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SB Technology Corp. Overview of Earnings Results Briefing for FY2023

This is a transcript of the SB Technology Corp. FY 2023 Results Briefing held on January 31, 2024.
Speaker: Mr. Shinichi Ata, President & CEO, SB Technology Corp.

Despite lower sales due to exclusion of Fontworks, Inc. from consolidation, operating income and net income will increase and year-end dividends will be increased by ¥10.

Summary

Summary

| FY2023 Q3

FY23Q3 Financial Results

Sales decreased due to restrained investment in Telecommunication and the deconsolidation of Fontworks, Inc.
SG&A expenses increased due to increased hiring, but profit margin improved.

Orders Received

Q3 orders received fell by-¥2.1 billion year on year, mainly due to the impact of the Telecommunication, **but the order backlog at the end of December was a record high of ¥26.6 billion.**

FY23 Forecast

By the impact of revised earnings forecasts for Cybertrust Japan Co., Ltd. and the transfer of Fontworks, Inc. shares
**Revised Sales -1 billion yen/Operating income-0.3 billion yen
/Net income +0.1 billion yen**

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Shinichi Ata: Hello everyone, I am Shinichi Ata, President & CEO of SB Technology. Thank you for participating in our financial briefing while you are very busy today. I would like to explain the outline of the results and the progress of the Medium-term Management Plan.

First, a summary of financial results for the third quarter of the fiscal year ending March 2024. Due to restrained investment in Telecommunication and the deconsolidation of Fontworks, Inc. net sales decreased. In addition, although SG&A expenses increased due to the strengthening of hiring and other factors, the profit margin has been on an improving trend.

About the orders received. Including the impact of the Telecommunication, orders received in the third quarter fell by ¥2.1 billion year on year, but the order backlog at the end of December was a record high of ¥26.6 billion.

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The full-year forecasts are for net sales to be negative ¥1 billion and operating income to be negative ¥300 million due to the revision of the earnings forecasts of subsidiary Cybertrust Japan Co., Ltd.. Net income attributable to owners of the parent was revised by ¥0.1 billion to ¥8.3 billion from ¥8.2 billion after the combined effect of the transfer of Fontworks, Inc. shares, etc.

Consolidated P/L (Apr—Dec cumulative)

		Consolidated P/L (Apr—Dec Cumulative)		FY2023 Q3	
[Millions of yen]	(Profit margin)	FY23Q3	FY22Q3	Change	Change %
Net sales		47,839	48,231	▲391	▲0.8%
Operating income		3,607 (7.5%)	3,541 (7.3%)	+66	+1.9%
Ordinary income		3,453 (7.2%)	3,489 (7.2%)	▲35	▲1.0%
Profit attributable to owners of parent		<small>Record High</small> 7,166 (15.0%)	2,108 (4.4%)	+5,057	+239.9%
Net profit					
EBITDA ※		4,862	4,778	+84	+1.8%

※EBITDA = Operating income + Amortization of goodwill + Depreciation

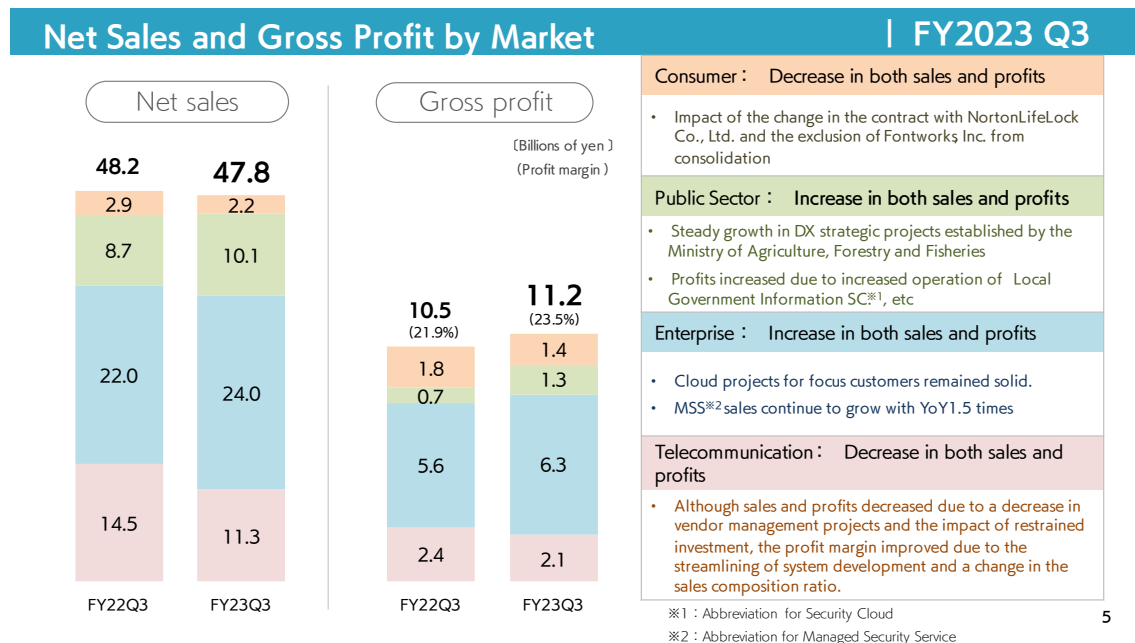
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This is consolidated PL. Net sales amounted to ¥47.839 billion, a year-on-year decrease of ¥391 million. Operating income was ¥3.607 billion, a year-on-year increase of ¥66 million, and ordinary income was ¥35 million.

