COMPANY RESEARCH AND ANALYSIS REPORT

Wacom Co., Ltd.

6727

Tokyo Stock Exchange First Section

19-Jun.-2018

FISCO Ltd. Analyst
Hiroyuki Asakawa

FISCO

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

Index

Summary

The new medium-term business plan was announced in the presence of new President Ide
Aiming for an operating profit margin of 10% on net sales over the ¥100bn mark through an earnings-driven growth strategy centered on customer-oriented technological leadership

Wacom Co., Ltd. <6727> (hereafter, also "the Company") is the world's leading manufacturer of pen tablets. It possesses a global share of 80- 90% of the market of creators and hobbyists. Its two main businesses are the Brand Business, selling its own-brand pen tablet products, and the Technology Solution Business, which consists of the supply of digital pen components to manufacturers of finished products, including tablets.

1. Operating profit increased substantially in FY3/18 and achieved a V-shaped recovery

In the FY3/18 results, net sales were ¥82,262mn (up 15.4% year on year (YoY)) and operating profit was ¥3,526mn (compared a loss of ¥1,171mn in the same period in the previous fiscal year), so sales increased considerably on the previous fiscal year and the operating loss became an operating profit. Both sales and profits were also above the revised forecasts announced in November 2017. In the fiscal period under review, profits increased greatly in Q2 due to the effects of new products in the Brand Business and the expansion of component sales in the Technology Solution Business, and this trend continued in the 2H to achieve the above-stated sales and profits. Looking at the results in more detail, we see that in the Brand Business, sales and profits were less than forecast due to the slump in sales of some products, but that this was covered by the growth in the results of the Technology Solution Business. In that sense, the results still have points to reflect upon and to be addressed in the future, but first of all, the Company should be positively evaluated for achieving a V-shaped recovery of sales and profits.

2. Aiming for an operating profit margin of 10% on net sales of ¥100bn in FY3/22

On April 1, 2018, President and Representative Director Nobutaka Ide was additionally appointed CEO. Since it was announced that Mr. Ide had been appointed President in October of last year, he has been working to formulate a new growth strategy, and recently the Company announced Wacom Chapter 2 as its new medium-term business plan. This plan sets out the following three points as the overall strategy; 1) advancing Technology Leadership, 2) close collaboration between Island & Ocean businesses, and 3) Extreme Focus in selection and concentration. In terms of the specific measures based on these strategies, the Company is working on measures including customer-oriented technological innovation, operational reforms, and establishment of a financial structure that prioritizes profitability. It has not announced numerical results targets for each fiscal year of the plan, but for the final fiscal year of FY3/22, it has set three management targets, of an operating profit margin of 10%, net sales of ¥100bn, and ROE of 15% to 20%.

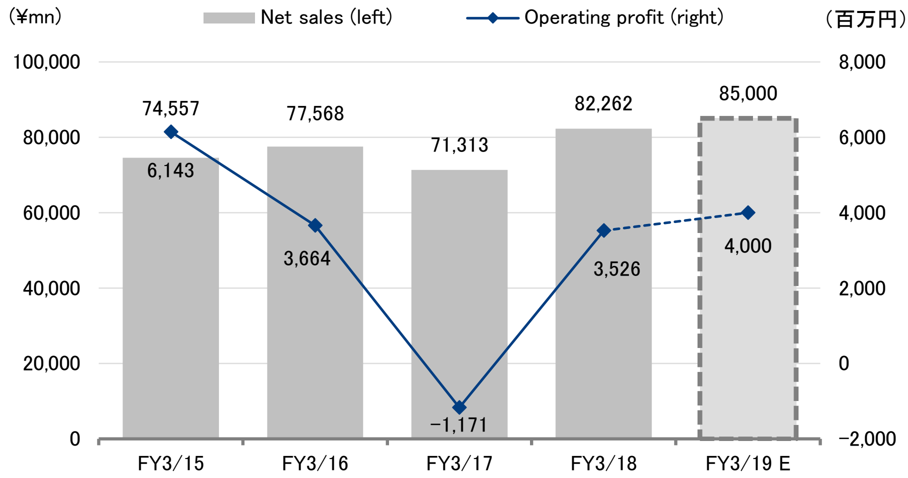
3. The focus for FY3/19 will be on to what extent can the Company accumulate results above its baseline forecasts of the Technology Solution Business

For FY3/19, the Company is forecasting higher sales and profits, of net sales of ¥85,000mn (up 3.3% YoY) and operating profit of ¥4,000mn (up 13.4%). FY3/19 is the first fiscal year of the new medium-term business plan, so it is an important year as the launch pad toward achieving the plan's management targets. The Company has indicated that the numerical results forecasts for the Technology Solution Business in FY3/19 are the "baseline." This means that they are the minimum amounts that should be achieved, and its real intention is to aim for results that exceed these forecasts. At FISCO, we think that this change in stance toward creating results forecasts is evidence that the Company is escaping from its previous own-goal structure, which is as we expected, and we shall be paying attention to further developments.

Key Points

- The overall strategy in the new medium-term business plan is on the three axes of Technology Leadership, Island & Ocean, and Extreme Focus
- Is tacking four high-priority issues, including "customer-oriented technological innovation"
- Aiming for net sales of ¥100bn that would enable an operating profit margin of 10% in FY3/22

Result trends



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

Company profile

Established in 1983, the Company has grown steadily with technology and now holds a share over 80% of the global market for pen tablets for creators

1. History

The Company was established in 1983 in Ageo City, Saitama Prefecture. Its name derived from "world" and "computer," while "WA" includes the meaning of "harmony between people and computers" ("WA" being the Japanese word for harmony). In 1984, it announced the world's first battery-less and cordless pen tablet. In 1987, it launched the SD Series of graphic pen tablets for professionals, which were used by the Walt Disney Company in the United States for film production. Subsequently, it constantly enhanced its products, and in the creative pen tablets markets for creators and hobbyists, since the 2000s it has consistently kept a global share of 80% and above.

In 2002, it entered into the pen sensor components field (currently, the Technology Solution Business). This business involves supply of components and modules, such as the Company's digital pens, control IC and sensor boards, to the manufacturers of finished products. As it is described in more detail below, the business is growing rapidly on the back of the expansions of the markets for tablets and smartphones.

In the securities market, after listing on the Japan Securities Dealers Association's JASDAQ market in April 2003, the Company listed on the Tokyo Stock Exchange (TSE) First Section in December 2005, where it remains today.

History

July 1983	Founded in Ageo City, Saitama Prefecture. Launched an electronic devices business (currently, the Brand Business) and an ECS business (currently, the engineering solutions business).
1984	Announced the creation of the world's first battery-less and cordless pen tablets, the WT series
1987	Announced the development of the world's first graphics tablets for professionals, the SD series
July 1990	Completed the Toyonodai plant in Kazo City, Saitama Prefecture
1990	U.S. Walt Disney Company produced "Beauty and the Beast" using Wacom pen tablets
September 1998	Announced the Intuos (now Wacom Intuos Pro) series of pen tablets for professionals
November 1999	Announced the creation of pen tablets for general consumers, the Graphire/FAVO (now Wacom Intuos)
September 2001	Announced the development of the Cintiq (now Wacom Cintiq Pro) series of pen tablets with liquid crystal displays
April 2002	Entered into the pen sensor components field (currently, the Technology Solution Business)
April 2003	Listed on the Japan Securities Dealers Association's JASDAQ market
December 2005	Listed on the TSE First Section
October 2008	Developed a high-performance multi-touch sensor system
May 2011	Announced the creation of the Bamboo stylus for use with the iPad
October 2011	Samsung Electronics began using Wacom's digital pen input system in its smartphones
September 2013	Announced the development of the Cintiq Companion (now Wacom MobileStudio Pro) mobile product incorporating an operating system
February 2014	Launched WILL™ digital ink technology
March 2014	Announced the development of active ES™ (electrostatic) coupling technology applicable to digital pens
April 2014	Cumulative production of pen input components for mobile devices reached 100 million units
April 2015	Revamped global organization
September 2015	Announced the development of the Company's first digital stationery, Bamboo Spark (now Bamboo Smartpad)
September 2016	Established the Digital Stationery Consortium
June 2017	Announced Bamboo Ink, a new stylus product for Windows Ink compliant with Microsoft pen protocol
December 2017	Transferred the Engineering Solution Business to Nitto Denko Corporation
May 2018	Announced Wacom Chapter 2, the new medium-term business plan

Source: Prepared by FISCO

The two business pillars are sales of own-brand finished products and the supply of parts for equipment

2. The business units and the main products

The Company's products are devices for computer interface called "pen tablets." While it is possible to utilize the commonly used mouse to draw pictures and write text, as the accuracy of the pointing when using it is low, it is difficult to draw a line exactly as intended. This is Wacom's products come in. When using a digital pen tablet (the name is derived from stone tablets) known together as a pen tablet, it becomes possible to input pictures and text simply and accurately.

