COMPANY RESEARCH AND ANALYSIS REPORT

Wacom Co., Ltd.

6727

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Index

Summary

In FY3/21, sales and profits increased significantly to achieve record high earnings. Sales for online education expanded dramatically due to the coronavirus pandemic. Medium-term business plan targets were achieved one year early, and a new medium-term management direction announced

Wacom Co., Ltd. <6727> (hereafter, also “the Company”) is the global leading manufacturer aiming to create value for customers based on technologies in the field of digital pen and ink. It dominates in brand clout and market share supported by professional creators such as designers and animators who work in studios for movie production or industrial design studios. Its two business segments are the Branded Business, in which it sells its own-brand Displays (LCD pen tablets) and Pen Tablets and other products, and the Technology Solution Business, in which it supplies proprietary digital pen technology as a component to manufacturers of finished products, including smartphones and tablet PCs.

1. FY3/21 results

In the FY3/21 consolidated results, net sales increased 22.5% year on year (YoY) to ¥108,531mn and operating profit rose 140.8% to ¥13,407mn. Thus, sales and profits increased significantly, hitting new record-high results. The global spread of the novel coronavirus (hereinafter, the coronavirus pandemic) caused a rapid surge in demand for online education and teleworking. In response, the Company’s Branded Business, which mainly sells Displays and Pen Tablets, expanded dramatically. Furthermore, in the AES Technology Solution and EMR Technology Solution segments sales grew to manufacturers to which the Company is an OEM supplier against a backdrop of increasing usage in the tablet and notebook PC markets. In profit-loss, operating profit increased significantly due to the effects of higher sales, improvements in the product mix, and efforts to streamline costs, with the operating profit margin improving greatly to 12.4% (6.3% in the previous fiscal year).

2. FY3/22 results outlook

In its consolidated results forecasts for FY3/22, the Company is projecting net sales to decrease by 6.0% YoY to ¥102,000mn and operating profit to decrease by 18.0% to ¥11,000mn, reflecting uncertainty associated with the impact of the coronavirus pandemic and lower sales and income expected under the baseline scenario. Although online education demand is expected to continue increasing, the forecast for lower sales mainly reflects the risk of lower sales in some areas such as demand for individual home-use hobby applications, as well as consideration of a certain level of risk in key parts procurement. On the other hand, in profit-loss, while profits are expected to decrease due to pressure on earnings from lower sales and continued active R&D investment for the future, the Company expects to secure an operating income margin at a level above 10%.

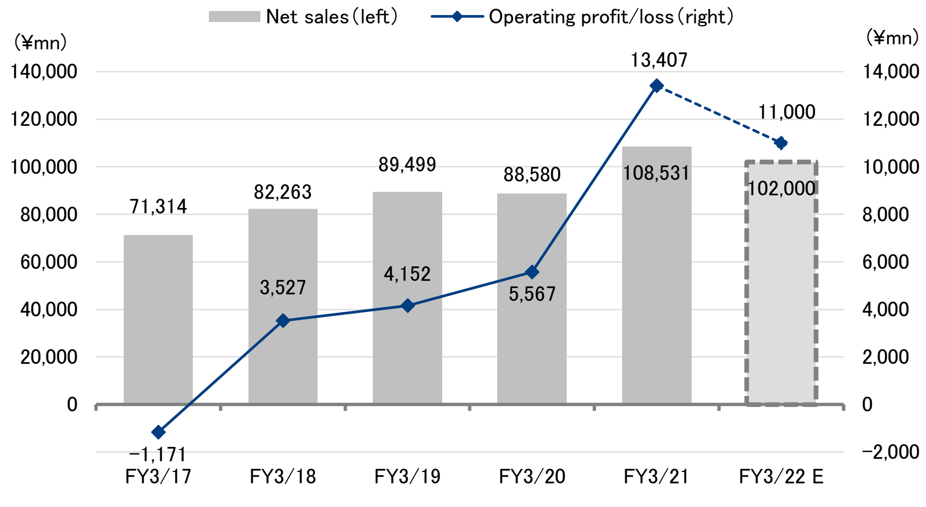
3. Growth strategy

The Company has been progressing "Wacom Chapter 2," its medium-term business plan formulated in FY3/19 and ending in FY3/22. However, having achieved the medium-term business plan targets one year early, the Company has announced a new medium-term business direction, "Wacom Chapter 3," (FY3/22 to FY3/25). The new direction will promote the specific value propositions and sustainable growth, inheriting the vision of "lifelong ink," and redefining five key strategic initiatives as well as six main streams for technology innovation for implementing the policy. In particular, the Company's leading strategy is to select three fields that have a high affinity with its existing technologies–AI, XR, and Security–and realize new value propositions in these fields using new technologies and business models. Taking the growth of existing businesses as a baseline and adding the impact of new core technologies and business models, the policy aims for double-digit growth.

Key Points

- Achieved record high earnings in FY3/21 atop significant growth in sales and profits
- Captured the demand for online education that grew in response to the coronavirus pandemic
- Despite projections for lower sales and profits under the baseline scenario for FY3/22, a high level of earnings is forecast to continue
- After early achievement of targets under medium-term business plan Wacom Chapter 2, the new medium-term business direction Wacom Chapter 3 was announced. Aiming for growth acceleration with the establishment of new core technologies and new business models

Results trends



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

Business overview

Global leader aiming to create value for customers based on technologies in the field of digital pen and ink

The Company is the world's leading company aiming to create value for customers based on technologies in the field of digital pen and ink. It sells products in more than 150 countries worldwide and dominates in brand clout and market share supported by professional creators such as designers and animators who work in studios for movie production or industrial design studios. Furthermore, as a Technology Leadership Company, it broadly supplies the latest digital pen technology to partner companies manufacturing smartphones, tablet PCs, digital stationery, and other products and is fostering a business field that specializes in education with partners from the educational industry.

The Company is also striving to create new growth opportunities by rebuilding product line-ups and further evolving the business model amid major changes in the market environment, including tougher competition in low- and mid-priced product categories and evolution of user needs and workflow, as well as the spread of online education and teleworking accompanying advances in digital technologies (IoT, VR/MR, AI, and others) and the communications environment (mobile, cloud, 5G, and others). In particular, although at the current time the coronavirus pandemic is having both positive and negative effects, the Company is entering the next growth phase by capturing new demand from the new normal.