Net income attributable to owners of parent was ¥7.166 billion, a record high for the first three quarters of the fiscal year under review.

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Net Sales and Gross Profit by Market



This is Net sales and gross profit by market. Telecommunication sales in the slide bar graph decreased by ¥3.2 billion year-on-year. Gross profit on the right-hand side also decreased by ¥300 million from ¥2.4 billion to ¥2.1 billion due to a decrease in sales of ¥3.2 billion, despite an improvement in the profit margin.

Enterprise sales increased by ¥2 billion year on year. Gross profit increased by ¥700 million, or approximately 10% year on year.

For the Public Sector, net sales ranged from ¥8.7 billion to ¥10.1 billion and gross profit ranged from ¥700 million to ¥1.3 billion. In the fiscal year ended March 2023, there were incidents in the local government information security cloud in March and August, and we were forced to respond to the incidents in the future. Since then, the system has been operating smoothly on a daily basis, and we believe that the system is now returning to its original benefit.

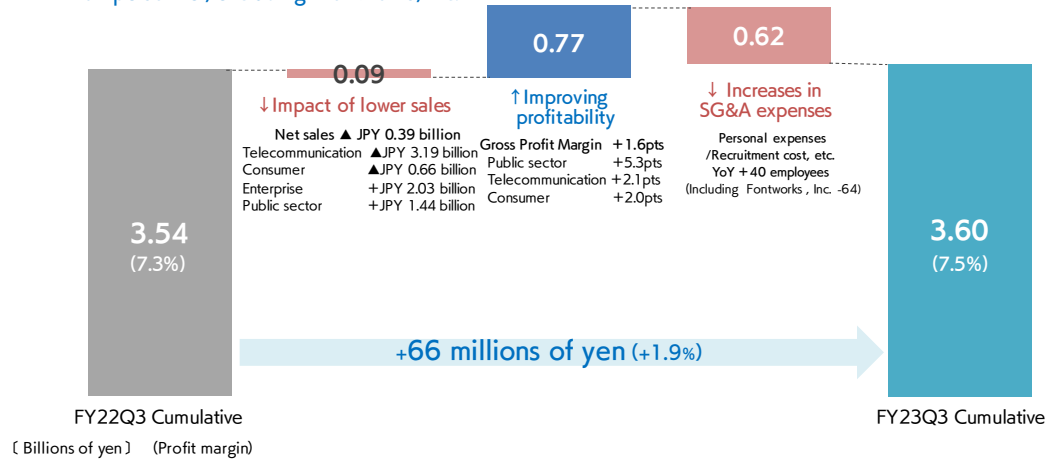
Consumer sales decreased from ¥2.9 billion to ¥2.2 billion. One of the factors is that the Fontworks, Inc. has been deconsolidated. The other is a gradual decrease over several years due to a contract change with NortonLifeLock Co., Ltd. Although gross profit is also declining, we are still maintaining a profit of ¥1.4 billion.