The biggest feature of the pen tablet is that it is accurate and highly precise. Depending on the product, some are able to detect the pen pressure and the inclination of the pen and thereby express the touch of the pen on the tablet screen more delicately. Utilizing such features, the pen tablet is used for creating designs, illustrations, graphics, and other such works on a computer.

The Company has two business units: Brand Business and Technology Solution Business. The Brand Business consists of WACOM brand products, such as pen tablet finished products and pens, for creative users, like creators and hobbyists, to general consumers, as well as enterprise users. The Technology Solution Business involves supply of the Company's pen tablet components (including digital pens, sensors, and control IC) to the manufacturers of tablets and smartphones. The Company was also in charge of Other Businesses coming from CAD systems for electronic design, which was referred to as the Engineering Solution Business, but this business was transferred on December 1, 2017. (Results for eight months have contributed to the financial statements for FY3/18.)

In the Brand Business, the Company has a wide lineup of products by target customer and product type. Products are divided into the Creative Business for creative users, the Consumer Business for general consumers, and Business Solutions for corporations. In the Creative Business, which is the core business in terms of the sizes of sales and profits, there are three product types: Pen tablets, Displays, and Mobiles. Understanding their differences is important to understanding aspects such as the competitive environment and the products' future potential.

Pen tablets, which are the most basic type of input device, are comprised of a pen and a tablet screen. The same as a mouse or a keyboard, they are used by connecting them to a PC. As they have a simple configuration, they come in a wide lineup, ranging from products for professionals to beginners.

Displays are similar to Mobiles in that the tablet screen is a liquid crystal display (LCD) tablets. So users can draw intuitively and directly on the screen using a digital pen. However, they are also similar to Pen tablets as they are input devices without an OS or memory device.

Mobiles entail integrating a pen tablet and a tablet PC so that users can draw with a digital pen onto a liquid crystal screen and save the data input into the device as it is. As the user inputs using a digital pen, the method of use is the same as that of a general tablet PC. However, the Company's mobile products use a dedicated input pen and their performance is overwhelmingly higher, and ultimately they are not PCs. Therefore, it is considered that they are not fundamentally in competition with PCs for high-end creative users. On the other hand, competitive relations can be seen for users at levels below this, and so-called cannibalism does occur for the Company.

Overview of the Business units and the main products

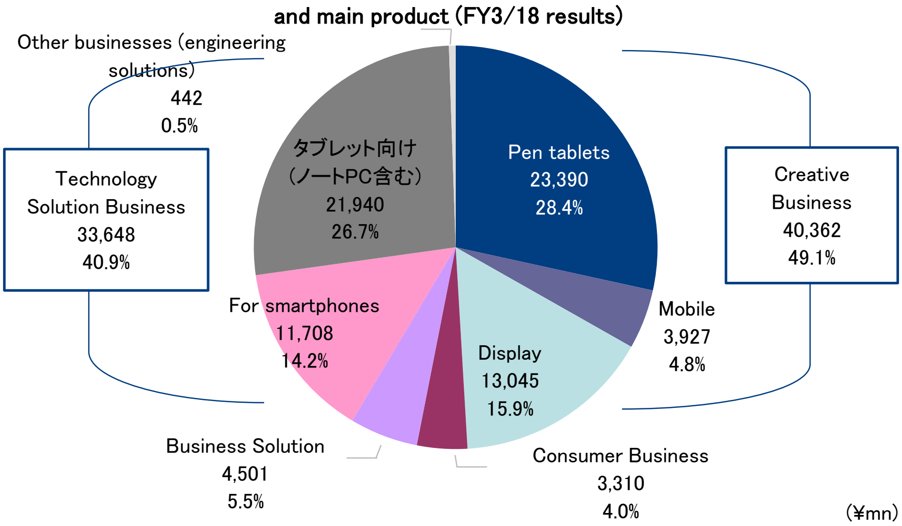
Business classification	Product classification	Main products	Product description	Intended use	Product series
Brand Business	Creative Business		"Supporting creative users expressing their passion"	-	-
		Pen tablets	Pen tablets for professionals that make possible extremely delicate drawing, such as from a pressure-sensitive pen, and pen tablets for general users that can be used via simple operations	Graphic design using computer graphics, film and animation production, photo editing, industrial design, illustrations, creation of homepages, etc.	Wacom Intuos Pro series, Intuos series
		Displays	users to draw and write text directly on an LCD screen		Wacom Cintiq Pro series, Cintiq series
		Mobiles	LCD pen tablets for professionals that enable		Wacom MobileStudio Pro series
	Consumer Business	Styluses, digital stationery	Digital stationery makes everyone's life more creative		Bamboo Series
	Business Solution	Pen tablets for businesses	Business-use products that enable users to draw and write text directly on an LCD screen	Used in the digital signature , education, and medical fields	STU Series DT Series
Technology Solution Business		Digital pens, sensors, touch panel components, and modules	-	For use in mobile devices, such as tablets, digital books, and cellular telecommunications equipment	-
	-	For smartphones	-	Pen sensor systems for smartphones	-
		For tablets	-	Pen sensor systems for tablet PCs and notebook PCs	-
Other	-	Digital design use CAD systems	-	Used in the manufacturing industry (for mechatronics)	-

Source: Prepared by FISCO from Company materials

The breakdown of business classification, product classification, and main products is in the graph. In FY3/18, the Brand Business supplied 58.6% of the Company's total net sales, the Technology Solution Business provided 40.9%, and Other Businesses accounted for 0.5%. Sales in the Brand Business are mainly from the Creative Business with 46% of whole. This business is divided into three by product and Pen tablets, and Displays are particularly large proportion.

The Technology Solution Business, which involves the supply of parts for equipment, contributed 41% of sales in FY3/18 results. A feature of this business is that customer companies' product strategies and sales trends cause results to vary greatly. There are two product categories according to usage: smartphones and tablet PCs (including notebook PCs).

Breakdown of net sales by business classification, product classification, and main product (FY3/18 results)



Source: Prepared by FISCO from Company materials

The Company sells worldwide through global subsidiaries Overseas sales comprise about 90% of its total consolidated net sales

3. Sales situations

The Company has established subsidiaries in regions throughout the world, starting with Wacom Computer Systems in 1988 (currently, Wacom Europe), up to Wacom India in 2010. It sells its brand products through these subsidiaries.

