium to long term for manufacturing staff.

## Implements manufacturing staffing business at three subsidiaries in the UK, expanding Asian business to Vietnam

### 5. Overseas field details and income structure

The “overseas field” is a categorization based on the geographical aspect of the business, rather than a distinction related to the nature of business in Japan. In the overseas field, the Company adjusts its market engagement and growth strategy by mature markets (mainly developed countries) and immature markets in Asia and other areas because extent of development in human resource service business differs depending on the level of social maturity.

In mature markets, the Company follows a basic policy of entering through acquisition of local companies due to the large number of existing human resource companies. It has acquired three subsidiaries in the UK (MTrec, GAP, and Quattro Group) with business content that corresponds to the manufacturing field in Japan. Income structure hence is nearly the same as its domestic manufacturing field.

Asia, meanwhile, is an immature market, and the Company is gradually building operations as the market advances. Its local subsidiaries are only engaged in staff introduction business at this point. This is because staffing markets are still under-developed. These sites are currently serving in a role of implementing market surveys and gathering information. The Company’s subsidiaries appear to be profitable thanks to having light cost structures.

Joint ventures, meanwhile, are more actively promoting business because the presence of a partner helps alleviate risk. The two joint ventures in China are both conducting Japanese-style staffing businesses. The early one in Shandong has already reached profitability, while the Guangdong business is following the same path as Shandong and is within range of profitability in the near future. In January 2019, the Company invested in a major staffing firm in Vietnam. We expect the Company to shift to a stage of full-fledged rollout of its own staffing business in Asia in the future if results at these joint ventures and investment affiliates steadily expand.

# Business performance

## Posted steep sales and profit increases; sales rose sharply on sustained high growth in engineering field and consolidated additions from two UK companies in the overseas field

The Company posted steep sales and profit gains in 1H FY6/19 with net sales at ¥40,246mn (+35.6% YoY), operating profit at ¥3,112mn (+40.8%), ordinary profit at ¥3,079mn (+39.9%), and profit attributable to owners of parent at ¥2,000mn (+52.4%). Net sales and operating profit reached all-time highs. EBITDA (operating profit + amortization of goodwill + depreciation + one-time acquisition costs), which the Company monitors as a key performance indicator (KPI), rose 31.0% to ¥3,673mn.

Overview of 1H FY6/19 results

(¥mn)

| | FY6/18 | | | FY6/19 | | | |
|---|---|---|---|---|---|---|---|
| | 1H results | 2H results | Full year | 1H results | YoY | Progress rate | Full-year forecast |
| Net sales | 29,676 | 35,687 | 65,363 | 40,246 | 35.6% | 49.1% | 82,000 |
| Operating profit | 2,210 | 2,086 | 4,297 | 3,112 | 40.8% | 51.9% | 6,000 |
| Operating profit margin | 7.4% | 5.8% | 6.6% | 7.7% | - | - | 7.3% |
| Ordinary profit | 2,201 | 2,027 | 4,228 | 3,079 | 39.9% | 52.2% | 5,900 |
| Profit attributable to owners of parent | 1,312 | 1,256 | 2,569 | 2,000 | 52.4% | 54.1% | 3,700 |
| EBITDA | 2,803 | 2,529 | 5,332 | 3,673 | 31.0% | 52.1% | 7,048 |

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

The Company runs its operations with three business segments (engineering, manufacturing, and overseas fields), and all three segments reported higher sales and profits YoY.

Hiring activity for new graduates was a major event in 1H. The Company has achieved very smooth progress in hiring for April 2019 and currently expects about 950 new entrants (it ultimately anticipates the addition of a few more tens of people because hiring efforts are continuing in 2H too).

Below we review trends by business segments.

Breakdown by business segments

(¥mn)