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Factors Behind Changes in Operating Income

Factors Behind Changes in Operating Income | FY2023 Q3

- Gross profit margin up 1.6 percentage points due to continued improvement in profitability despite lower sales of Telecommunication and Consumer
- Reinforcement of resources, such as recruitment, led to an increase in sales pipe costs, and an increase of 104 personnel, excluding Fontworks, Inc.



This is the factors behind changes in operating income. The negative ¥390 million decrease in net sales had a negative impact on operating income of ¥90 million. The breakdown of the decrease in sales is as shown on the slide. A breakdown of the improvement in profitability is that the Public Sector is returning to normal operation after the incident and improved profitability for Telecommunication and Consumer.

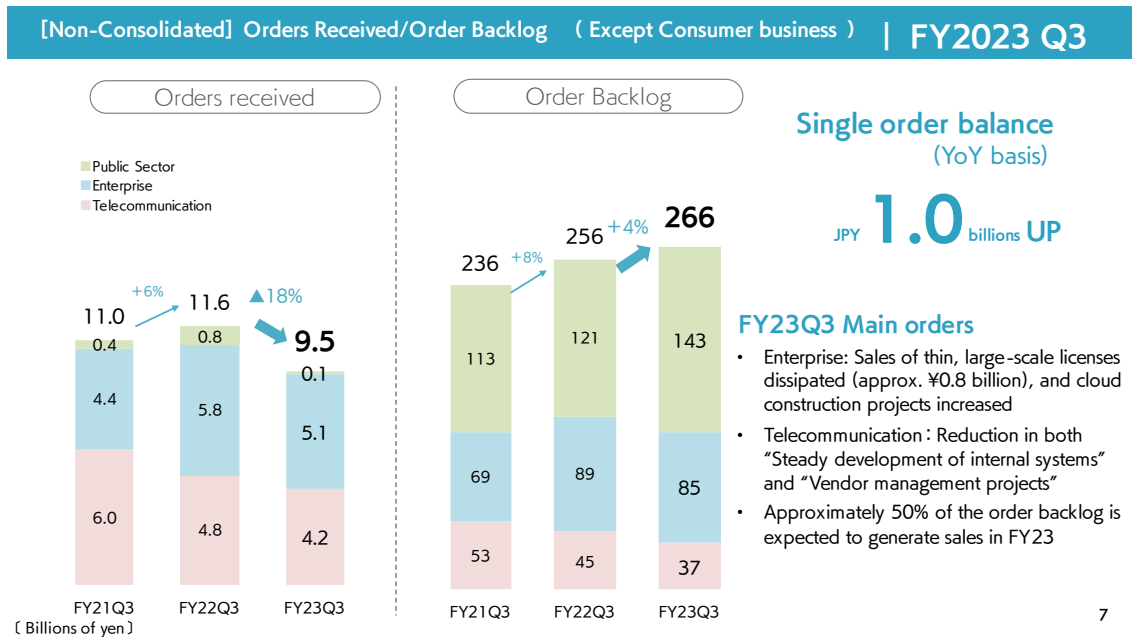
The increase in SG&A expenses was mainly due to personnel expenses and activity expenses, and as of the end of December, there was an increase of about 40 employees from the previous fiscal year. This figure includes those excluded from the Fontworks, Inc. consolidation and increases the number of employees by 104 excluding the effect of the Fontworks, Inc. consolidation exclusion.

The increase in SG&A expenses was mainly due to personnel expenses and activity expenses, and as of the end of December, there was an increase of about 40 employees from the previous fiscal year. This figure includes those excluded from the Fontworks, Inc. consolidation and increases the number of employees by 104 excluding the effect of the Fontworks, Inc. consolidation exclusion.

The amount of sales pipe costs is simply expressed in the form of numbers of employees, but I would like to see a considerable increase in the number of employees, mainly in the area of SB Technology. As a result, operating income for the third quarter totaled ¥3.6 billion.

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[Non-Consolidated] Orders Received/Order Backlog (Except Consumer business)



I will explain about the orders received. Compared to fiscal 2021, before the start of the Medium-Term Management Plan, Telecommunication orders fell from ¥6 billion to ¥4.2 billion. Enterprises range from ¥4.4 billion to ¥5.1 billion. As for the Public Sector, the key point is how much new projects can be received in the fourth quarter, when bidding is concentrated.