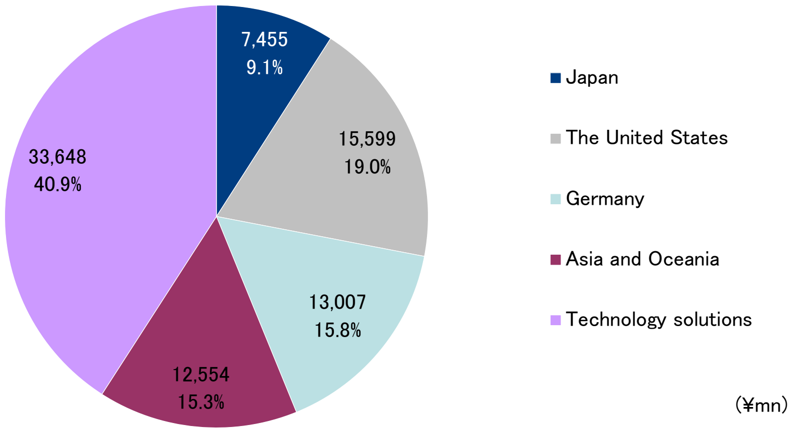
History of Establishment of Subsidiaries

April 1988	Established Wacom Computer Systems (now, Wacom Europe), in Neuss, Germany
July 1991	Established Wacom Technology in Vancouver, US
March 2000	Established Wacom China in Beijing, China
April 2004	Established Wacom Digital Solutions (currently, Wacom Korea) in Seoul, South Korea
April 2005	Established Wacom Australia Pty. Ltd. in North Ryde, Australia
April 2006	Established Wacom Hong Kong in Hong Kong
May 2006	Established Wacom Singapore in Singapore
September 2008	Established Wacom Taiwan Information in Taiwan
August 2010	Established Wacom Technology Services in Vancouver, the United States
October 2010	Established Wacom India Pvt. Ltd. in New Delhi, India

Source: Prepared by FISCO from Company materials

For its internal management purpose, the Company tabulates and publishes net sales for the Technology Solution Business under Japan in its official disclosure of "Sales by Regional Subsidiary". Therefore, only the Brand Business publishes results by country and region. Most of the sales by the Technology Solution Business are made overseas. Thus, about 90% of the Company's total consolidated net sales are made overseas, and these overseas sales are affected by fluctuations in exchange rates.

Net sales conditions by region (FY3/18 results)



Source: Prepared by FISCO from Company materials

With regards to the effects of exchange rates, it is necessary to be aware that their effects on net sales and operating profit differ depending on the currency (the yen rates against the US dollar and the euro). A weak yen is beneficial for net sales both against the dollar and the euro. Conversely, for profits (operating profit), a strong yen is beneficial (and a weak yen disadvantageous) against the dollar as the overseas production rate is high, at 98%, and production costs are US dollar denominated. Against the euro, a weak yen is beneficial (a weak yen is disadvantageous) for profits, the same as for sales. The Company also conducts production and sales activities in the Asia region, but as the currencies of Asian countries are basically linked to the US dollar, we can consider that the fluctuations in the US dollar apply to these currencies. So in terms of the effects on sales and profits, a weak yen against these currencies is beneficial for both sales and profits.

Approach to the exchange rate effects amounts

Currency	Fluctuation direction	Impact on net sales	Impact on operating profit	Remark
USD	Weak JPY	Increased sales	Reduced profit	Overseas production costs are calculated in USD so the weaker JPY results in higher procurement costs and decreases operating profit
EUR	Weak JPY	Increased sales	Reduced profit	Exposure only through sales, which is frankly a benefit of a weaker JPY
Asian currencies	Weak JPY	Increased sales	Reduced profit	Asian currencies are tied to the USD in many cases High-priority issues

Source: Prepared by FISCO

98% of the Company's products are manufactured outside Japan However, the Company supplies the equipment for production, thereby preventing the leakage of its technology and know-how

4. The manufacturing formation

Although the Company has a plant at its headquarters in Kazo City, Saitama Prefecture, it is basically a fabless company. It plans, develops, and designs products and components and outsources production to OEM and ODM in Japan and overseas. Many of these plants are located in mainland China, but from the perspective of mitigating country risk, it also utilizes EMS (electronic manufacturing services) centered on Taiwanese and Japanese capital. In terms of production ratio whether inside or outside Japan, the percentage from outside Japan is overwhelmingly larger, at approximately 98%, with the remainder being produced at the headquarters plant and by outsourcers in Japan.

The Company is a fabless company, but the structure is that it develops and designs in-house the manufacturing equipment used on the production lines, manufactures the manufacturing equipment under the company's control, and then this equipment is installed in the plants of its outsourcers, which carry out the production. Through this method, the Company aims to both utilize inexpensive labor costs from production outside Japan and to black box its technologies and expertise to prevent them flowing out of the Group.

Results trends

Achieved a V-shaped recovery in profits in FY3/18 from the contribution of new products and the spur of component supply for tablet players

1. FY3/18 results

For FY3/18, the Company posted a 15.4% YoY rise in net sales to ¥82,262mn, an operating profit of ¥3,526mn, reversing the operating loss of ¥1,171mn, an ordinary profit of ¥3,584mn, reversing the ordinary loss of ¥870mn, and a net profit attributable to owners of the parent of ¥2,361mn, reversing the net loss of ¥5,534mn.

On November 1, 2017, the Company announced its revised full fiscal year forecasts. In the end, sales and profits both exceeded these revised forecasts, by approximately 2% for net sales and approximately 20% for operating profit.

The FY3/18 results, which achieved a V-shaped recovery, appear to be positive at first glance, but they cannot necessarily be given a perfect score. This is because, as is explained below, sales and profits in the Brand Business, which the Company expected to recover, did not reach their forecasts. It seems that the Company itself is aware that this is an important issue toward recovering growth momentum from FY3/19 onwards.

Summary of FY3/18 results

(¥mn)

	FY3/17			FY3/18						
	1H	2H	Full fiscal year	1H	2H	Initial forcast	Revised forcast	Full fiscal year	YoY growth rate	% Revised forcast
Net sales	33,797	37,517	71,313	40,689	41,573	76,800	80,900	82,262	15.4%	1.7%
Gross profit	13,240	14,324	27,565	15,703	16,056	-	-	31,759	15.2%	-
SG&A expenses	14,138	14,598	28,736	14,202	14,031	-	-	28,233	-1.8%	-
Operating profit	-898	-273	-1,171	1,501	2,025	1,800	2,900	3,526	-	21.6%
Operating profit margin	-2.7%	-0.7%	-1.6%	3.7%	4.9%	2.3%	3.6%	4.3%	-	
Recurring profit	-1,021	150	-870	1,641	1,942	1,740	3,100	3,584	-	15.6%
Profit attributable to owners of parent YoY	-1,226	-4,308	-5,534	1,673	688	1,130	1,930	2,361	-	22.4%

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

During the1H of the fiscal year under review, profits recovered and a so-called V-shaped recovery was achieved. The 2H started with the forecasts unchanged from the 1H, but in the end, the results in the 2H trended above the forecasts, and the forecasts were exceeded for the full fiscal year. However, the results differed according to the business segment, with the Brand Business failing to achieve both its sales and profits forecasts in the 2H, and these shortfalls being absorbed by the acquisition of orders for front-loaded projects from FY3/19 in the Technology Solution Business.

In the Brand Business, FY3/18 began with all new products having been launched. In the pen tablet and digital pen markets, the Company is firmly maintaining its competitive advantages for brand power, products, and technologies. In this situation, the delays in the releases of new products in FY3/17 meant consumers refrained from purchases, leading to the worsening of results. But in FY3/18, such trends were wiped away and segment sales increased by 9.8% YoY.

In the Technology Solution Business, net sales grew significantly due to the increase in adoption of the Company's digital pens for tablets and notebook PCs. For smartphones, mass production shipments for Samsung Electronics' Galaxy Note8 trended steadily, but declined for the other products in the Note Series, and therefore net sales declined. As a result of the above, segment net sales increased 25.8% YoY, driven by the growth in sales for tablets and PCs.