Its two business segments are the Branded Business, which sells the Company's own-brand Displays, Pen Tablets and other products, and the Technology Solution Business, which supplies proprietary digital pen technology as a component to manufacturers of finished products, including smartphones and tablet PCs. The two businesses have formed a more or less balanced business composition in terms of net sales and operating profit for FY3/21.

With the overseas sales ratio (overseas local entity sales ratio excluding the Technology Solution Business) at about 86%*, careful attention should be given to the impact of foreign exchange market fluctuations on earnings (in particular, fluctuations in the euro-yen rate have a major impact on operating profit).

* Asia-Oceania sales at about 27.0%, (of which China at 13.0%), European sales (Germany) at about 30.0% and US sales at about 29.0%.

Additionally, while development sites are practically all concentrated in Japan, excluding developments of digital ink and security-related software (which are mainly in Europe), the Company consigns production to multiple overseas partners (which are mostly major electronics manufacturing service companies owned by either Japanese or Taiwanese with production bases in China). It plans to increasingly diversify production sites to Southeast Asia and other nearby areas from the standpoint of alleviating supply-chain concentration risk.

Business and major product features

Promoting updates in the product portfolio that address changes in the business environment and de facto standardization of proprietary technologies

1. Branded Business

The Company has a broad lineup for target customers and product types. It sorts products into two categories: (1) Creative Solution and (2) Business Solution*.

* In order to conduct a more appropriate results briefing through reflecting changes in the business environment, the Company changed aspects such as category ranges and names of business segments from FY3/21. Specifically, the previous three product categories of the Creative Business, the Consumer Business, and Business Solution were reduced to two, and the Creative Business was renamed Creative Solution. It also integrated the Consumer Business with Mobiles within Creative Solution.

(1) Creative Solution

This is the core business since the Company's founding and possesses strong brand clout and market share with professional creators. Product types include Displays, Pen Tablets and Mobiles, and understanding their differences is important in assessing the competition environment and growth potential.

a) Displays

This category covers products that use an LCD panel as the tablet* and are similar to Mobiles, which are explained below, in terms of directly writing on an LCD screen with a digital pen. Meanwhile, they are also PC peripherals, similar to Pen Tablets as an input device that does not have an OS or storage feature. Prices for larger products range from around ¥200,000 to ¥400,000. Users are mainly professionals and advanced amateurs, and the Company holds an overwhelming share in this market. In response to market changes (such as expanded scope and demand shift from Pen Tablets), it released multiple new models including a 16-inch entry model with an actual sales price in the ¥60,000 to 70,000 range (tax exclusive; same below) in January 2019, a 22-inch model (actual sales price in the ¥100,000 to 110,000 range) in July 2019, and a 13-inch model for beginners (actual sales price in the ¥30,000 to 40,000 range) in January 2020. The Company is steadily expanding results even in the entry model segment where it faces tough price competition from other companies (Chinese manufacturers, etc.).

* Sometimes referred to as “LCD pen tablets” too.

b) Pen Tablets

The most basic device* consists of a digital pen and tablet (blackboard type) and has contributed to the Company's results as a mainstay product. It is a PC peripheral used over a connection to a PC, similar to a mouse or keyboard. The Company offers a broad lineup that ranges from professional to beginner products thanks to a simple configuration. While it is sustaining competitiveness in the professional high-end market, competition has intensified in the low- to mid-priced category where it is difficult to achieve differentiation. Furthermore, since the Company has strategically shifted management resources in response to a demand shift toward Displays with better operability and lower prices, sales have been steadily trending downward in the past few years.

* Sometimes referred to as “opaque pen tablets” too.

c) Mobiles, others.*

The Mobiles category covers Displays for use as an input device that contain an OS and storage feature. From the standpoint of usability, they are the same as standard tablet PCs with general pen entry support (many of these products utilize the Company's pen sensor system) and might even appear to have a competitive relationship (fostering competition with the Technology Solution Business in the Company's case). However, the difference is obvious to users who place emphasis on input performance, and it makes more sense for general users who do not have this focus to select standard tablet PCs rather than the Company's Mobiles that function focusing on input devices. These products hence have clear segmentation in performance and functionality. Also, in products other than Mobiles, it sells a group of products for general consumers that are used, for example, to create illustrations and notes on a digital device, such as the stylus pen for Windows tablet PCs and digital stationery.

* Integrated the Consumer Business into the former Mobiles category.

(2) Business Solution

The Company sells business-use products that are capable of direct drawing and character entry on an LCD screen. Usage is increasing in digital signature (hotel check-in, credit card payments, etc.) and medical (electronic medical records, etc.) areas.

2. Technology Solution Business

This business is divided into two segments, AES Technology Solution and EMR Technology Solution, based on digital pen technologies*. It supplies pen sensor systems to smartphone and tablet and notebook PC manufacturers. In particular, the Company is expanding sales to Samsung Electronics <KRX: 005930> (Galaxy Note series) in smartphone-related use, a growing market. Tablet and notebook PC manufacturers highly rate the Company's technology, and it deals with major manufacturers and the number of projects is steadily growing. The Company aims to expand business scale through promotion of its proprietary digital pen technology as a de facto standard, while expanding the scope of users.

* The Company's technologies consist of Active ES (proprietary electrostatic coupling, battery required for pen) format technology and EMR (electro-magnetic resonance) rapid, high-precision positioning sensors (battery not required).

Financial highlights

In FY3/21, sales and profits increased significantly to achieve record high earnings. Sales for online education expanded dramatically due to the coronavirus pandemic

1. FY3/21 results

In the 1H FY3/21 consolidated results, net sales increased 22.5% YoY to ¥108,531mn, operating profit rose 140.8% to ¥13,407mn, ordinary profit climbed 171.3% to ¥14,090mn, and profit attributable to owners of parent grew 161.0% to ¥10,225mn. Thus, sales and profits increased significantly and were higher than expected, hitting new record-high results.