The graph on the right side of the slide shows the balance of orders received. As of the end of December, the amount of outstanding orders received was ¥26.6 billion. Approximately half of this amount is scheduled to be sold in the fourth quarter of the fiscal year, as the 5-year contract for the Local Government Information Security Cloud and the Ministry of Agriculture, Forestry and Fisheries have decided to apply for electronic applications in the next fiscal year.

Also, as a major reform in the Enterprise, we are planning to reduce as much as possible the work done by licensed sales, which is extremely thin in profit. However, we do not discontinue licensing for systems that can be left to system integration or subsequent operation after sales.

In the third quarter of the previous fiscal year, we received about ¥800 million in orders for license sales. However, based on this policy, we are declining from the third quarter because we are hesitant to receive orders that we cannot anticipate in the future.

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FY23 Full-year Earnings Forecasts

FY23 Full-year Earnings Forecasts					FY2023 Q3	
[Millions of yen] (Profit margin)	FY23 earnings forecast ('23/7/19 revision)	FY23 earnings forecast (Revised this time)	Change	FY22	YoY	
					Change	Change %
Net sales	68,000	67,000	▲1,000	67,227	▲227	▲0.3%
Telecommunication	16,300	16,050	▲250	19,575	▲3,525	▲18.0%
Enterprise	35,400	34,400	▲1,000	30,356	+4,043	+13.3%
Public Sector	14,000	14,000	0	13,224	+775	+5.9%
Consumer	2,300	2,550	+250	4,070	▲1,521	▲37.4%
Operating income	5,900 (8.7%)	5,600 (8.4%)	▲300	5,557 (8.3%)	+43	+0.8%
Ordinary income	5,750 (8.5%)	5,450 (8.1%)	▲300	5,499 (8.2%)	▲49	▲0.9%
Profit attributable to owners of parent Net profit	8,200 (12.1%)	8,300 (12.4%)	+100	3,497 (5.2%)	+4,803	+137.3%

* Fontworks Inc. is not subject to consolidation after Q3

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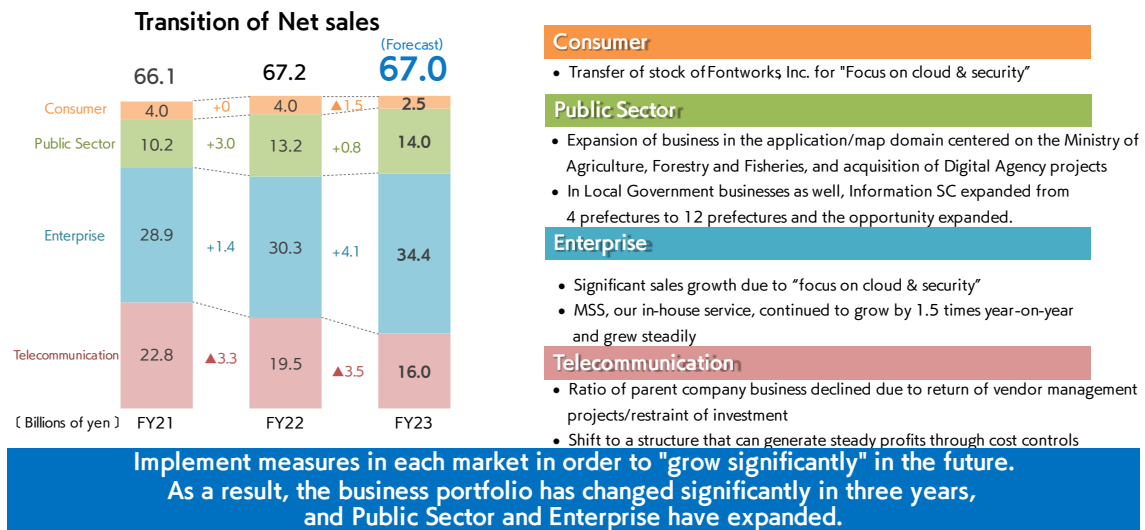
This is the full year earnings forecasts. As explained in the summary, we have revised our sales forecast from ¥68 billion to ¥67 billion from minus ¥1 billion in line with the revised earnings forecast of Cybertrust Japan Co., Ltd. Operating income will also be ¥5.6 billion, a negative ¥300 million from the forecast of ¥5.9 billion. At the same time, ordinary income will also be calculated at a negative ¥300 million.