Details by business segment

(¥mn)

		FY3/17			FY3/18					
							Full fiscal year			
		1H	2H	Full fiscal year	1H	2H	Initial forcast	Revised forcast	Results	YoY growth rate
Net sales	Brand Business	19,326	24,547	43,873	22,442	25,730	49,200	49,000	48,173	9.8%
	Technology Solution Business	14,141	12,615	26,757	17,902	15,745	26,900	31,450	33,647	25.8%
	Other	327	354	682	344	97	700	450	441	-35.2%
	Subtotal	33,796	37,517	71,313	40,689	41,573	76,800	80,900	82,262	15.4%
	Adjusted amount	0	0	0	0	0	0	0	0	-
	Net sales total	33,796	37,517	71,313	40,689	41,573	76,800	80,900	82,262	15.4%
Operating profit	Brand Business	2,051	3,633	5,684	2,549	3,920	8,100	7,660	6,469	13.8%
	Technology Solution Business	1,788	655	2,443	3,531	2,146	2,260	3,900	5,677	132.4%
	Other	-13	-19	-32	-38	-26	40	-50	-65	-
	Subtotal	3,826	4,269	8,095	6,041	6,040	10,400	11,510	12,082	49.2%
	Adjusted amount	-4,724	-4,542	-9,266	-4,540	-4,014	-8,600	-8,610	-8,555	-
	Operating profit total	-897	-273	-1,171	1,501	2,025	1,800	2,900	3,526	401.1%

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

The two points for profits are the effects of exchange rates and SG&A expenses

Exchange rates were a factor causing profits to decline in FY3/17, and the rates in the fiscal period under review were ¥110.81 to the US dollar and ¥129.45 to the euro, which meant the yen weakened by 1.6% (¥1.78) and 8.4% (¥10.08) respectively compared to FY3/17. As previously explained, a weak yen against the dollar is disadvantageous for profits, so the weakening of the yen caused profits to decline ¥80mn. But as a weak yen against the euro is advantageous for profits, it caused profits to increase ¥550mn. A weak yen is beneficial with regards to Asian currencies also, and profits increased ¥310mn as a result. Therefore, the overall effect of exchange rates was to increase profits ¥780mn.

Exchange rate effect amount (FY3/18 results)

Currency	Changes in exchange rates	Net sales	Operating profit
1 US dollar	¥1.78 weak yen	+¥800mn	-¥80mn
1 euro	¥10.08 weak yen	+¥1,010mn	+¥550mn
Asian currencies, total (Numbers in parentheses: Chinese yuan)	(¥0.54weak yen)	+¥470mn (+¥200mn)	+¥310mn (+¥130mn)
Total		+¥2,280mn	+¥780mn

Source: From the Company's results briefing materials

SG&A expenses decreased by 1.8% (¥503mn), from ¥28,736mn in the previous fiscal year to ¥28,233mn. Although personnel expenses increased, other expenses decreased, including sales promotion expenses, advertising and publicity expenses, outsourcing expenses, and depreciation expenses. The majority of the rest of the increase was a provision for a bad-debt loss following the collapse of a North American sales agency, and there was only a slight increase on excluding this.

The effect of exchange rates on SG&A expenses (the amount of increase due to the weakening of the yen against the dollar and the euro) was approximately ¥760mn. This exchange rate effect amount combined with the above described provision for a bad-debt loss was a total of around ¥1bn. So therefore in the fiscal period under review, in actuality the Company was able to reduce SG&A expenses by ¥1.5bn compared to the previous fiscal year.

Breakdown of SG&A expenses

(¥mn)

	FY3/17	FY3/18	YOY	
			Change	YoY growth rate
Personnel expenses	9,656	9,795	139	1.4%
R & D expenses	4,397	4,385	-12	-0.3%
Promotion · Advertisement cost	3,581	3,261	-320	-8.9%
Outsourcing cost	2,746	2,353	-393	-14.3%
Depreciation cost	1,558	1,321	-237	-15.2%
Other	6,799	7,118	319	4.7%
SG&A expenses total	28,736	28,233	-503	-1.8%
SG & A expenses ratio	40.3%	34.3%	-	-

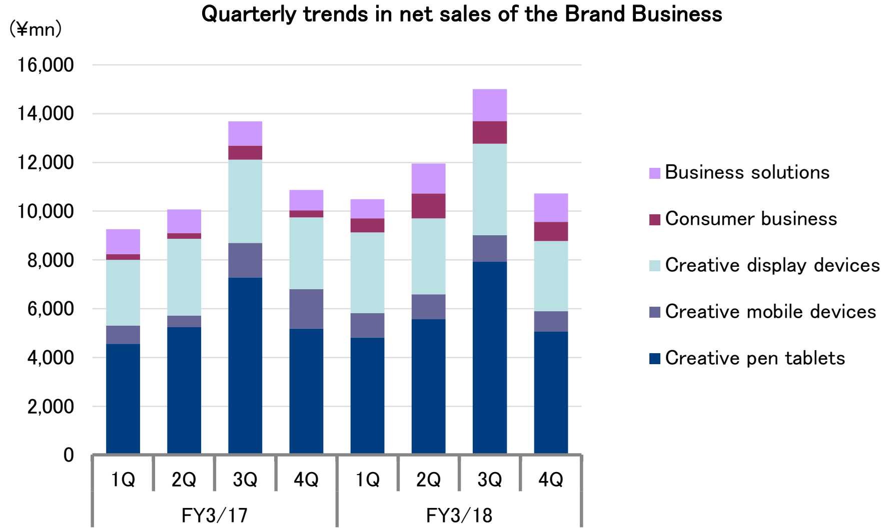
Source: Prepared by FISCO from the Company's results briefing materials

Sales and profits both increased YOY, but each failed to reach their forecasts due to an unexpected decrease in sales of Creative mobile products

2.Quarterly trends in net sales of the Brand Business

In the Brand Business, sales and profits increased, with net sales of ¥48,173mn (up 9.8% YoY) and operating profit of ¥6,469mn (up 13.8%). However, both were below their forecasts (the revised forecasts announced in November 2017, same below), net sales by 1.7% and operating profit by 15.5%.

Quarterly trends in net sales of the Brand Business



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

In the core creative business, net sales were ¥40,362mn, up 4.2% YoY but 1.9% below their forecast. The details by product are as follows.

(1) Pen tablets

Net sales were ¥23,390mn, up 5.0% YoY but 1.9% below the forecast. The reason why net sales were below the forecast was the slump in sales of Intuos Pro for professionals. New products were released in FY3/17, but the momentum was not sustained and sales in FY3/18 declined YoY. At FISCO, we think that rather than due to competition with other companies, this was due to the shift within the Company to Mobiles and Displays. The slump in sales for professionals was absorbed by the growth in sales of Intuos for consumers and in models for emerging countries, and a YoY increase in sales was secured. In sales for consumers, the Company launched new products in March 2018 at the end of the fiscal period, and they made strong starts and contributed to results in the fiscal year under review (although their fully fledged contributions will be in FY3/19). In sales for emerging countries, the Company continued to acquire new users in China and elsewhere, and the number of shipments increased about 20% YoY.

(2) Displays

Net sales were ¥13,045mn, up 6.7% YoY and 2.4% above the forecast. Sales increased significantly of both models of the new product of Wacom Cintiq Pro 13/16, which absorbed the decline from existing models and pushed-up segment net sales. The Company is advancing the development of the large-sized new product Wacom Cintiq Pro 24/32, but due to a development delay, only the 24-inch size was launched at the end of March 2018. The fully fledged contributions to sales and profits of the large sizes, including the 32-inch model, are expected in FY3/19.

(3) Mobiles

Net sales were ¥3,927mn, down 7.5% YoY and 13.9% below the forecast. Mobile devices are products in which a pen tablet and tablet PC are integrated, so in terms of usability, they are the same as general tablets that use digital pens for the input device. Therefore, the Company's mobile devices and the tablet products of other companies are in competition, depending on the user. The Company's mobile devices are ultimately positioned as input-only devices and are characterized by their high functionality, so there is no competition in the market for high function models for professional creators and they are able to maintain their competitive advantages. However, for other users, it would seem that the Company's Mobile are losing out to the competition. In FY3/17, it launched Wacom MobileStudio Pro 13/16, but in FY3/18 it entered the second half of its life cycle, which led to a decline in sales.

(4) Consumer Business

Net sales increased 150.6% YoY to ¥3,310mn largely due to sales growth of the Bamboo Ink stylus, which it jointly developed with Microsoft <MSFT>, mainly in North America. Also, sales of Bamboo Slate and Bamboo Folio, which are digital stationary products launched in September 2016, secured the same level of sales and profits as the previous year.

(5) Business Solution

Net sales were ¥4,501mn, up 17.9% YoY. In the business field, competition is continuing with general mobile devices, such as tablets, mainly in Europe so the fiscal year under review started with some concerns, including about a decline in sales as a reaction to the large-scale projects acquired from Indian public institutions in the previous fiscal year. However, sales grew and increased significantly YoY, as liquid crystal pen tablets were adopted by North American financial institutions. Also, the Wacom Clipboard new product, which was released in June 2018, uncovered new BtoB needs through a function that instantaneously digitizes the content that is filled-in on various types of forms, and sales grew.