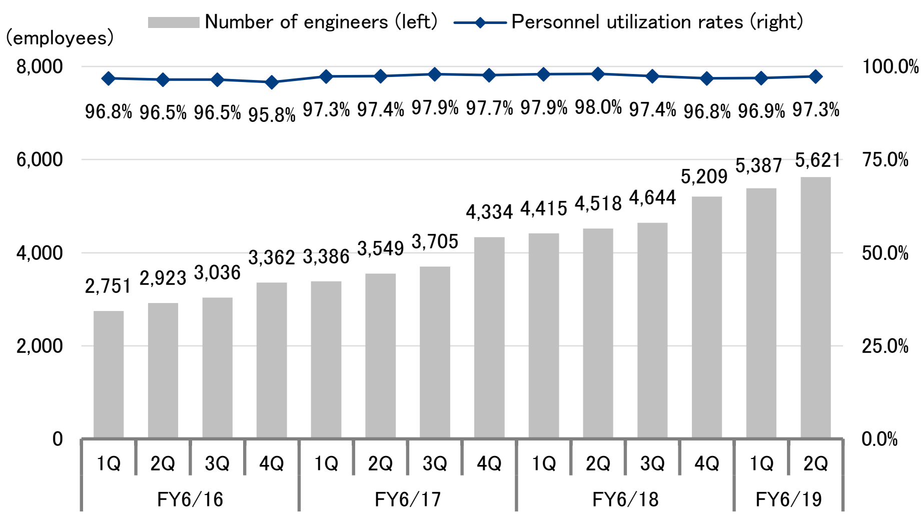
| | | FY6/18 | | | FY6/19 | | | |
|---|---|---|---|---|---|---|---|---|
| | | 1H | 2H | Full year | 1H | YoY | Progress rate | Full-year forecast |
| Net sales | Engineering field | 16,069 | 17,504 | 33,573 | 19,875 | 23.7% | 48.2% | 41,230 |
| | Manufacturing field | 4,918 | 4,984 | 9,902 | 5,105 | 3.8% | 46.4% | 11,000 |
| | Overseas field | 8,711 | 13,262 | 21,974 | 15,317 | 75.8% | 51.3% | 29,830 |
| | Other | 30 | 38 | 69 | 51 | 69.8% | 65.4% | 78 |
| | Net sales prior to adjustment (total) | 29,729 | 35,790 | 65,519 | 40,349 | 35.7% | 49.1% | 82,138 |
| | Adjustment | -53 | -102 | -156 | -103 | - | - | -138 |
| | Net sales (total) | 29,676 | 35,687 | 65,363 | 40,246 | 35.6% | 49.1% | 82,000 |
| EBITDA | Engineering field | 2,281 | 2,115 | 4,396 | 3,011 | 32.0% | 51.3% | 5,873 |
| | Manufacturing field | 254 | 282 | 536 | 266 | 4.9% | 47.3% | 562 |
| | Overseas field | 311 | 165 | 476 | 432 | 39.0% | 59.1% | 731 |
| | Other | -57 | -74 | -131 | -72 | - | - | -244 |
| | EBITDA prior to adjustment (total) | 2,790 | 2,488 | 5,278 | 3,638 | 30.4% | 52.5% | 6,923 |
| | Adjustment | 13 | 41 | 54 | 35 | 156.2% | 28.0% | 125 |
| | EBITDA (total) | 2,803 | 2,529 | 5,332 | 3,673 | 31.0% | 52.1% | 7,048 |

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

### 1. Trends in the engineering field

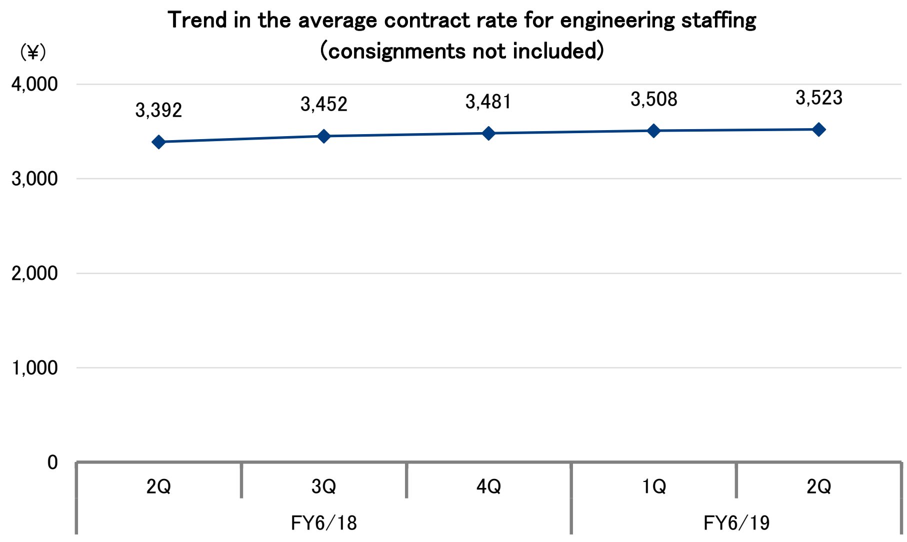
The engineering field booked ¥19,875mn in net sales (+23.7% YoY) and ¥3,011mn in EBITDA (+32.0%). Engineer staffing volume steadily expanded at all customers amid sustained strong demand in transportation equipment and electric equipment industries, which are existing core areas, and robust demand in IT-related industries where the Company is focusing efforts.

Trends in the number of engineers and utilization rates




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

The average contract rate on a quarterly basis continues to rise each quarter amid vibrant demand for engineers. It increased 3.9% YoY to ¥3,523 in 2Q FY6/19 (Oct-Dec 2018). This trend and above-mentioned increase in the number of dispatched engineers are major drivers fueling high sales growth in the 20% range.




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

### 2. Trends in the manufacturing field

The manufacturing field reported ¥5,105mn in net sales (+3.8% YoY) and ¥266mn in EBITDA (+4.9%). The Company positions the manufacturing field a "stable growth" business, and puts priority on securing profitability rather than expanding market share. In 1H, it continued to focus on locally-oriented sales activity and promoted acquisition of projects with high contract rates. These efforts supported 5.2% EBITDA margin (5.1% operating margin) in 1H, which is top-class profitability in the manufacturing staffing industry.