Net income attributable to owners of the parent company is basically affected by ¥100 million or more after tax and in our proportionate share when operating income is minus ¥300 million. However, the impact of the transfer of Fontworks, Inc. shares and other assets is more than ¥200 million, so minus more than ¥100 million, minus more than ¥200 million, for a gain of ¥100 million. Therefore, we have revised the forecast of ¥8.2 billion to ¥8.3 billion.

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Progress of the Fourth Medium-Term Management Plan

Progress of the Fourth Medium-Term Business Plan | FY2023 Q3



※ FY23 figures are consolidated earnings forecasts

I will explain the progress of the Fourth Medium-Term Business Plan. The 3rd Medium-Term Business Plan runs through fiscal 2021, but sales per se have not increased as much. However, the contents have changed considerably.

Telecommunication sales amounted to ¥22.8 billion in fiscal 2021, and this fiscal year's forecast is ¥16 billion, a decrease of approximately 30%. This is due to the fact that the return of vendor management projects and the restraint on investment in telecommunications businesses have drastically reduced the number of jobs.

On the other hand, Enterprise sales of ¥28.9 billion in fiscal 2021 and ¥34.4 billion in the current fiscal year, and Public Sector sales of ¥10.2 billion in fiscal 2021 and ¥14 billion in the current fiscal year. These two are focus areas.

It's not that Telecommunication is not a focus area, but the area that must be extended is growing by 23 percent. This year's forecast is that the two areas of Enterprise and Public Sector account for 72% of total sales, and we intend to grow by steadily expanding these areas.

Sales of Enterprise are growing significantly due to their "focus on cloud and security." Symbolically, our proprietary service, MSS (Managed Security Service), also continued to grow sales by 1.5 times year-on-year, and is growing steadily.

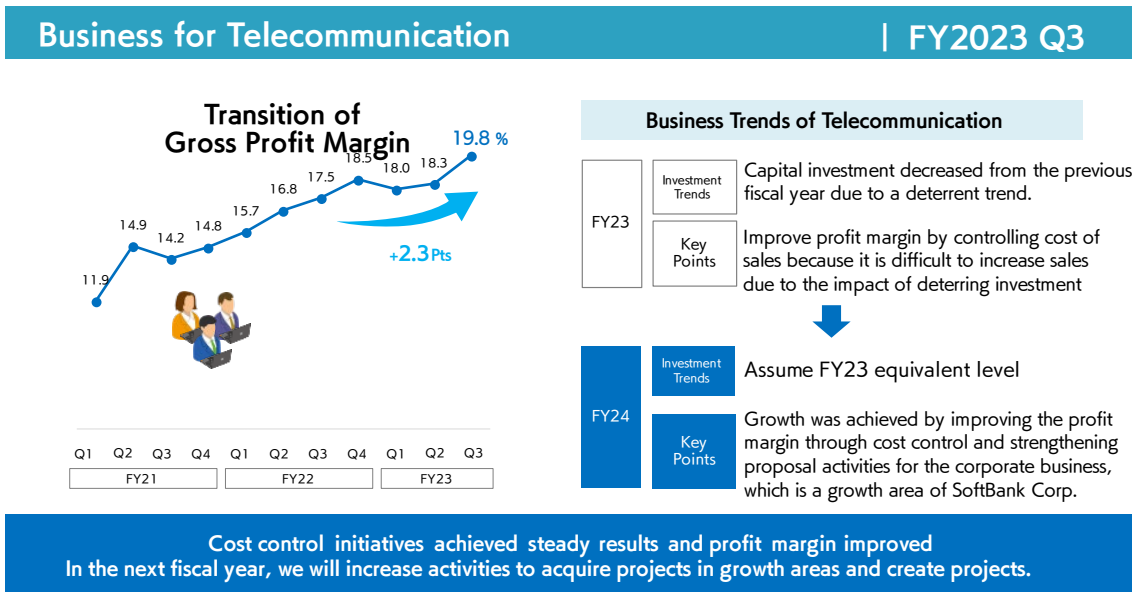
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MSS has been growing 50% year on year for three to four years, and has been growing gradually, although it is not explosive. Since the role of the Security Operation Center is the monitoring of operations by manned personnel, it is an important point of MSS to ensure that analysts are educated and deployed.

In addition, the Public Sector expanded its business to areas such as electronic applications and map areas this term, and also acquired Digital Agency projects related to real estate registry records in the base registry. Regarding municipal business, we have been preparing to provide 12 prefectures and 405 municipalities with various applications that can work with the Local Government Information Security Cloud since the next fiscal year.