Sales in the Brand Business by product line

(¥mn)

	FY3/17			FY3/18						
	1H	2H	Full fiscal year	1H	2H	Initial forcast	Revised forcast	Full fiscal year	YoY growth rate	% Revised forcast
Brand Business	19,327	24,547	43,874	22,442	25,731	49,200	49,000	48,173	9.8%	-1.7%
Creative Business	16,876	21,861	38,737	18,821	21,541	43,370	41,150	40,362	4.2%	-1.9%
Pen tablets	9,794	12,473	22,267	10,394	12,996	23,430	23,850	23,390	5.0%	-1.9%
Displays	5,858	6,365	12,223	6,412	6,633	14,140	12,740	13,045	6.7%	2.4%
Mobiles	1,224	3,023	4,247	2,015	1,912	5,800	4,560	3,927	-7.5%	-13.9%
Consumer Business	465	856	1,321	1,606	1,704	1,730	3,470	3,310	150.6%	-4.6%
Business Solution	1,986	1,830	3,816	2,015	2,486	4,100	4,380	4,501	17.9%	2.8%
Operating profit	2,051	3,634	5,685	2,549	3,921	8,100	7,660	6,470	13.8%	-15.5%
Operating profit margin	10.6%	14.8%	13.0%	11.4%	15.2%	16.5%	15.6%	13.4%	-	-

Source: Prepared by FISCO from Company materials

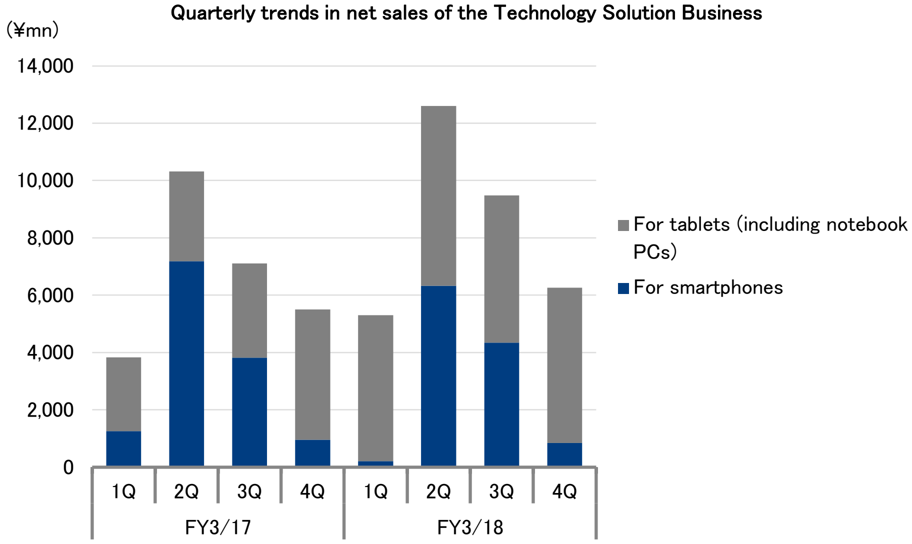
In the Brand Business segment in FY3/18, although a YoY increase in sales was secured, categories that failed to achieve forecasts could be seen here and there. On analyzing the reason for this, it seems that even among new products, the market response to highly functional models is better. So in this sense, at FISCO we think that the Company's products are able to maintain their customers' brand loyalty and competitive advantages. On the other hand, we feel it is possible that the negative aspect of the delay in the development of large-size Displays, which invited the slump in results in FY3/17, will drag on as before. We think that the greatest point to focus on in FY3/18 is whether it was able to completely resolve this issue at an early stage, and we shall be watching carefully for developments from FY3/19 and beyond.

Sales for tablets and notebook PCs grew, pushing-up segment sales and profits

3. Trends in the Technology Solution Business

In the Technology Solution Business, both sales and profits increased significantly, with net sales of ¥33,648mn (up 25.8% YoY) and operating profit of ¥5,678mn (up 132.4%). Both also exceeded their forecasts, net sales by 7.0% and operating profit by 45.6%.

Quarterly trends in net sales of the Technology Solution Business



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

Products in the Technology Solution Business are divided into for smartphones and for tablets and notebook PCs (from FY3/18, the total for notebook PCs has been included in for tablets). Within the products, sales for smartphones declined 11.4% YoY to ¥11,708mn and were also 7.3% below the forecast. In this business, the Company supplies the pen and the sensor system for Samsung Electronics' Galaxy Note series. In FY3/18, there were hardly any sales in Q1 from the effects of the stall in sales of Galaxy Note7 in the 2H of the previous year. From the July to September period, the supply for the Galaxy Note8 started and sales got back on a recovery track, but this was not enough to compensate for the slump in Q1, so sales declined YoY. Moreover, sales were apparently below the forecast mainly for Galaxy Note8.

Net sales for tablets and notebook PCs were ¥21,940mn, up 61.9% YoY and 16.6% above the forecast. The Company conducts an OEM supply of active ES (AES) digital pens to tablet and notebook PC manufacturers, and their adoption of new models increased and net sales grew significantly. In the background to this is the fact that the positioning of the digital pen among tablet manufacturers is changing to an awareness that “it is a device essential to increase marketability.” In addition, business discussions scheduled for FY3/19 were pushed forward to the fiscal period under review, which also led to the results exceeding the forecasts.

In terms of product type, EMR (electromagnetic resonance) and Active ES (AES, electrostatic). In FY3/18, sales of models equipped with an AES system pen increased, but EMR system sales also steadily grew for the education market, including for Google’s Chromebook.

Sales in the Technology Solution Business by product line

(¥mn)

	FY3/17			FY3/18						
	1H	2H	Full fiscal year	1H	2H	Initial forcast	Revised forcast	Full fiscal year	YoY growth rate	% Revised forcast
Technology Solution Business	14,142	12,616	26,758	17,902	15,746	26,900	31,450	33,647	25.8%	7.0%
For smartphones	8,435	4,773	13,208	6,529	5,179	11,000	12,630	11,708	-11.4%	-7.3%
For tablets (including notebook PCs)	5,707	7,843	13,550	11,373	10,567	15,900	18,820	21,940	61.9%	16.6%
Operating profit	1,788	655	2,443	3,531	2,147	2,260	3,900	5,677	132.4%	45.6%
Operating profit margin	12.6%	5.2%	9.1%	19.7%	13.6%	8.4%	12.4%	16.9%	-	-

Note: The YoY growth rate for tablet PCs in FY3/18 compares the total figure for tablet PCs and notebook PCs from the previous fiscal year.
Source: Prepared by FISCO from Company materials

At FISCO, we honestly evaluate the FY3/18 results in the Technology Solution Business to be positive. The Company itself is taking a cautious stance because orders were received ahead of schedule as stated above (including a decline in FY3/19 as a reaction to the previous strong results). But there is no doubt that a situation in which the change in the market trend to “digital pens are indispensable for tablets” is expected to continue in the future is a positive one for the Company. Going forward, based on the fact that the tablet products of the various companies to which the Company supplies digital pens compete with the Mobiles in the Brand Business, we shall be focusing on how it achieves a balance in terms of the growth of sales and profits between the Brand Business and the Technology Solution Business.

Medium- to long-term growth strategy: Wacom Chapter 2, the new medium-term business plan

Implemented on the three axes of Technology Leadership, Island & Ocean, and Extreme Focus

1. Outline of Wacom Chapter 2, the new medium-term business plan

Since the past, the Company has aimed to realize medium- to long-term growth through formulating and implementing a medium-term business plan. Mr. Nobutaka Ide, who was announced in October 2017 of appointment to Representative Director, President and CEO, took office in April 2018, however since the announcement he has been working to formulate a new growth strategy. As a result, in May of this year the Company announced Wacom Chapter 2 (FY3/19 to FY3/22) as its new medium-term business plan.

The title of the new medium-term business plan, Chapter 2, indicates that it is a continuation of Chapter 1, which was the progress made up to March 2018 under the Company's management vision of "for a creative world" (a world alive with creativity).