### 3. Trends in the overseas field

The overseas field booked ¥15,317mn in net sales (+75.8% YoY) and ¥432mn in EBITDA (+39.0%). The Company added GAP as a subsidiary on December 1, 2017 and Quattro Group on August 31, 2018. The 1H results include six-months results from GAP (vs. three-months results in 1H FY6/18) and four-months results from Quattro Group (vs. zero), sharply lifting net sales. Consolidated additions by GAP and Quattro Group facilitated a hefty rise in EBITDA. While posting operating loss of ¥69mn in 1H FY6/18 due to amortization of goodwill, the segment managed to reach ¥104mn in operating profit even with amortization of goodwill this year.

# Medium- to long-term growth strategy

## Aims to sustain strong growth by expanding regionally and in business fields; headed for the early achievement of ¥10bn in operating profit

### 1. Overview of new mid-term business plan

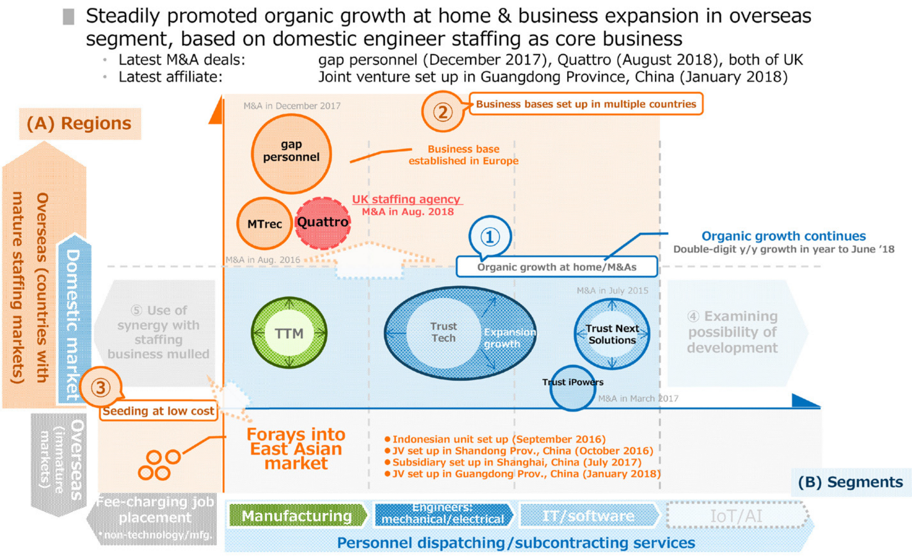
The Company presented a new three-year mid-term business plan (rolling mid-term plan) that covers FY6/19-21 at the disclosure of FY6/18 results and have since been working on achieving the targets laid out in the plan.

The Company's growth strategy framework remains basically the same as in mid-term business plans up to now. It continues to focus on establishing a unique market position and maintaining strong growth through expanding regionally and in business fields via initiatives from each of these perspectives.

On the regional track, the Company started with the domestic market and has also targeted countries and regions with mature staffing markets outside of Japan thus far. This approach led to acquisitions of three staffing companies in the UK. The Company has been promoting staff introduction and staffing businesses in China and Asia too, and we think these markets offer future growth opportunities.

On the business field track, the Company began with the manufacturing field and then shifted weight to the engineering field. While demand from transportation equipment and electric equipment industries drove the engineering field up to now, expectations have risen for growth led by demand from IT and software development industries accompanying changes in the industrial structure.

Image of medium-term growth strategy



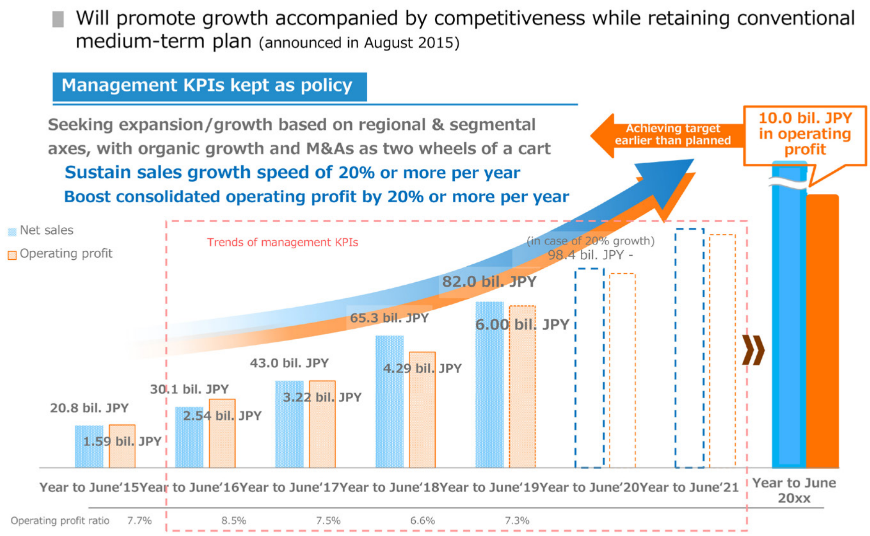

Source: The Company's results briefing materials

While the new mid-term business plan does not appear to offer much that is new at first glance, we think it has evolved from the previous plan because the Company offers more specific and detailed goals and fleshed out initiatives to achieve the goals and is taking concrete steps in various areas.