For sales, alongside the effect of the coronavirus pandemic, demand rapidly increased, including for online education and for teleworking. As a result, sales increased greatly in the Branded Business, mainly of Displays and Pen Tablets. In the Technology Solution Business, sales in the AES Technology Solution and EMR Technology Solution segments grew to manufacturers to which the Company is an OEM supplier against a backdrop of increasing usage in the tablet and notebook PC markets. Foreign currency exchange effects worked to reduce net sales by around ¥1.63bn.

In profit-loss, gross profit greatly increased, mainly due to the effects of the higher sales and improvements to the product mix (particularly the growth of Pen Tablets, which have a high profit margin). In addition, in SG&A expenses, despite increased personnel expenses, mainly for the provision for bonuses as performance-linked remuneration, the SG&A expenses ratio improved to reach a new record low, mainly due to efforts to optimize various costs. As a result, the Company achieved substantial increases in operating profit, while the operating profit margin rose significantly to 12.4% (from 6.3% in the previous fiscal year). Foreign currency exchange effects increased operating profit by around ¥0.11bn).

Looking at the Company's financial position, total assets increased by 39.1% form the end of the previous period to ¥71,181mn, mainly reflecting the securing of liquidity on hand (cash and deposits) and an increase in inventories associated with expanding business. On the other hand, shareholders' equity also increased by 35.9% to ¥37,688mn due to the accumulation of internal reserves, so the equity ratio remained about level at 52.9% (54.2% at the end of the previous period.)

FY3/21 financial results

(¥mn)

	FY3/20		FY3/21		Change amount
	Results	% of sales	Results	% of sales	
Net sales	88,579		108,531		19,951
Branded Business	42,587	48.1%	56,678	52.2%	14,091
Technology Solution Business	45,992	51.9%	51,852	47.8%	5,860
Cost of sales	58,872	66.5%	67,123	61.8%	8,250
SG&A expenses	24,140	27.3%	28,000	25.8%	3,859
Operating profit	5,566	6.3%	13,407	12.4%	7,840
Branded Business	1,706	4.0%	9,095	16.0%	7,389
Technology Solution Business	7,650	16.6%	9,260	17.9%	1,610
Adjustment	-3,789	-	-4,948	-	-1,159
Ordinary profit	5,194	5.9%	14,090	13.0%	8,896
Profit attributable to owners of parent	3,917	4.4%	10,225	9.4%	6,308

	End of March 2020 Results	End of March 2021 Results	Change amount
Total assets	51,155	71,181	20,025
Shareholders' equity	27,734	37,688	9,954
Equity ratio	54.2%	52.9%	-1.3%

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

Breakdown of SG&A expenses

(¥mn)

	FY3/20 Results	FY3/21 Results	Change	
			Amount	%
Personnel expenses	9,049	12,464	3,416	37.7%
R&D expenses	4,214	4,663	448	10.6%
Sales promotion and advertising expenses	2,498	2,490	-8	-0.3%
Freight and packing expenses	1,018	1,422	403	39.6%
Outsourcing expenses	1,419	1,347	-72	-5.0%
Depreciation	940	647	-293	-31.1%
Other	5,003	4,967	-36	-0.7%
Total	24,140	28,000	3,860	16.0%

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

2. Results overview by segment

(1) Branded Business

Net sales increased by 33.1% YoY to ¥56,678mn and segment profit was up 433.0% to ¥9,095mn, a significant increase in sales and profits that exceeded expectations. In profit-loss, the segment profit margin improved dramatically to 16.0% (4.0% in the previous fiscal year), reflecting the effects of higher sales and improvements in the product mix. A recovery in sales of Pen Tablets, which have an especially high product margin, and growth in entry-level models in Displays seem to have made a significant contribution to higher profits.

Earnings breakdown in the Branded Business

(¥mn)

	FY3/20 Results	FY3/21 Results	Change	
			Amount	%
Creative Solution	38,473	52,937	14,464	37.6%
Displays	17,581	23,393	5,812	33.1%
Pen Tablets	18,411	27,581	9,170	49.8%
Mobiles, others	2,481	1,963	-518	-20.9%
Business Solution	4,114	3,741	-373	-9.1%

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

a) Creative Solution sales

Net sales increased greatly, rising 37.6% YoY to ¥52,937mn. They were partially affected by factors such as self-restraint on sales promotion events and restrictions on sales activities due to the coronavirus pandemic. However, because of the increase in demand, including for online education, sales grew rapidly of entry models in the mainstay Displays and low-to mid-priced models in Pen Tablets. In particular, in Displays, sales of entry models such as the 22-inch size announced in July 2019 and the 13-inch size announced in January 2020 grew significantly. Also, sales of low-to mid-priced models in Pen Tablets, which had been contracting due to intensifying competition, changed direction and increased significantly. Alongside this, the Company was able to secure an increase in sales for the professional models as well, even while being impacted by the restrictions on sales activities. Therefore, results grew significantly from the Company capturing new demand, assisted by demand related to staying at home (individual home-use hobby applications, etc.) associated with the coronavirus pandemic, as well as the spread of online education and teleworking, among other factors. On the other hand, for Mobiles, others., although sales of Mobiles increased from the updating of the product lineup in FY3/20, overall sales decreased because of the decline in sales of stylus pens which are other than Mobiles.

b) Business Solution sales

Net sales decreased 9.1% year on year to ¥3,741mn. In addition to the impacts of market trends and changes to the competitive environment, results were affected by restrictions on sales activities. Therefore, sales of signature LCD tablets for financial institutions, mainly in Europe, decreased significantly.

(2) Technology Solution Business

Net sales increased 12.7% YoY to ¥51,852mn and segment profit rose 21.0% to ¥9,260mn, for a favorable performance.

Earnings breakdown in the Technology Solution Business

(¥mn)

	FY3/20 Results	FY3/21 Results	Change	
			Amount	%
AES technology	17,282	18,727	1,445	8.4%
EMR Solution, others	28,711	33,126	4,415	15.4%

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

a) AES Technology Solution sales

Net sales increased 8.4% YoY to ¥18,727mn. The Company secured higher sales despite supply chain constraints under the coronavirus pandemic and the impact of a partial slackening in demand for PCs for corporate customers. The Active ES format digital pens have also continued to be highly regarded by manufacturers to which the Company is an OEM supplier.

b) EMR Technology Solution, others sales

Net sales grew, increasing 15.4% YoY to ¥33,126mn atop growth in demand from manufacturers to which the Company is an OEM supplier.