Based on this, new President Ide included the new concept of "Life-long Ink" in the new medium-term business plan. The point here is "Ink," which signifies digital ink. At FISCO, our understanding is that the Company is appealing to delivering the best digital ink experiences throughout their lifetime will become newly synonymous with the technologies that it is focusing on the most.

The Company-wide strategy described in Wacom Chapter 2 is comprised of three axes; 1) Technology Leadership, 2) Island & Ocean, and 3) Extreme Focus. This Company-wide strategy can be said to be the code of conduct or the standards for implementing the new medium-term business plan.

Technology Leadership means aiming to continue to provide customers with technological innovations and to differentiate itself through technologies. Since the past, the Company has strongly focused on technologies, but this current strategy is distinctive on two points. The first point is the emphasis on technologies for customers, as symbolized by phrases such as "journeys with customers," "dialogues with customers," and "relationships with customers." The second point is incorporating the appeal from the value of "hand written and hand drawn" into "technological innovation." The former can be taken as a given, but the latter can also be said to be a very important viewpoint when considering the characteristics of pen tablets. The Company is aiming to realize technological innovation from these two viewpoints and to solidify its position as the leader in its current business domains.

Island & Ocean expresses the Company's Branded Business (Island) and Technology Business (Ocean). Both of these two businesses have different missions. The Branded Business provides users with final products under the Wacom brand. Here, the aim is to offer customers the best possible experience through uncovering and meeting their needs technologically or functionally. On the other hand, in the Technology Business, the goal is to provide the Company's technologies to outside third parties, and with them as the partners, to make its digital pen and digital ink technologies the de-facto standard. Therefore, it pursues the development of technologies that allows it to be selected as a partner and for which the Company itself does not become buried in a relationship with a huge customer company. The point of the Island & Ocean strategy is to aim for growth by having both these businesses, which have different missions, collaborate closely, while pursuing synergies. The Company can be said to be taking this strategy as an attempt to create a new business domain not bound by existing business fields by not referring to either the Brand Business or Technology Solution Business and calling them the Branded Business and Technology Business to heighten collaboration between the two business fields.

Extreme Focus signifies "extreme selection and concentration." President Ide has stated that the Company will "carry out extreme selection and concentration in all areas and for all operations." This strategy seems to have emerged from a reflection on the past, in which the expansion of the product lineup and technological development above the Company's optimal size (such as its corporate size and human resources) invited a deterioration of business results. In light of the Company's current size, it is considered indispensable that it conducts focused business development and invests in talented human resources. Even though the matter is under consideration, the current situation would seem to be that it has not yet decided on the specifics, for example such as whether it should focus on the level of a business unit, a product lineup, or SKU (inventory management)). It seems that it will make a decision while observing the conditions in the business development in the future. Conversely, it has already started partially moving toward concentration and strengthening. The Company integrated the departments that are related to digital ink and established the Ink Division. It seems that the aim of this is to increase efficiency and development speed by consolidating into a single division the work relating to digital ink that was previously conducted by multiple departments and rigorously select and concentrate to further heighten customer-oriented operations. Going forward, it is expected that this development will gradually grow throughout the entire Company.

Is tacking four high-priority issues, including "customer-oriented technological innovation"

2. Specific measures and results outlook

In terms of the specific measures based on the previously described Company-wide strategy, the Company has set four high-priority issues.

High-priority issues

4 high-priority issues
Customer-oriented technological innovation
Organization/operational reforms
Solid financial structure securing profitability
Enhancement of management quality through BOD* reform

*BOD: Board of Directors
Source: Prepared by FISCO from Company materials

(1) Customer-oriented technological innovation

One of the direct causes of the deterioration of results in FY3/17 was the slump in the Brand Business. In the background to this cause was the fact that product planning and product development exceeded the Company's capacity and it was unable to pursue customer satisfaction. It recognizes that these points are management issues it has to address, and up to the present time it has been implementing improvement measures.

Going forward, in accordance with the framework of the above-mentioned Technology Leadership, the Company will incorporate (commercialize) technological innovation into specific brand products and pursue growth. It has not yet clarified the details, but it is considered that digital ink will occupy a major position in the Company's technological appeal in the future. In terms of the direction of the evolution of digital ink, one suggestion is products that utilize the integration of VR (Virtual Realty) and MR (Mixed Reality).

As previously stated, the partner strategy serves as the framework for the Technology Solution Business; namely, expanding the Company's pen tablet technologies through partnering with major PC and tablet manufacturers. It has placed the central axis of its growth strategy for the future on the opening-up of new markets, and in terms of the specific markets, the assumptions include the spread in the use of digital pens in the education field, the opening-up of the digital stationary market, and cooperation with AI.

(2) Organization/Operational reforms

The Company is also working on organizational restructuring as part of its measures to resolve issues. It has set two key objectives, focusing on customers and simplifying the organizational structure, and it is working to realize them. Up to the present time, it has integrated the digital ink-related departments and established the Ink Division, and in addition its measures include establishing the CTO office, reviewing the product development process and restructuring toward customer support that is attributable to each business. Through this organizational restructuring, the Company will accelerate the resolution of issues, including those relating to technological innovation, development methods, CRM (customer management) and quality improvements.

(3) Solid financial structure securing profitability

From the viewpoint of profitability, what the Company will tackle first is optimizing SG&A expenses. It has set the specific target of keeping down the ratio of SG&A expenses to net sales to the minimum level of the last 10 years. The minimum value in the last 10 years was 26.7% in FY3/13, so it seems that this will be the standard going forward.

What is important is not the absolute amount of SG&A expenses, but ultimately its ratio to net sales. In order for the Company to realize its goal of Technology Leadership, it has declared that it will maintain its active investment in research and development. On the other hand, its policy for the other departments is to thoroughly achieve productivity improvement and cost reductions and aim to expand net sales as the ratio denominator, and thereby reduce the ratio of SG&A expenses to net sales.

(4) Enhancement of management quality through BOD* reform

* BOD: Board of Directors

To improve the quality of management, President Ide considers that it is indispensable to have a structure in place to make management decisions through full discussions by the Board of Directors, rather than relying on individuals. A Board of Directors that can have high quality strategic discussions as a technology company is precisely the type of Board of Directors that President Ide considers to be ideal.

The Company has cited three viewpoints for the reorganization; selecting people who can conduct strategic discussions, ensuring that the size of the Board of Directors is appropriate, and appointing outside directors to secure fairness and transparency. The Board of Directors is expected to be reorganized in accordance with this framework.

At FISCO, our understanding is that the action items (1) to (4) described above and their content are only those have been started at the present time or hypothetical examples. It can be said that these four items are a frank reflection of the circumstances that the Company was forced into for the previous medium-term business plan, of having to pull back after making a start, and it expresses its intentions that first of all each of the existing issues will be resolved one by one. Therefore, it is estimated that the specific contents of these "high-priority issues" and the items themselves will change alongside the progress made in the future.

Aiming for an operating profit margin of 10% on net sales of ¥100bn in FY3/22

3. The medium-term business plan's financial targets

The Company has set the following financial targets in Wacom Chapter 2 for the plan's final fiscal year of FY3/22; an operating profit margin of 10%, net sales of ¥100bn, and consolidated ROE of 15% to 20%.

The Wacom Chapter 2 numerical targets

(¥mn)

	FY3/18	FY3/19	FY3/22	
			Forecast	CAGR
Net sales	82,262	85,000	100,000	5%
Brand Business	48,173	50,300	60,400	6%
Technology Solution Business	33,647	34,700	39,600	4%
Operating profit	3,526	4,000	10,000	-
Operating profit margin	4.3%	4.7%	10.0%	-
Profit attributable to owners of parent YoY	2,361	2,980	6,948	-
ROE	10.8%	13%	15-20%	-
Capital adequacy ratio	44.5%	-	60%	-

Source: Prepared by FISCO from the Company's Medium–term business plan briefing materials

Breaking down net sales by business segment, the targets are ¥60,400mn for the Brand Business and ¥39,600mn for the Technology Solution Business. These are 4 year average annual growth rates of 6% and 4%, respectively. The reason why the annual average growth rate of the Technology Solution Business is lower would seem to be that it is highly uncertain and lacking in transparency due to the strong degree of importance of the partner strategy. In terms of the Company's true intentions, at FISCO we estimate that it actually assumes a high rate of growth for it that may surpass that of the Brand Business.