The Company only mentions "at least 20% annual growth in net sales and operating profit" as its performance goals from the second year of the three-year mid-term business plan (which corresponds to FY6/20 in the new plan). While it retains the same style this time, the Company also cited ¥10bn in operating profit as a medium-term goal. Application of the basic policy of 20% annual growth in operating profit puts attainment timing beyond the existing plan (in other words, no sooner than FY6/22). However, the Company is seeking to achieve this goal in the current mid-term business plan period in light of its track record up to now of fulfilling mid-term business plan goals one year ahead of time.

As explained above, net sales and profits are making very healthy progress thus far through 1H FY6/19.

Mid-term business plan's goals




Source: The Company's results briefing materials

## "Growth driver" business; hopes to continue robust growth and high profitability by aggressively hiring engineers and implementing talent management and other measures to enhance engineer value

### 2. Medium-term growth strategy and progress in the engineering field

As growth strategy in the engineering field, the Company wants to sustain high growth and improve profitability through concentrated investment of business resources with positioning as the main source of group growth. In this context, the Company presents three specific tactical investment areas – 1) increased hiring in all areas (new university graduates, mid-career, and overseas), 2) utilization of AI and RPA to enhance engineer value and tasks, and 3) new acquisitions. Numerical goals are 10,000 active engineers and 15% operating margin.

**Strategy and goals for the engineering field in the mid-term plan**

| Engineering field | |
|---|---|
| Strategy | Goals |
| Sustain high growth and improve profitability via concentrated investment of business resources with positioning as the main source of group growth | ☆ Investment content: Hiring (new university graduate, mid-career, and overseas)<br>Utilization of AI and RPA to enhance engineer value and tasks, new acquisitions, and others<br>☆ Target operating margin: 15%<br>☆ Target number of active engineers: 10,000 people |

Source: Prepared by FISCO from Company materials

Looking at progress in 1H FY6/19, the number of engineers is expanding smoothly, reaching 5,621 at the end of December 2018 with a 97.3% utilization rate as discussed above.

The Company is also aggressively hiring new university graduates who join in April 2019 and expects to add a total of just over 950 people, including 750 engineers. It is steadily hiring mid-career engineers as well, alongside of the new university graduates, and aims to expand the number of engineers to 6,600 people by the end of FY6/19 through these measures.

The Company targets 15% operating margin as profitability in this segment and attained a 14.0% margin for the engineering field in 1H FY6/19. At the quarterly level, operating margin was 11.7% in 1Q (Jul-Sep) and 16.1% in 2Q (Oct-Dec). We attribute the disparity to seasonal factors (differences in busyness and seasonal cost fluctuation). Nevertheless, the engineering field is clearly approaching the attainment of 15% operating margin as an average for the full year. While some observers might suggest that there is not much room left for earnings growth driven by operating margin improvement given this level, the Company explains that it still anticipates 1-2 points of margin upside.

Increase in the average dispatching price is an effective way to lifting margin. While the average dispatching price has been steadily rising due to tight supply-demand conditions, the Company is also taking steps to realize a higher average fee by implementing more precise management of “talent” (skills, personal traits, etc.) for individual engineers and dispatching engineers to locations that maximize value. Furthermore, it continues to make operational advances and improve wages, bonuses, and other terms for engineers. These efforts are targeting higher profit margin in a win-win format for engineers and the Company.

The fundamental approach of “achieving growth via regional and business field initiatives” in the Company’s growth strategy means sustaining growth in transportation equipment and electric equipment industries, the existing core areas, and expanding IT-related business as a new growth area for the engineering field. We think 1H results confirmed steady progress with these activities. In sales by industry, transportation equipment and electric equipment delivered healthy increases of 13.1% and 31.0% YoY respectively, providing solid earnings base in the engineering field, while the information and communications industry realized even stronger growth with a 40.0% gain and raised its share of segment sales from 8.5% a year earlier to 9.6% in 1H.

YoY sales comparison by industry in the engineering field

(¥mn)

| | 1H FY6/18 | | 1H FY6/19 | | |
|---|---|---|---|---|---|
| | Net sales | % of net sales | Net sales | % of net sales | YoY |
| Progress rate | 7,683 | 47.8% | 8,688 | 43.7% | 13.1% |
| Transportation equipment | 4,013 | 25.0% | 5,259 | 26.5% | 31.0% |
| Electric equipment<br>Information and communications | 1,369 | 8.5% | 1,916 | 9.6% | 40.0% |
| Machinery | 1,467 | 9.1% | 1,803 | 9.1% | 22.9% |
| Precision equipment | 318 | 2.0% | 617 | 3.1% | 94.0% |
| Chemicals | 216 | 1.3% | 235 | 1.2% | 8.8% |
| Other | 1,003 | 6.2% | 1,356 | 6.8% | 35.2% |
| Net sales (total) | 16,069 | 100.0% | 19,875 | 100.0% | 23.7% |

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

## Generates industry-leading profitability through locally-oriented hiring and sales

### 3. Medium-term growth strategy and progress in manufacturing field

The Company positions the manufacturing field as a “stable growth” business. In light of labor shortage as a structural issue in Japanese society, the Company has adopted a fundamental policy of prioritizing growth through sustaining and improving the industry-top profitability that it has already attained in the manufacturing staffing industry rather than pursuing expansion of scale and market share.