In fiscal 2023, we provided explanations on services to local governments in early autumn. We believe that we will be able to adopt it in the timing from February to March, when the budget for the next year will be decided.

Business for Telecommunication



It is business for Telecommunication. In order to increase profitability, we have made efforts to reduce vendor management deals and increase the percentage of work that meets with higher added value and the latest technology. As a result, gross margin increased from 18 percent at the start of this year to 19.8 percent in the third quarter. We will continue to work on such operational improvements.

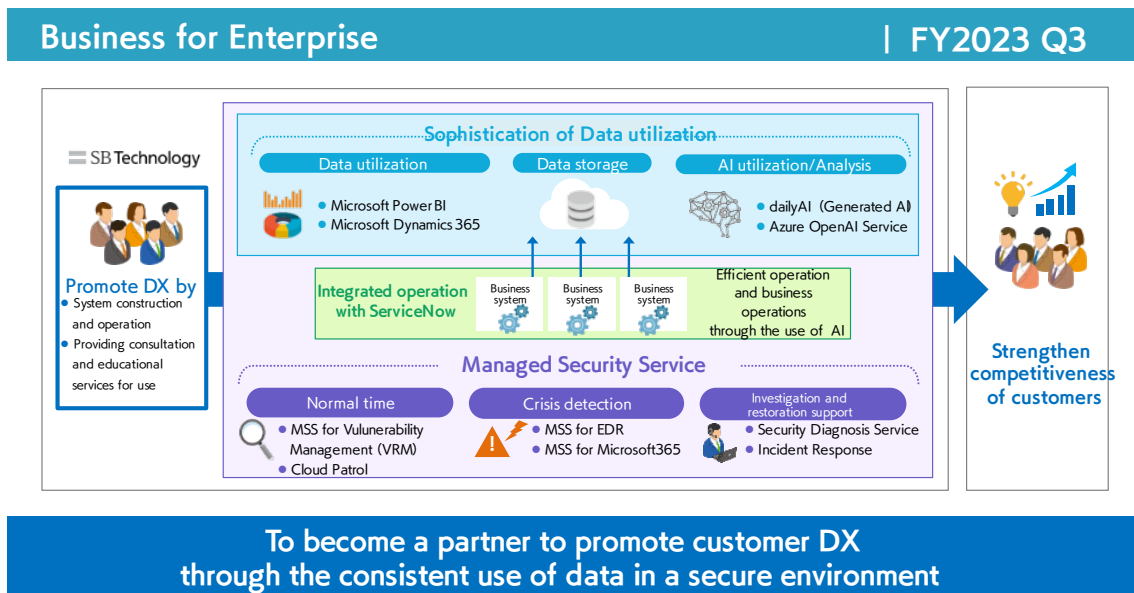
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In addition, we have begun full-scale use of offshore technology in Southeast Asia, which we have explained to date, from this fiscal year. We are currently trading with four companies, and we intend to develop this field through a stronger cooperative relationship with one of them.

Only five people were ordered from that company in the first quarter, but we are currently having 40 people, and planning to have more than 50 people in March. Telecommunications companies, which are the ordering sources, reduce costs, and we believe that we can secure profits.

We expect these initiatives to drive our gross profit margin in the 20 percent range for the next fiscal year.

Business for Enterprise



It is business for Enterprise. I have been informing you many times, but in the future we must make use of the data. However, in order to make use of data, it is not necessary to include tools, but it is necessary to enhance security and increase the ability to push up from the bottom.

In the consumer business, there are many cases in which data can be obtained by leaving anything to AI, but in manufacturing and other industries, we understand that they are looking for ways in which original data can be utilized within the company without leaking to the outside. For this reason, we believe that enhancing security-related measures such as MSS will be a prerequisite for the construction of AI and other tools-and data-utilization environments.

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Our features are to integrate and operate these in "ServiceNow". In enterprise systems, even if vulnerabilities are discovered, it is currently impossible to quickly repair them. Therefore, it is necessary to consider the risk priorities and the timing at which the program is modified to ensure that the modified system will operate normally. We will focus on ServiceNow as a platform that can manage these.