3. Key takeaways of FY3/21 results

Comprehensively assessing the FY3/21 results from the above, although there are factors adversely affecting some of the results, including restrictions on sales activities due to the coronavirus pandemic, the results can be evaluated positively as being significantly higher than initially expected by the Company due to successful capture of new demand. In particular, for online education, the measures it has conducted up to the present time for this growth field can be viewed as bearing fruit, and going forward, it seems we can expect results to grow sustainably. On the other hand, some of the demand related to staying at home (individual home-use hobby applications, etc.) associated with the coronavirus pandemic is a temporary factor, and close attention needs to be paid to this point.

Outlook

Lower sales and profits projected under the baseline scenario for FY3/22. However, high level of earnings is forecast to continue, with continued growth in demand for the education field

For the FY3/22 consolidated results outlook, the Company expects sales and profits to decrease under its baseline scenario, considering the uncertainties associated with the effects of the coronavirus epidemic. Forecasts are for net sales to decrease 6.0% YoY to ¥102,000mn, operating profit to decrease 18.0% to ¥11,000mn, ordinary profit to decrease 21.9% ¥11,000mn, and profit attributable to owners of parent to decrease 21.8% to ¥8,000mn.

In net sales, lower sales are expected in both the Branded Business and the Technology Solution Business. Expectations of a larger decrease in sales in the Branded Business reflect the incorporation of the risk of a partial decrease in sales associated with demand for individual home-use hobby applications, etc. and a certain level of risk in key parts procurement in the production supply chain, among other factors, despite a continuous increase in demand expected for online education.

Meanwhile in profit-loss, operating profit is expected to decrease due to the impact of lower sales on profits and continued active R&D investment* for the future. As a result, the operating profit margin is also expected to decline to 10.8% (from 12.4% in the previous fiscal year), but to remain at a level above 10%.

* New product development and next-generation technology development, etc. aimed at advancing technology leadership

Forecasts for FY3/22

(¥mn)

	FY3/21		FY3/22 (Forecast)		Change	
	Results	% of sales	Amount	% of sales	Amount	%
Net sales	108,531		102,000		-6,531	-6.0%
Branded Business	56,678	52.2%	51,500	50.5%	-5,178	-9.1%
Technology Solution Business	51,852	47.8%	50,500	49.5%	-1,352	-2.6%
Cost of sales	67,123	61.8%				
SG&A expenses	28,000	25.8%				
Operating profit	13,407	12.4%	11,000	10.8%	-2,407	-18.0%
Branded Business	9,095	16.0%	7,500	14.6%	-1,595	-17.5%
Technology Solution Business	9,260	17.9%	8,200	16.2%	-1,060	-11.5%
Adjustment	-4,948	-	-4,700	-	248	-5.0%
Ordinary profit	14,090	13.0%	11,000	10.8%	-3,090	-21.9%
Profit attributable to owners of parent	10,225	9.4%	8,000	7.8%	-2,225	-21.8%

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

Below we review results outlooks and activity policies by business area.

(1) Branded Business

Net sales are forecast to decrease 9.1% YoY to ¥51,000mn and segment profit to decrease 17.5% to ¥7,500mn. The net sales forecast incorporates the risk of a partial decrease in demand for individual home-use hobby applications, etc., despite projecting a continuous increase in demand for online education. In profit-loss, the outlook takes into account the abovementioned demand forecast as well as active R&D investment for the future, etc.

(2) Technology Solution Business

Net sales are forecast to decrease 2.6% YoY to ¥50,500mn and segment profit to decrease 11.5% to ¥8,200mn. The Company's policy is to maintain and develop strong relationships with its major customers while aiming to capture business opportunities leading to the fields such as digital transformation (DX) in education. The Company will also engage in active R&D investment for the future.

Results trends in past years

Technology Solution Business driving growth over the past few years

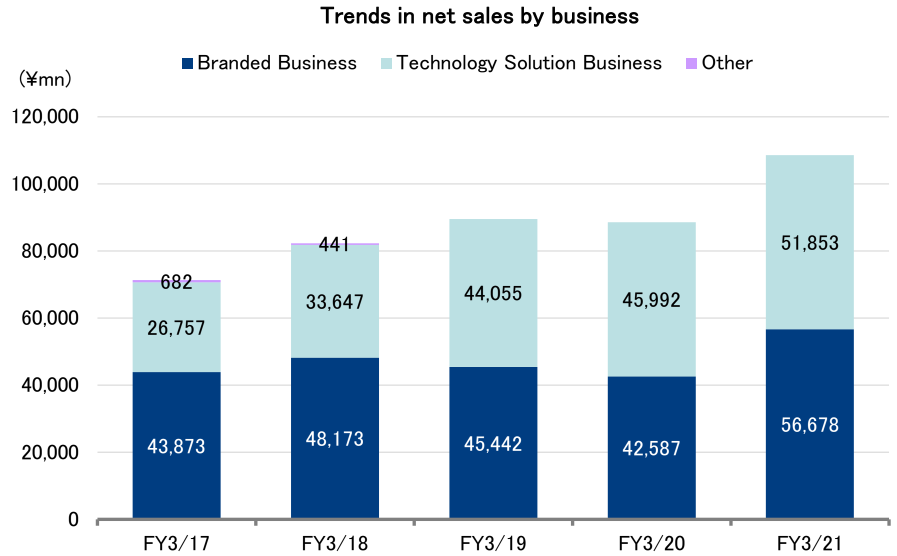
Looking at how sales trended up to the previous period, the large slump in FY3/17 occurred because of the combined impacts of yen appreciation, product cycle movement, product recalls by Samsung Electronics, and other factors. Since then, however, sales recovered with growth in the Technology Solution Business. Nevertheless, Branded Business sales have been trending lower with the structure of positive growth in the Technology Solution Business continuing to offset its decline. However, the Brand Business experienced rapid growth in sales in FY3/21, mainly for online education due to the coronavirus pandemic, and achieved new record high earnings.