As numerical goals, it targets 5% operating margin, a symbol of high profits for the manufacturing staffing industry, and then also aims for 10% sales growth, an indicator of growth potential, while maintaining profit margin.

Strategy and goals for the manufacturing field in the mid-term business plan

| Manufacturing field | |
|---|---|
| Strategy | Goals |
| Maintain a steady expansion pace while sustaining robust profitability from the past three years | ☆ Robust profitability: Keeping operating margin in the 5% range<br>☆ Targeted growth rate: Roughly 10% annually |

Source: Prepared by FISCO from Company materials

In 1H FY6/19, it posted 5.1% segment operating margin, as explained above, realizing the 5% goal. Just as in the engineering field, rise in the average dispatching price contributed substantially to profitability. Since it is not easy to revise the dispatching price with existing customers and this does not happen often, the Company worked to sustain profitability by recruiting higher-priced deals for new contracts.

The Company previously focused on increase in staffing volume and better operational efficiency as drivers of profit expansion, rather than raising the average fee, in manufacturing field. Rigorous application of locally-oriented hiring and sales activities was an important measures in accomplishing this.

Locally-oriented hiring and sales are core elements of the Company’s business model. While this stance has not changed, the Company leveraged growing tightness for manufacturing staff in regions near major metropolitan areas to recruit projects with a higher dispatching price in 1H.

While recruiting personnel is an important aspect of the growth strategy in manufacturing field too, it needs to be controlled more precisely in the engineering field because of greater susceptibility to economic shifts. At the start of FY6/19, the Company presented its target to increase manufacturing technicians to 2,900 by the end of June 2019. This includes mid-career hires to join during the fiscal year and 200 new university graduate hires to join from April 2019. However, the number of manufacturing technicians decreased in the past year; 2,466 at the end of June 2018, 2,378 at the end of September 2018, and 2,351 at the end of December 2018. The Company still expects to add 200 new university graduates in April 2019 as planned, but might not attain the initial target of 2,900 technicians at the end of June 2019.

As seen above, while the manufacturing field is sustaining profitability, the top-priority issue, in accordance with the strategy of achieving stable growth with priority on profitability, it is becoming tougher to reach the second goal of growth in business scale (10% net sales growth). We advise against taking an adverse view of this outcome and instead recommend a positive reaction to adherence to the growth strategy's primary goal of emphasis on profitability and demonstration of the Company's robust adaptability to changes in the business environment.

## Healthy progress at the three UK firms with a policy of profit emphasis, entered staffing business in Vietnam too following China in Asia

### 4. Medium-term growth strategy and progress in the overseas field

In the overseas field, the Company rapidly expanded with the purchase of UK-based MTrec in August 2016 and successive acquisitions of UK staffing firms. The top priority in this process has been conducting management with emphasis on profits in the overseas field. While the Company's M&A deals in the UK appears to be proceeding in line with expectations, there is still considerable room for improvement in profitability compared to the domestic manufacturing field. We think this point led to awareness of the need for management that emphasizes profits.

In Asia, an immature market, meanwhile, the Company has ramped up from zero through establishment of subsidiaries and joint ventures. The current medium-term plan describes a "transition of the business stage from laying seeds to sprouting" and targets initiatives with strong profit awareness, just as in advanced countries. While the Company operates staff introduction and staffing businesses in Asia, staffing business clearly offers larger business potential. It assessed situations in Asian markets through low-risk staff introduction business thus far. However, we think it is planning to proceed in full-fledged rollouts with staffing business.

**Strategy and goals in the mid-term plan for the overseas field**

| Overseas field | |
|---|---|
| Strategy | Goals |
| ☆ Pursuing growth with emphasis on earnings underpinned by UK business that expanded to ¥30bn in sales over the past three years<br>☆ Businesses in the Asian market are transitioning from "laying seeds" to "sprouting" | |

Source: Prepared by FISCO from Company materials

MTrec is implementing structural reforms in FY6/19. With its location in northeastern England, Mtrec has many customers in the automotive industry and these customers tend to be large. Currently, meanwhile, it is widening to other industries, including foods, home electronics, and logistics and shifting to mid-sized and smaller projects. We think the company is aiming to stabilize profits and break up risks through expansions of customer industries and in the number of customers. We expect its performance to bottom out in FY6/19 and recover to higher sales and profits from FY6/20.

GAP is making healthy progress with sales and profit increases and appears to be outpacing the internal plan. While GAP acquired Quattro Group as a subsidiary in August 2018, both companies mainly provide services to the food industry and are capable of having a complementary relationship with GAP based in western England and Quattro Group in eastern England. Quattro Group seems to be performing well, similar to GAP.

We believe MTrec has the highest operating margin among the three UK firms because of its numerous automotive industry customers that pay the most expensive dispatching price in the manufacturing sector. However, even MTrec is only achieving about 4% operating margin, a weaker level than the domestic manufacturing field's margin in the 5% range. The Company intends to promote measure to improve this point.