Since then, we have created and proposed an environment that utilizes AI while isolating data within the company, not just from the Internet. The "dailyAI" was released in the third quarter of last year, and the version is gradually being upgraded.

At this point, we will start an in-house demonstration test to upload files contained in each personal computer. At the next stage of dailyAI, we will be able to determine the scope of authority that data users can access and use in a secure environment that is separated from servers connected over the Internet. From April 2024, we plan to develop this service as a formally completed service.

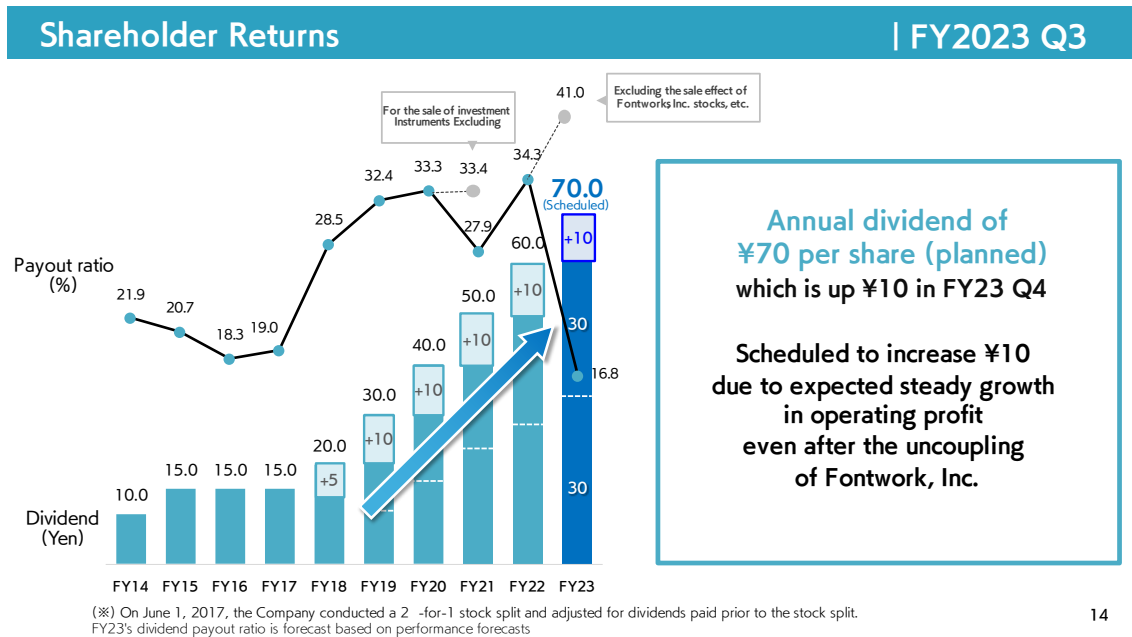
The generation AI has become a very hot topic since around April 2023, but the "useful AI" that we think about is one that allows AI to learn including confidentiality in the company and use it without having to carry it outside. We are now ready to provide such a AI. Since February of this year, we have been carrying out in-house demonstration tests, and we are preparing to provide a fee charging service from April on a certain level of completion.

We would like to explain our business for Public Sector next, but this time we do proposal activities for more than 400 municipalities in addition to the Central Ministry from late January to March. Therefore, we would like to refrain from commenting on this matter and report that the system is operating smoothly at present.

I would like to report that "this was the result of such orders" during this fiscal year's end in April. The above is the progress of the medium-term management plan. We have yet to find a flashy idea, but we expect that we will be able to do some sort of feeding that would cause flowers to open in the next fiscal year, which is the third year.

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Shareholder Returns



It's Shareholder returns. Our basic policy is to return the profit growth of our business to our shareholders as dividends. In addition, I would like to explain that the funds obtained from the sale of Fontworks, Inc., and other equities would be used to invest for the next growth.

In the current fiscal year, I felt that operating income grew even after excluding the impact of Fontworks, Inc. being excluded from consolidation. Therefore, we plan to increase the dividend by ¥10, the same as in the past four years.

The most recent dividend payout ratio range from 33% to 34%. This term is assumed to be 41%, excluding the impact of sale of Fontworks, Inc. `stocks, etc.

Disclaimer:

This is an English translation of the captioned release. This translation is prepared and provided for the purpose of the reader's convenience. All readers are recommended to refer to the original version in Japanese of the release for complete information.