The main reason for the contracting trend in the Branded Business sales in recent years had been the need for time to fully compensate for growing competition in low- and mid-priced products in Pen Tablets, which had been a mainstay product, through a strategic demand shift to Displays. However, Displays is steadily developing a new market and ramping up sales with entry models with high profit margins, so that it is important to recognize trend change in the sales mix (ratios).

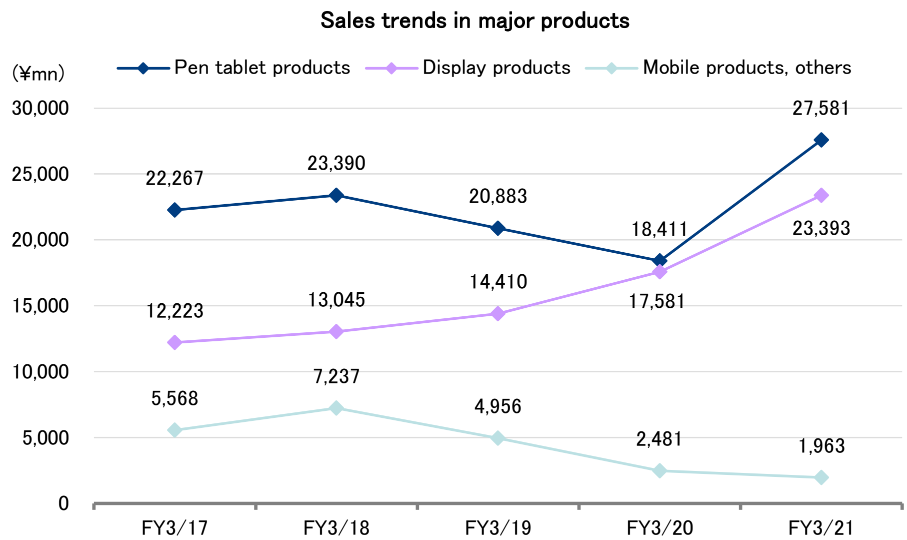
Growth in the Technology Solution Business over the past few years, meanwhile, reflects expansion of the market for pen sensor systems for tablets and notebook PCs and strong performance in pen sensor systems for smartphones (particularly with Samsung Electronics' Galaxy Note series) aided by enhanced functionality.

In profit-loss, with the exception of an operating loss in FY3/17, the operating profit margin has improved gradually from the 4% level to the 6% level while conducting aggressive R&D and new product development. In FY3/21, the profit margin improved dramatically due to higher profits atop a significant increase in sales, improvements in the product mix, and optimization of SG&A expenses, etc.

In financial standing, while the capital ratio temporarily slipped in FY3/17 on a hefty net loss due to recording impairment losses, it has steadily improved since then with buildup of retained profits and has moved close to 60%, the near-term goal for financial soundness. ROE, which reflects capital efficiency, has been at the double-digit level, exceptionally over 30% in FY3/21, and we think that the Company's finances are in excellent condition.

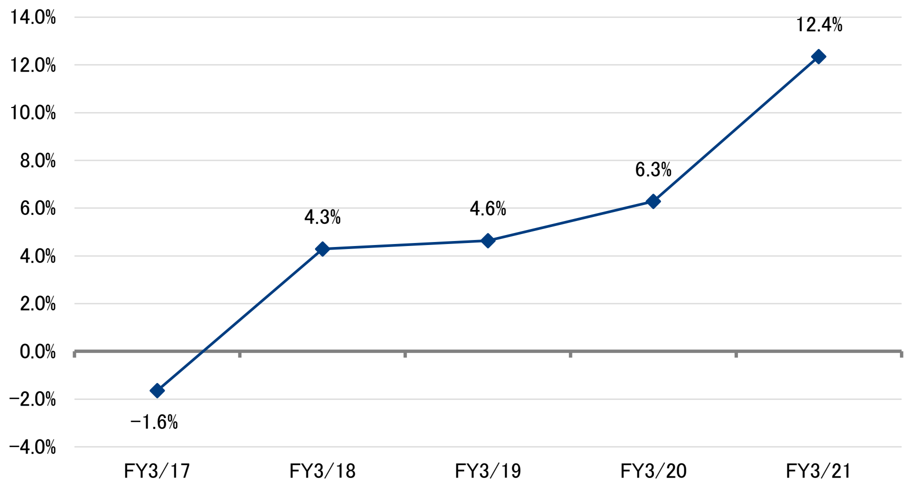


Source: Prepared by FISCO from the Company's financial results



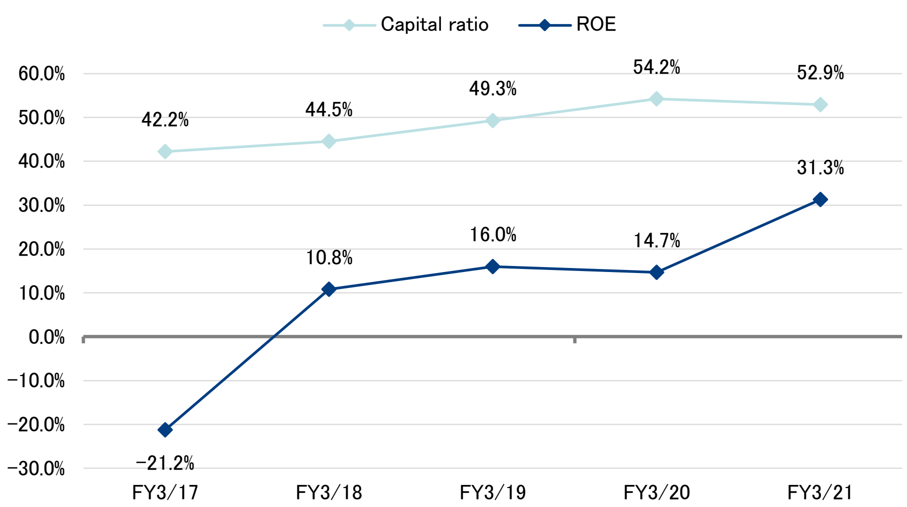
Source: Prepared by FISCO from the Company's financial results