**List of subsidiaries in the UK**

| Name | MTrec Limited | 1998 Holdings Limited | Quattro Group Holdings Limited |
|---|---|---|---|
| Main business subsidiaries | - | GAP Personnel Holdings Ltd. | Quattro Recruitment Ltd. |
| Founded | March 2006 | June 1998 | January 2010 (company establishment date) |
| Location | Newcastle upon Tyne, United Kingdom | Wrexham, United Kingdom | Norwich, United Kingdom |
| Fiscal year | March | March | May |
| Business performance* | Net sales: £44.9mn<br>Profit before tax: £2.3mn | Net sales: £133.0mn<br>Profit before tax: £2.6mn | Net sales: £43.6mn<br>Profit before tax: £1.4mn |
| Number of employees | Approx. 50 | Approx. 230 | (-) |
| Number of dispatched staff | Approx. 3,000 | Approx. 7,000 | (-) |
| Share purchase date | August 30, 2016 | December 1, 2017 | August 31,02018 |
| Share purchase ratio | 85% | 75% | 75% |
| Acquisition costs (one-time) | ¥160mn (FY6/17) | ¥230mn (FY6/18) | ¥70mn (FY6/19) |
| Goodwill | Approx. ¥1,400mn | Approx. ¥2,500mn | (-) |
| Depreciation period | 10 years | 10 years | (-) |

Note: Results are FY3/16 for MTrec, FY3/17 for GAP, and FY5/18 for Quattro; values taken from disclosed materials
Source: Prepared by FISCO from Company materials

In Asia, the Company runs a Japan-style staffing business in China through two venture companies. Japan-style staffing business is gradually making inroads locally, and results appear to be steadily advancing with this trend. Profitability has taken hold at the earlier Shandong joint venture, and the Guangdong joint venture has been ramping up its business too since the latter half of 2018.

As a recent new initiative, the Company purchased a 44.42% stake in LAI, which owns one of Vietnam's top staffing firms Le & Associates (L&A). L&A is a leading staffing firm in Vietnam with annual sales of just over ¥4bn. Meanwhile, the Company itself aggressively hires Vietnamese engineers in Japan. It is widely known that Vietnam is growing in importance as an Asian destination for Japanese companies. We think the Company is aiming for synergies with L&A in a variety of areas, including expansion of transactions with Japanese companies located in Vietnam and personnel interaction between the Company's headquarters and L&A.

# Business outlook

## Upbeat trends continuing in all three segments in 2H FY6/19 too, though the Company is also carefully monitoring Brexit and US-China trade friction impacts

For FY6/19, Trust Tech has kept the initial forecast unchanged projecting significant increase in sales and profits, with net sales at ¥82,000mn (up 25.5% YoY), operating profit at ¥6,000mn (up 39.6%), ordinary profit at ¥5,900mn (up 39.5%), profit attributable to owners of parent at ¥3,700mn (up 44.0%) , and EBITDA at ¥7,048 mn (up 32.3%) in FY6/19.

Overview of the FY6/19 outlook

(¥mn)

| | FY6/18 | | | FY6/19 | | | | |
|---|---|---|---|---|---|---|---|---|
| | 1H | 2H | Full year | 1H results | 2H forecast | YoY | Full-year forecast | YoY |
| Net sales | 29,676 | 35,687 | 65,363 | 40,246 | 41,754 | 17.0% | 82,000 | 25.5% |
| Operating profit | 2,210 | 2,086 | 4,297 | 3,112 | 2,888 | 38.4% | 6,000 | 39.6% |
| (Operating profit margin) | 7.4% | 5.8% | 6.6% | 7.7% | 6.9% | - | 7.3% | - |
| Ordinary profit | 2,201 | 2,027 | 4,228 | 3,079 | 2,821 | 39.1% | 5,900 | 39.5% |
| Profit attributable to owners of parent | 1,312 | 1,256 | 2,569 | 2,000 | 1,700 | 35.3% | 3,700 | 44.0% |
| EBITDA | 2,803 | 2,529 | 5,332 | 3,673 | 3,375 | 33.5% | 7,048 | 32.2% |

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

Despite very healthy advances in 1H results, as explained above, the Company is taking a conservative stance for 2H results based on uncertainty about prospects for economic and other conditions and kept the initial forecast unchanged for FY6/19. As a result, the Company expects ¥41,754mn in net sales (+17.0% YoY), ¥2,888mn in operating profit (+38.4%), ¥2,821mn in ordinary profit (+39.1%), and ¥1,700mn in profit attributable to owners of parent (+35.3%) for 2H FY6/19.

We think the conservative stance toward 2H is very reasonable. There is already evidence of impacts from US-China trade friction in a variety of industries in Japan. In the overseas field, the UK, which is the Company's main market, is about to leave the EU (Brexit). As media and other reports indicate that Brexit could cause various disruptions, we believe it is natural to be wary of what might happen.