The fact that the Company is maintaining a target ROE in the range of 15% to 20% would seem to be because it is adopting a capital policy that considers ROE in the relative relation with the cost of shareholders' equity. Naturally, it is aiming for "ROE>cost of shareholders' equity," but it has not clarified a specific level for the cost of shareholders' equity.

With regards to returns to shareholders, this partially overlaps with the description in the Returns to Shareholders section. But based on dividends, the Company is also considering paying special dividends and flexibly acquiring treasury shares. On that basis, its policy is to stably grow (increase) dividends and as a supplementary indicator, it is aiming for a dividend payout ratio of 30%.

Business outlook

Forecasts are for higher sales and profits, driven by the growth in sales and profits for the Brand Business

● Company forecasts for FY3/19

For FY3/19, the Company forecasts a 3.3% YoY rise in net sales to ¥85,000mn, an operating profit of ¥4,000mn, a 13.4% rise YoY, ordinary profit of ¥3,920mn, a 9.4% rise and a net profit attributable to owners of the parent of ¥2,980mn, a 26.2% rise YoY.

Outlook of company forecasts for FY3/19

(¥mn)

	FY3/18			FY3/19					
	1H	2H	Full fiscal year	1H forecast	YoY growth rate	2H forecast	YoY growth rate	Full year forecast	YoY growth rate
Net sales	40,689	41,573	82,262	41,330	1.6%	43,670	5.0%	85,000	3.3%
Gross profit	15,703	16,056	31,759	-	-	-	-	-	-
SG&A expenses	14,202	14,031	28,233	-	-	-	-	-	-
Operating profit	1,501	2,025	3,526	830	-44.7%	3,170	56.5%	4,000	13.4%
Operating profit margin	3.7%	4.9%	4.3%	2.0%	-	7.3%	-	4.7%	-
Recurring profit	1,641	1,942	3,584	670	-59.2%	3,250	67.3%	3,920	9.4%
Profit attributable to owners of parent YoY	1,673	688	2,361	660	-60.6%	2,320	237.2%	2,980	26.2%

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

At FISCO, we think that on a Company-wide basis, the net sales and profits forecasts are sufficiently persuasive. However, looking at the breakdown by segment, the impression is that the outlook for profits in the Brand Business is too bullish on the point that it assumes that the operating profit margin will improve greatly. In contrast, the forecasts for the Technology Solution Business are extremely conservative, and, as recognized by the Company itself, they incorporate only the demand that is visible at the present time. In the breakdown by segment, although it is possible that the results may diverge from the Company forecasts, overall our opinion at the current point in time is that the results will be probably be in line with these forecasts.

The details by business segment are as follows.

Forecasts by business segment

(¥mn)

		FY3/18				FY3/18	
				Full fiscal year		Full fiscal year	
		1H	2H	Results	YoY growth rate	Initial forcast	YoY growth rate
Net sales	Brand Business	22,442	25,730	48,173	9.8%	50,300	4.4%
	Technology Solution Business	17,902	15,745	33,647	25.8%	34,700	3.1%
	Other	344	97	441	-35.2%	0	
	Subtotal	40,689	41,573	82,262	15.4%	85,000	3.3%
	Adjusted amount	0	0	0	-	0	
	Net sales total	40,689	41,573	82,262	15.4%	85,000	3.3%
Operating profit	Brand Business	2,549	3,920	6,469	13.8%	9,700	49.9%
	Technology Solution Business	3,531	2,146	5,677	132.4%	2,590	-54.4%
	Other	-38	-26	-65	-	0	
	Subtotal	6,041	6,040	12,082	49.2%	12,290	1.7%
	Adjusted amount	-4,540	-4,014	-8,555	-	-8,290	
	Operating profit total	1,501	2,025	3,526	401.1%	4,000	13.4%

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

In the Brand Business, the forecasts are net sales of ¥50,300mn (up 4.4% YoY) and operating profit of ¥9,700mn (up 49.9%). The driving force behind the higher sales is expected to be the increase of 7.1% YoY for mainstay products in the Creative Business. In contrast to this, the forecast for the Consumer Business is a decrease of 20.2%. This would seem to be a reaction to the fact that this business overachieved in FY3/18. Within the Creative Business, on the one hand it is expected that sales of Pen tablets and Displays will both increase in emerging countries and that growth will be steady, including from the effects of new products. But on the other hand, it is forecast that sales of Mobiles will decline due to the intensification of competition with tablets, the same as in the previous fiscal year.

The reason for the forecast of a significant increase in operating profit is that the Company intends to raise the gross profit margin by improving the product mix and refraining in this fiscal period from the price cuts and related measures for existing models that it conducted in the previous fiscal period. The improvement to the product mix will be from the full contributions of the new products launched in the previous fiscal period and from the contributions of the new products scheduled to be launched in this fiscal period. In conjunction with the measures to keep down SG&A expenses described above, the forecast is that the operating profit margin will rise to 19.3%.

Sales forecast in the Brand Business by product line

(¥mn)

	FY3/18			FY3/19	
	1H	2H	Full fiscal year	Full fiscal year forcast	YoY growth rate
Brand Business	22,442	25,731	48,173	50,300	4.4%
Creative Business	18,821	21,541	40,362	43,240	7.1%
Pen tablets	10,394	12,996	23,390	25,050	7.1%
Displays	6,412	6,633	13,045	14,370	10.2%
Mobiles	2,015	1,912	3,927	3,820	-2.7%
Consumer Business	1,606	1,704	3,310	2,640	-20.2%
Business Solution	2,015	2,486	4,501	4,420	-1.8%
Operating profit	2,549	3,921	6,470	9,700	49.9%
Operating profit margin	11.4%	15.2%	13.4%	19.3%	-

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

In the Technology Solution Business, the forecasts are for sales to increase but for profits to decrease substantially, of net sales of ¥34,700mn (up 3.1% YoY) and operating profit of ¥2,590mn (down 54.4%). On considering the uncertainty in this business, the Company has set these forecasts to be the baseline (signifying the absolute minimum values that should be achieved). In reality, it plans to significantly increase sales for smartphones, and in addition, demand is expected to grow for tablets and notebook PCs, so it would seem to be aiming for results that exceed the above figures.

By end product, sales for smartphones are forecast to increase 25.1% YoY. The Company expects that shipments for Samsung Electronics' Galaxy Note8 will continue this year following its introduction into the market in the previous fiscal year, and that mass-market shipments of pen sensor systems for next-generation models forecast to be introduced this year can also be expected. In contrast to this, it forecasts that sales for tablets and PCs will decline 8.6% to ¥20,050mn. This is largely from the effect of considering the impact of the portion of orders that were pushed forward to the prior fiscal year, earlier than anticipated. The amounts from this effect are ¥1.5bn for net sales and ¥500mn for operating profit.

The reasons for the substantial decrease in operating profit is that, in addition to the amount from the effect of orders being pushed forward describe above, that costs to invest in technological development for the future will increase. The Company has budgeted for R&D costs in this fiscal period of ¥5,000mn (compared to ¥4,385mn in the previous fiscal period) on a Company-wide basis, and it is estimated that much of this YoY increase relates to the Technology Solution Business.