Trends in operating profit margin



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

Trends in capital ratio and ROE



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

Growth strategy

As the targets of the medium-term business plan, Wacom Chapter 2, were achieved a year early, the Company announced a new medium-term business direction, Wacom Chapter 3. The Company is to create a foundation for accelerating growth by developing new core technologies

1. Progress of medium-term business plan Wacom Chapter 2

(1) Early achievement of the targets of Wacom Chapter 2

The Company has been progressing the medium-term business plan Wacom Chapter 2, formulated in FY3/19 and finishing in FY3/22. Under the plan, the Company aims to achieve sustainable growth by creating value needed by customers while constantly staying at the market forefront in pen and ink digital technology as a Technology Leadership Company. Specifically, the Company engaged in three companywide strategies: 1) Advancing technology leadership, 2) Close cooperation through island and ocean strategy and 3) Bold selection and concentration, with targets for FY3/22 of a 10% profit margin (¥10,000mn in operating profit), ¥100,000mn in net sales, and ROE of 15-20%. By steadily engaging in solving management issues and executing strategies, the Company achieved its main KPI targets one year early, and has therefore announced a new medium-term business direction, Wacom Chapter 3 (FY3/22-FY3/25).

(2) Summary of Wacom Chapter 2

The Company not only achieved its earnings targets one year early, but also had considerable success in 1) reforming the product portfolio, 2) expanding opportunities for digital pen experiences, 3) building a lean organizational structure, and 4) fostering a corporate culture that makes full use of individual capabilities, as summarized below.

1) Reforming the product portfolio

The Company reformed its product portfolio to widen the target of entry-level users for its brand products, and succeeded in providing ink experiences to many users, not only in the creative field, where it has developed deep collaboration with application partners, but also in the education field. Through this initiative, the Company has contributed to expanding its business foundation, which will lead to high future usage of core technologies related to digital ink that are currently under development.

2) Expanding opportunities for digital pen experiences

The Company has successfully provided digital experiences of pen and paper that have been evolved through its technology solutions to users not only of widespread devices such as tablet and notebook PCs, but also among diverse business partners handling digital paper and dedicated devices for education providers, and so forth. In doing so, it has advanced preparations for diverse workstyles, learning styles, and use cases.

3) Building a lean organizational structure

The Company has been actively engaged in cross-divisional initiatives in the areas of R&D and technology development, product planning, materials procurement, quality control, and inventory control. While focusing on issues to be addressed, it has inculcated a focus on profits throughout the entire organization, resulting in company-wide improvement in profitability. Through this effort, the Company has built a foundation to support active, sustainable technology investment for the future.

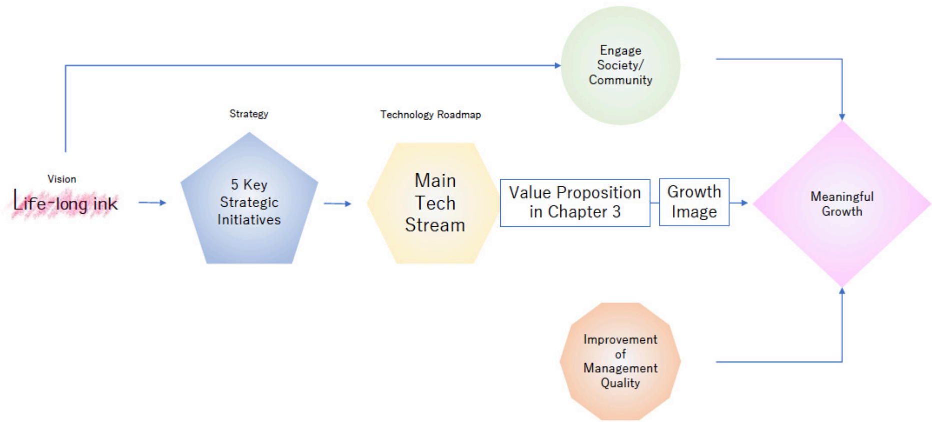
4) Fostering a corporate culture that makes full use of individual capabilities

At the center of the engineer organization, the Company set up multiple project teams with highly motivated individuals at the core. By creating value through the combination of strengths possessed by various partner communities, the Company has cultivated an awareness of sharing growth with all stakeholders.

2. Outline of Wacom Chapter 3, the new medium-term business direction

Under the direction, the Company has redefined five key strategic initiatives for inheriting the vision of "lifelong ink," (continuing to provide "meaningful human experiences" to customers and society over a long time period based on Wacom's technology), and further developing and evolving the initiatives it has undertaken to date. In carrying out the five strategy approaches, the Company has set out "six main streams for technology innovation," which it will operate as a corporate technology roadmap. The Company will use these to promote specific value propositions and sustainable growth. Moreover, the policy also calls for initiatives to increase the quality of management through corporate governance reforms and for engagement with society and communities through the Company's unique approaches.

Storyline of Wacom Chapter 3



Source: From the Company's results briefing materials

(1) Five key strategic initiatives

1) Technology Leadership

Under this strategy, the Company will continue to focus on technology innovation as the source of its value provision, maintaining and developing its unrivalled technological advantage. The Company has worked to contribute to various types of digital transformation (DX) (public service desk procedures, document filing, and writing on PDFs in workflows, as well as digital voting, etc.), inclusion in various advanced devices and digital stationery, etc., and incorporation in smart home solutions. Now, the Company intends to continue providing the highest level of "pen, paper, and ink experience" through technology development spanning hardware, software, and services.

2) Community Engagement

Under this strategy, the Company will form valuable experiences not only by itself, but also through deep collaboration with communities (partners). In a recent example, the Company jointly held an online drawing festival together with pixiv Inc.* In other collaborations, the Company has created designated Chromebook-compatible products, Android compatibility, and worked on building creative workflows in remote environments.

* For three days from May 22, 2021, the Company held the Drawfest live-streamed viewer-participation event. Popular illustrators and manga creators around the world gave online seminars and workshops on drawing and held participative programs for viewers to complete drawings all together within the time frame.