The Company sustained upbeat momentum in all three segments (two domestic businesses and overseas business) through 1H. Manpower shortages at domestic development and manufacturing sites constitute a structural issue, and we expect firm needs to secure human resources, even with some economic fluctuation in the engineering field. Additionally, in the overseas field, the Company is shifting from large customers to mid-sized ones and broadening customer industries with aims of spreading out risk and bolstering profit stability. We see a good chance of the Company attaining FY6/19 targets even with impacts from changes in the external environment, such as US-China trade friction and Brexit.

### Breakdown by business segments

(¥mn)

| | | FY6/18 | | | FY6/19 | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | 1H | 2H | Full year | 1H | YoY | 2H forecast | YoY | Full-year forecast | YoY |
| Net sales | Engineering field | 16,069 | 17,504 | 33,573 | 19,875 | 23.7% | 21,355 | 22.0% | 41,230 | 22.8% |
| | Manufacturing field | 4,918 | 4,984 | 9,902 | 5,105 | 3.8% | 5,895 | 18.3% | 11,000 | 11.1% |
| | Overseas field | 8,711 | 13,263 | 21,974 | 15,317 | 75.8% | 14,513 | 9.4% | 29,830 | 35.7% |
| | Other | 30 | 39 | 69 | 51 | 69.8% | 27 | -30.5% | 78 | 12.7% |
| | Net sales prior to adjustment (total) | 29,729 | 35,790 | 65,519 | 40,349 | 35.7% | 41,789 | 16.8% | 82,138 | 25.4% |
| | Adjustment | -53 | -103 | -156 | -103 | - | -35 | - | -138 | - |
| | Net sales (total) | 29,676 | 35,687 | 65,363 | 40,246 | 35.6% | 41,754 | 17.0% | 82,000 | 25.5% |
| EBITDA | Engineering field | 2,281 | 2,115 | 4,396 | 3,011 | 32.0% | 2,862 | 35.3% | 5,873 | 33.6% |
| | Manufacturing field | 254 | 282 | 536 | 266 | 4.9% | 296 | 5.0% | 562 | 4.9% |
| | Overseas field | 311 | 165 | 476 | 432 | 39.0% | 299 | 81.2% | 731 | 53.6% |
| | Other | -57 | -74 | -131 | -72 | - | -172 | - | -244 | - |
| | EBITDA prior to adjustment (total) | 2,790 | 2,487 | 5,277 | 3,637 | 30.4% | 3,286 | 32.1% | 6,923 | 31.2% |
| | Adjustment | 13 | 41 | 54 | 35 | 156.2% | 90 | 119.5% | 125 | 131.5% |
| | EBITDA (total) | 2,803 | 2,529 | 5,332 | 3,673 | 31.0% | 3,375 | 33.5% | 7,048 | 32.2% |

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

### Simplified income statement and key indicators

(¥mn)

| | FY6/15 | FY6/16 | FY6/17 | FY6/18 | FY6/19 | |
|---|---|---|---|---|---|---|
| | | | | | 1H | Full-year forecast |
| Net sales | 20,819 | 30,143 | 43,035 | 65,363 | 40,246 | 82,000 |
| YoY | 18.0% | 44.8% | 42.8% | 51.9% | 35.6% | 25.5% |
| Gross profit | 4,868 | 7,192 | 9,344 | 13,302 | 8,583 | - |
| Sales ratio | 23.4% | 23.9% | 21.7% | 20.4% | 21.3% | - |
| SG&A expenses | 3,271 | 4,643 | 6,124 | 9,005 | 5,471 | - |
| Sales ratio | 15.7% | 15.4% | 14.2% | 13.8% | 13.6% | - |
| Operating profit | 1,597 | 2,549 | 3,220 | 4,297 | 3,112 | 6,000 |
| YoY | 23.7% | 59.6% | 26.3% | 33.4% | 40.8% | 39.6% |
| Operating margin | 7.7% | 8.5% | 7.5% | 6.6% | 7.7% | 7.3% |
| Ordinary profit | 1,623 | 2,528 | 3,185 | 4,228 | 3,079 | 5,900 |
| YoY | 23.1% | 55.8% | 26.0% | 32.7% | 39.9% | 39.5% |
| Profit attributable to owners of parent | 1,024 | 1,523 | 1,923 | 2,569 | 2,000 | 3,700 |
| YoY | 28.5% | 48.7% | 26.3% | 33.5% | 52.4% | 44.0% |
| EPS after the stock split (¥) | 53.39 | 78.91 | 99.17 | 128.63 | 94.43 | 174.70 |
| Dividend after the stock split (¥) | 30.00 | 40.00 | 45.00 | 55.00 | 30.00 | 70.00 |
| BPS after the stock split (¥) | 228.22 | 274.80 | 339.37 | 641.30 | - | - |