Sales forecast in the Technology Solution Business by product line

(¥mn)

	FY3/18			FY3/19	
	1H	2H	Full fiscal year	Full fiscal year forcast	YoY growth rate
Technology Solution Business	17,902	15,746	33,647	34,700	3.1%
For smartphones	6,529	5,179	11,708	14,650	25.1%
For tablets (including notebook PCs)	11,373	10,567	21,940	20,050	-8.6%
Operating profit	3,531	2,147	5,677	2,590	-54.4%
Operating profit margin	19.7%	13.6%	16.9%	7.5%	-

Note: The YoY growth rate for tablet PCs in FY3/18 compares the total figure for tablet PCs and notebook PCs from the previous fiscal year.
Source: Prepared by FISCO from the Company's financial results and the briefing materials

The profit statement and the main indicators

(¥mn)

	FY3/15	FY3/16	FY3/17	FY3/18	FY3/19 1H (F)	FY3/19 Full fiscal year (F)
Net sales	74,557	77,568	71,313	82,262	41,330	85,000
YoY	-5.2%	4.0%	-8.1%	15.4%	1.6%	3.3%
Gross profit	30,050	30,735	27,565	31,759	-	-
Gross margin	40.3%	39.6%	38.7%	38.6%	-	-
SG&A expenses	23,908	27,071	28,736	28,233	-	-
Ratio of SG&A expenses to net sales	32.1%	34.9%	40.3%	34.3%	-	-
Operating profit	6,142	3,664	-1,171	3,526	830	4,000
YoY	-29.1%	-40.3%	-	-	-44.7%	13.4%
Operating profit margin	8.2%	4.7%	-1.6%	4.3%	2.0%	4.7%
Recurring profit	6,064	3,776	-870	3,584	670	3,920
YoY	-26.8%	-37.7%	-	-	-59.2%	9.4%
Profit attributable to owners of parent	3,473	2,309	-5,534	2,361	660	2,980
YoY	-33.8%	-33.5%	-	-	-60.6%	26.2%
EPS after adjustment for share-split (¥)	20.86	14.00	-33.93	14.55	4.06	18.35
Dividends after adjustment for share-split (¥)	18.00	18.00	6.00	6.00	-	6.00
BPS after adjustment for share-split (¥)	202.14	188.22	130.75	139.45	-	-
Capital investment amount	4,082	4,862	3,580	1,513	-	2,300
Depreciation and amortization	1,970	2,004	2,573	2,421	-	2,600
R&D expenses	3,180	4,342	4,397	4,385	-	5,000

Source: Prepared by FISCO from the financial results summary

Balance Sheet

(¥mn)

	FY3/14	FY3/15	FY3/16	FY3/17	FY3/18
Current assets	40,073	40,187	37,873	39,499	42,588
Cash and deposits	15,393	16,686	14,365	14,204	19,157
Notes and accounts receivable	11,388	9,875	10,161	10,768	10,738
Inventories	9,329	10,216	10,097	10,097	9,719
other	3,963	3,411	3,250	4,877	2,975
Fixed assets	10,785	11,269	13,692	10,749	8,320
Tangible fixed assets	5,332	4,608	4,538	4,303	4,301
Intangible fixed assets	3,221	5,441	8,131	4,312	2,951
Investments and other assets	2,231	1,219	1,023	2,133	1,068
Total assets	50,859	51,456	51,566	50,249	50,909
Current liabilities	16,239	15,880	16,478	17,383	16,752
Accounts payable	9,429	9,203	6,102	7,481	7,100
Short-term debt	600	600	4,000	3,000	3,000
other	6,210	6,077	6,376	6,902	6,652
Fixed liabilities	1,820	1,717	3,991	11,508	11,488
Shareholders' equity	31,939	32,617	30,770	21,536	22,924
Capital	4,203	4,203	4,203	4,203	4,203
Capital surplus	7,563	7,550	7,513	6,098	6,098
Retained earnings	21,710	22,318	21,629	13,134	14,522
Treasury stock	-1,538	-1,455	-2,576	-1,900	-1,900
Total accumulated other comprehensive profit	713	1,061	188	-306	-280
Stock acquisition right	147	180	133	126	25
Net assets, total	32,799	33,858	31,096	21,356	22,668
Total liabilities and net assets	50,859	51,456	51,566	50,249	50,909

Source: Prepared by FISCO from the financial results summary

Cash Flow Statement

(¥mn)

	FY3/14	FY3/15	FY3/16	FY3/17	FY3/18
Cash flow from operating activities	733	6,782	2,009	121	6,781
Cash flow from investing activities	-4,415	-3,277	-4,878	-3,479	-767
Cash flow from financing activities	-3,255	-2,849	1,209	3,298	-974
Gain or loss on translation of foreign currency cash and deposits	735	637	-661	-100	-87
Change in cash and deposits balance	-6,202	1,292	-2,321	-160	4,952
Cash and deposits balance at start of fiscal year	21,596	15,393	16,686	14,365	14,204
Cash and deposits balance at end of fiscal year	15,393	16,686	14,365	14,204	19,157

Source: Prepared by FISCO from the financial results summary

Returns to shareholders

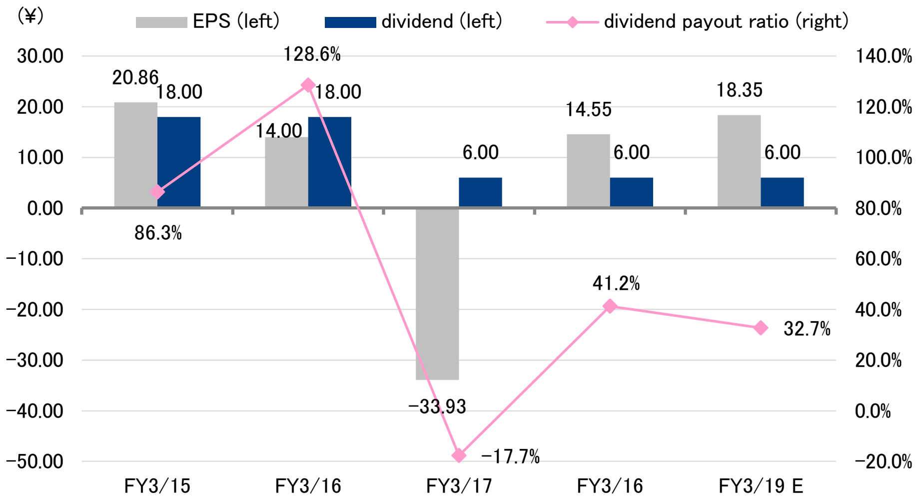
Plans a dividend of ¥6 in FY3/18

The Company's basic policy towards shareholder returns is to pay steady dividends based on its profits after considering the amount of funds to be retained for future business development and sound financial base. Management has made guidance of maintaining a dividend payout ratio of at around 40% in the past, but it lowered the target in FY3/18 to around 30%. Besides, to reduce the clerical cost of paying dividends, the Company pays them only once at the end of each fiscal year.

The Company will pay a dividend for FY3/18 in line with the previous dividend forecast of ¥6, which is unchanged from the previous fiscal year. The dividend payout ratio will be 41.2%. For FY3/19, it has announced a dividend forecast of ¥6, again unchanged YoY. Based on the forecast earnings per share, the dividend payout ratio will be 32.7%.

At FISCO, we think that the reasoning behind the fact that the Company has reduced the dividend payout ratio as the standard for dividends is convincing to a certain extent. It has announced Wacom Chapter 2 as its new medium-term business plan and clarified its growth strategy and targets for sales and profits in the future. In the plan, it has set a growth scenario based on the development of new products and the spread in the use of digital ink, and in the background to this scenario are its strong financial needs to invest in growth. As this investment domain is envisaged to carry with its considerable business risks, to provide financial support for the active pursuit of returns (ROE targets of 15-20%), the Company is aiming to supplement its retained earnings (about 60% of the capital adequacy ratio) by reducing the standard for the dividend payout ratio. We consider that the products the Company is creating and digital ink have high growth potential, and we expect that this investment of funds will contribute to maximizing returns to shareholders in the medium- to long-term.

Trends in EPS, dividend, and dividend payout ratio



Source: Prepared by FISCO from Company materials

Information security

In light of its business model, the risk of information leakages and related risks are low

The Company is highly aware of the need for information security, and it is responding to generally anticipated cyber-attacks and other such threats. Its technologies are highly applicable for uses in the future, such as for capturing big data. However, the Company itself will not be the actor that collects the big data and ultimately its stance is that it only provides the tools for this. In this sense, it can be said that the risks relating to the management and leakage of information are extremely low. Also, it is developing cloud-type services, but this development is being conducted overseas (outside of Japan) with global standard basis and it seems that it is also taking measures for information security with a higher awareness than general attitudes in Japan.

Disclaimer