3) New Core Technology, New Value Proposition

This strategy is to provide new value based on new core technologies in addition to existing core technologies. The idea is to select three fields that have a high affinity with its existing technologies–AI, XR, and Security–and realize new value propositions in these fields using new technologies and business models. The Company is already moving on collaborative projects with other companies, for example, creation of a new educational experience*1 through digital ink and AI, protection of copyrights through blockchain certification,*2 and drawing experiences in XR space.*3

*1 The Company entered a comprehensive business alliance agreement with Zoshinkai Holdings Inc. (Z-kai Group) for the use of Handwriting x Digital in the education field and has also been working on joint development with sdtech Inc. towards use of AI in Handwriting x Digital, among others.

*2 A system that uses digital signature authentication technology to certify digital art works by incorporating a signature into the digital artwork and its certificate, thereby preserving and circulating the copyright of the creator.

*3 New creation experiences that involve joint creation by multiple and remote creators, as well as free exchange between 2D and 3D.

4) Technology Innovation for Sustainable Society

The Company aims to contribute to the development of a sustainable society through technology and product development that contributes to environmental care. Through its existing participation in the Japan Climate Initiative (JCI) and establishment of the tech team for environment-friendly product development, the Company is promoting technology innovation that leverages its unique strengths. The Company is also working to align corporate action with the circular economy. For example, it is engaged in activities to reuse stages made from waste materials as furniture.

5) Meaningful Growth

Under this direction, ensuring sound financial growth, the Company will target multi-dimensional, “meaningful growth” incorporating customers, users, society, communities, and individual stakeholders. This means aiming for sustainable growth from a long-term perspective.

(2) Six main streams for technology innovation and specific value examples

1) Pen technology (current core technologies/ current business models)

The Company will further develop its digital pen technology, which is the source of its value proposition, and aim to introduce new product lines including environmentally friendly products.

2) Pen and paper technology (current core technologies/ current business models)

The Company will cultivate new customer groups through collaborations with all kinds of “paper” (displays, apps).

3) Universal ink technologies (current core technologies/ current business models)

The Company will provide remote DX experiences, for example in the creative and education fields, through collaboration with data formats and apps, and cloud compatibility.

4) AI x Digital ink (new core technologies/ new business models)

The Company will expand into individually optimized education and creative support services, etc., by developing plugins that enable AI and ink collaboration.

5) XR x Digital ink (new core technologies/ new business models)

The Company will provide new 3D drawing work-flows for the creative, education, construction, and medical sectors through 3D drawing technology in XR space.

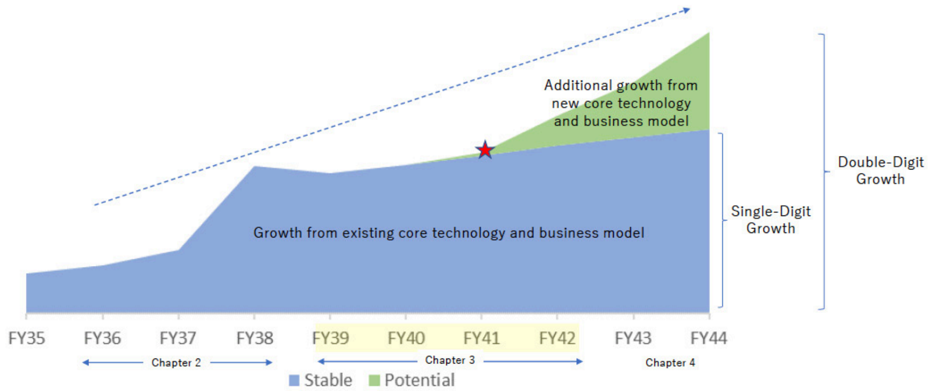
6) Security x Digital ink (new core technologies/ new business models)

The Company will provide individual authentication and copyright protection services for the creative, medical and other sectors, through handwriting-based personal authentical technologies.

3. Envisaged growth and financial policy

Through the new medium-term business direction, Wacom Chapter 3, the Company will further promote its current core technologies and business model, while working to accelerate growth in the next stage by taking a strategic focus on establishing new core technologies and business models. The direction does not set numerical targets for a single point in four years' time but has set out expectations for the Company's growth direction and progress on its strategic initiatives. However, in its envisaged growth scenario, the Company has a baseline of stable growth through its current core technologies and business models, with plans to establish new core technologies and business models in the second two years, and then increase growth into the double-digit range in the next stage, starting from the fifth year onward. Furthermore, for its financial policies, the Company has 1) set ROIC of 25–30% as a new indicator and will target 2) ROE around 20%, and 3) dividend payout ratio around 30%. In addition, the Board of Directors will engage in frank and active discussion, keeping a close eye on the efficiency of business activities and capital efficiency in order to increase the feasibility of growth.

Envisaged growth scenario under Wacom Chapter 3 (operating profit)



Note: Timeline from FY39 to FY42 shows the period from FY3/22 to FY3/25
Source: From the Company's results briefing materials

4. Focus points identified by FISCO analysts

We consider that the Company has achieved tremendous results under Wacom Chapter 2, including its earnings, changes in its product portfolio (growth in entry-level models for display products, etc.) and expansion into the education field, which represents a large market. On the other hand, we see Wacom Chapter 3, as an important basis for forecasting the Company's direction and future potential, as it establishes three new technologies (AI, XR, security) and new business models during the target period and has a major focus on how the Company will go about creating a platform for accelerating growth. For this reason, the Company's success is likely to be determined not only by its inhouse technology development, but also by the degree to which it can deliver value through new services based on collaboration with other companies. However, the Company's policy of avoiding red oceans with harsh competition and aiming to create value in new markets (blue oceans) is reasonable. From another perspective, the very fact that the Company is in a position to attempt this can also be seen as a significant advantage. In terms of new business models, the Company seems likely to focus on providing Software as a Service (SaaS), and an important point to focus on will be how the shift to a fee based revenue model will impact on the Company's growth and earning potential.