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

### Simplified balance sheet

(¥mn)

| | As of June 30, 2015 | As of June 30, 2016 | As of June 30, 2017 | As of June 30, 2018 | As of December 31, 2019 |
|---|---|---|---|---|---|
| Current assets | 6,551 | 8,984 | 11,999 | 20,190 | 21,816 |
| Cash and deposits | 3,038 | 3,930 | 4,581 | 9,410 | 9,509 |
| Notes and accounts receivable - trade | 2,954 | 4,060 | 6,245 | 10,045 | 11,426 |
| Non-current assets | 1,174 | 2,929 | 4,805 | 7,936 | 8,186 |
| Property, plant and equipment | 221 | 256 | 427 | 595 | 635 |
| Intangible assets | 130 | 2,202 | 3,845 | 5,960 | 6,514 |
| Investment and other assets | 821 | 471 | 532 | 1,380 | 1,037 |
| Total assets | 7,725 | 11,914 | 16,805 | 28,127 | 30,003 |
| Current liabilities | 3,287 | 6,531 | 7,641 | 12,405 | 12,943 |
| Accrued expenses | 1,754 | 2,394 | 3,031 | 4,208 | 3,649 |
| Short-term loans payable | - | 1,900 | 1,571 | 2,641 | 3,167 |
| Non-current liabilities | 31 | 60 | 2,466 | 2,005 | 2,008 |
| Long-term loans payable | - | - | 2,306 | 1,810 | 1,562 |
| Shareholders' equity | 4,409 | 5,323 | 6,520 | 13,385 | 14,620 |
| Capital stock | 1,529 | 1,538 | 1,562 | 4,199 | 4,213 |
| Capital surplus | 687 | 696 | 720 | 3,356 | 3,318 |
| Retained earnings | 2,193 | 3,089 | 4,238 | 5,830 | 7,089 |
| Accumulated other comprehensive income | -3 | -5 | 74 | 196 | 214 |
| Net assets | 4,406 | 5,322 | 6,697 | 13,715 | 15,052 |
| Total liabilities and net assets | 7,725 | 11,914 | 16,805 | 28,127 | 30,003 |

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

### Cash flow statement

(¥mn)

| | FY6/15 | FY6/16 | FY6/17 | FY6/18 | 1H FY6/19 |
|---|---|---|---|---|---|
| Cash flows from operating activities | 1,209 | 1,418 | 2,274 | 5,144 | 986 |
| Cash flows from investing activities | -147 | -1,807 | -2,395 | -2,720 | -321 |
| Cash flows from financing activities | -459 | 1,287 | 764 | 2,415 | -553 |
| Effect of exchange rate change on cash and cash equivalents | 6 | -6 | 8 | -10 | -12 |
| Net increase (decrease) in cash and cash equivalents | 609 | 892 | 651 | 4,829 | 99 |
| Cash and cash equivalents at beginning of period | 2,429 | 3,038 | 3,930 | 4,581 | 9,410 |
| Cash and cash equivalents at end of period | 3,038 | 3,930 | 4,581 | 9,410 | 9,509 |

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

# Shareholder returns

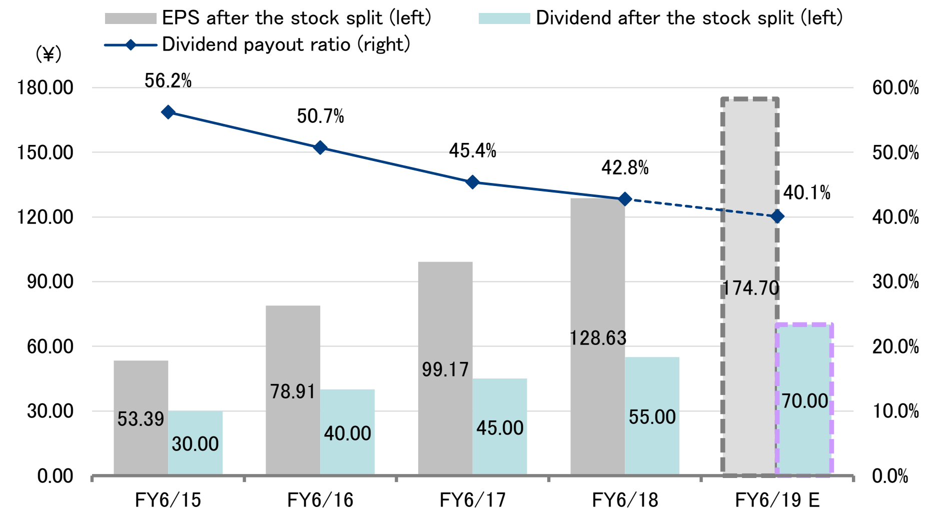
## In FY6/19, plans to increase the dividend by ¥15 YoY to ¥70. Dividend increase for the seventh consecutive year

Trust Tech sees shareholder returns as an important management issue and is mainly focusing on dividends. It places emphasis on stability in setting the dividend value, but also intends to have the dividend reflect earnings while securing internal retention in order to fund expansion of business scope and improvements in the income structure.

The Company announced a ¥70 dividend for FY6/19, an increase of ¥15 YoY, at the start of the fiscal year (¥30 interim and ¥40 period-end dividends). It retained this stance after 1H results. This puts dividend payout ratio at 40.1% based on estimated EPS of ¥174.70.

While the dividend payout ratio has been declining annually compared to the past level, we believe the Company demonstrate strong awareness of shareholder compensation in light of dividend hikes in seven straight years (after adjusting for share splits), multiple growth investment projects with overseas acquisitions and additions to domestic personnel, and three share splits in the past eight years.

Earnings per share, dividend, and dividend payout ratio




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

## Disclaimer