Initiatives for society

Supporting a sustainable society through provision of "lifelong ink"

The Company places emphasis on initiatives that contributes to ESG improvements and a sustainable society. It posts information on the "Social Initiatives" section of the Company website and discloses its fundamental views and specific activities. We think the Company's use of a concept of "lifelong ink" to describe its technology stands out. This reflects awareness of the origins of its significance and value creation in support for a sustainable society by facilitating "writing and drawing" experiences that accumulate throughout a person's life and communicating them to future generations. Together with various community partners, the Company is pursuing the potential of "lifelong ink*," not only in people's everyday lives, but also in fields ranging from the creative to business and education. In this way, the Company's direction should lead to sustainable growth for users and for the Company itself.

* For example, in the education field, it is developing AI Ink for Education, which provides a learning environment tailored to individuals by clarifying the learning characteristics of individual students from line-of-sight data and pen movements made during learning.

Moreover, the Company values relationships made between the local communities and individual staff members working in its bases around the world, while working to develop operations and products that are sensitive to the environment. The Company intends to continue making proposals for the future image of society together with the community, such as Ars Electronica*1 rather than just as a single company. Moreover, The Company also intends to conduct social implementation of technology services such as STEAM education*2 and exploratory learning*3.

*1 Ars Electronica, a global creative entity, has been continuously proposing "new creativity and future societal concepts facilitated by cutting-edge technologies" over 40 years from its location in Austria.
*2 Science, technology, engineering, art, and mathematics (STEAM) education is a gradually increasing trend in society. In the art domain, which is a component of STEAM, enabling visualization of the creative activity by creators can help to promote learning by others in creative activities.
*3 For example, combining programing education and digital pen and using AI to analyze the tracks of an individual student's ink data enables the development of logical thinking skills.

Also, the Company considers responding to climate change to be an important issue in environmental management and is working to reduce greenhouse gases, while it is also conducting business activities based on risks and opportunities in the business environment relating to climate change. In particular, it is progressing BCP to respond to the risk of a restriction to corporate activities due to floods and other natural disasters, which are increasing year by year. It also recognizes that developing environmentally friendly products is an opportunity and is working on strengthening the structure for this. In addition, as an action that will lead to a reduction in CO_2 emissions in the value chain as a whole, it requires that its suppliers support and implement the Wacom Supplier Code of Conduct.

Returns to shareholders

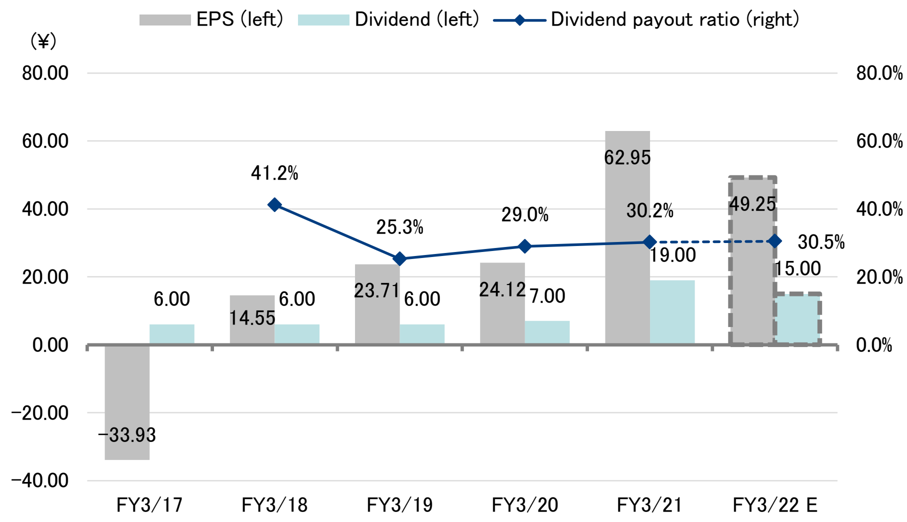
For FY3/21, the Company as set a dividend per share of ¥19 (including a special dividend of ¥5.5), an increase of ¥12 YoY. The forecast dividend for FY3/22 is ¥15 per share. The Company also intends to engage in a treasury stock acquisition with a total amount of up to ¥10.0bn

The Company's basic policy towards shareholder returns is to pay steady dividends on its profits after considering the amount of funds to be retained for future business development and a sound financial base. The Company had previously set a dividend payout ratio of around 40% as the standard for the dividend level, but from FY3/18, it lowered it to around 30%. This was in order to solidify the foundations for growth in the future and was necessary to increase its financial soundness, while the background is the fact that it has set a target to aim for at the present time of around 60% for the equity ratio (it was 52.9 % at the end of FY3/21). Also, the Company only pays dividends once at the end of the fiscal period in consideration of keeping down administrative costs.

For the dividend for FY3/21, the Company has decided to pay ¥19 per share (ordinary dividend ¥13.5, special dividend ¥5.5; dividend payout ratio 30.2%), up ¥12 YoY. The increase reflects a significant increase in profits above expectations, which enabled the Company to achieve the management targets of Wacom Chapter 2 a year early. Moreover, for FY3/22 the Company expects to pay a dividend of ¥15 per share (expected dividend payout ratio 30.5%). This means that the starting ordinary dividend base for the first year of Wacom Chapter 3 is ¥1.5 higher, which can be seen as increasing the dividend in line with medium-term growth.

On May 12, 2021, the Company announced its intention to conduct a treasury stock acquisition for a total amount of ¥10.0bn over the period until March 31, 2025. The initiative appears to be intended as a use for cash flow, giving consideration to a balance between investment and shareholder returns.

Trends in EPS, dividend, and dividend payout ratio



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

Company profile

Established in 1983, the Company has grown steadily with technology and now leads the global market of pen tablets for creators

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, a part of the new Reiwa era). In 1984, it announced the world’s first 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 tablet market for creators, it has consistently kept a leading position on a global basis since the 2000s.

In 1991, it entered into the pen sensor components field (currently, the Technology Solution Business). The Company conducts OEM supply of digital pens, control ICs, touch pads, and other parts and modules to finished product manufacturers. It has been achieving rapid growth amid expansion of tablet, notebook PC, and smartphone markets.

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

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