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SB Technology Corp.
Overview of Earnings Results Briefing for FY2021 Q3

This is a transcript of the SB Technology Corp. FY 2021 Q3 Results Briefing held on January 27, 2022.
Speaker: Mr. Shinichi Ata, President & CEO, SB Technology Corp.

SB Technology, Operating Income up +48%

Operating income is expected to double in three years, and dividend forecasts are also revised upward.

Financial Results for the Third Quarter of the Fiscal Year Ending March 2022

Shinichi Ata: Hello everyone. I am Shinichi Ata, the representative director and president of SB Technology. Thank you very much for attending our financial results briefing today at such a busy time.

Today, I would like to explain the outline and outlook of our performance and the direction of our next medium-term business plan. After that, we will accept questions from you. Thank you very much.

Information1

Thanks to these efforts, from April 4, 2022, we will shift to a prime market listed company. Going forward, we will further strengthen governance in order to meet the expectations of our stakeholders, with the aim of achieving sustainable growth and increasing corporate value over the medium to long term. There are still some Explain items at present, but by the next general meeting of the stockholder held in June, I think many parts will be eliminated except for some.

Information2

This is the information I have already informed you of, and we have been appointed Yukari Tominaga and Yuka Miyagawa as our advisors since July. In addition to this, Mr. Madoka Sawa has participated since January, and a total of three people have become our advisors. Regarding the former two people, from July we have participated in our monthly board of directors, and we have received a quarterly business review and received various advice.

Regarding Mr. Madoka Sawa, we have also been participating in board meetings since this month.
The three members will be informed of the situation of having received an internal approval as a director candidate.

Results Summary

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An overview of business results. Regarding the financial results summary, we were able to achieve record highs in all indicators, including net sales and operating income, thanks to DX support from government agencies and private companies. In terms of orders received, orders in the manufacturing industry, in addition to public and Softbank, have been recovering, and we were able to achieve record high orders and order backlog in the third quarter.

As for the outlook for the full fiscal year, we were able to reduce costs by strengthening cost control of projects, and we have revised our operating income upward to ¥5 billion.

Premise for this briefing material

The graph on the slide shows sales trends for the past 10 years. The grayed-out segment is the amount of EC purchases that had been recorded as sales under the previous accounting standard. As a result of the adoption of the new revenue recognition standard, for example, the portion that was ¥17.9 billion in the previous fiscal year is set at zero in the current fiscal year.

Therefore, in the blue part, we would like to see changes in sales for 10 years under the same assumption as this fiscal year. The forecast for the current fiscal year is ¥65 billion.

Consolidated PL (April-December cumulative)

Progress up to the third quarter. Net sales were approximately ¥47.6 billion, an increase of approximately ¥11.783 billion, or 33% year on year. Operating income was ¥3.66 billion, an increase of ¥1.187 billion, or 48% through the third quarter. Ordinary income and quarterly net income are shown in the slides.

Impact of change in accounting standards (net sales)

I will explain the bridges for sales. Last year's net sales were approximately 49 billion yen, which is the figure for the settlement of accounts up to the third quarter before the change in accounting standards. Approximately ¥13.2 billion is negative due to the impact of the new revenue recognition standard, and approximately ¥35.8 billion is the adjusted figure for last year. Adding this to the ¥790 million sales of the three subsidiaries in the first quarter, which had not started last year, we are bridged to about ¥47.6 billion as an increase of about ¥11 billion.

Solution classification

Changes in sales by solution category. From the bottom of the slide chart, EC is in a flat form. Technical Solutions ranges from ¥16.8 billion to ¥21.6 billion, and cloud-based sales, such as Business IT and Corporate IT, from ¥15.9 billion to ¥22.9 billion. The current composition ratio is 48.2%.

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Our goal is to exceed 50%, and we expect this composition ratio to increase in the fourth quarter.

In terms of marginal income, technical solutions increased from ¥4.8 billion to ¥5.9 billion, while Business IT and Corporate IT increased from ¥6.5 billion to ¥8.1 billion. The area of EC is high margin, but it remains flat at ¥2.3 billion. I think it looks big in terms of profit margin because the profit standard has changed.

Sales by Customer Type

Sales by customer. The yellow portion of the bar chart on the left side of the slide shows Softbank Group sales ranging from 17.2 billion yen to 22.5 billion yen. The blue part is for Enterprise/Public sales, from 17.1 billion to 23.6 billion.

Breakdown by Softbank Group: In Technical Solutions, due to the expansion of the scope of Softbank projects, this has also grown from ¥12.8 billion to ¥17.2 billion. Cloud-related items also increased from 4.1 billion yen to 5 billion yen, an increase of about 20 percent.

Regarding the Enterprise/Public on the right side of the slide, what kind of project was able to extend is indicated on the top. We were also able to greatly increase sales from 11.8 billion yen to 17.9 billion yen.

Factors Behind Changes in Operating Income

This is a bridge to operating profit. Operating income up to the third quarter of last year was 2.47 billion yen, plus the marginal profit of 2.71 billion yen. Regarding fixed costs, personnel expenses for 52 employees have increased, so the figure, including the increase in such personnel expenses, is 1.03 billion yen.

The increase in the allowance for losses is 490 million yen. I think this was explained in the same way in the second quarter, but it is known in the digital map project. Including all of the estimated losses in the fourth quarter, the provision is 490 million yen, but it is within the plan when the business results were revised in the second quarter and is controllable. As a result, operating income was ¥3.66 billion.

[Non-Consolidated] Orders Received/Order Backlog （ Excluding EC services）

In this fiscal year's results outlook, the left-hand side of the slide shows the trend in orders received from quarter to quarter. In this third quarter, we were able to win a new order for 11 billion yen.
As a result, the order backlog at the end of December 2021 was 23.6 billion yen.

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More than half of this amount, more than ¥12 billion, is expected to be sales for the fiscal year under review. I think that the remaining portion of the more than 11 billion yen is expected to be sold after the next fiscal year. We were also able to increase orders by 30% or more.

Revision to Full-Year Financial Results Forecasts

Correction of performance forecast. Last year's sales were 52.5 billion yen, but this year's sales will be 65 billion yen. The initial forecast was 59 billion yen, but the price was 65 billion yen as we maintained what we talked about in the second quarter.

As I mentioned in the highlights above, operating profit has increased due to tighter management of costs. There are many projects that will be delivered in March, but as a result of packing the costs, the number has increased slightly. The initial target was 4.3 billion yen, and the previous forecast was 4.6 billion yen, but this time we have revised it upward to 5 billion yen.

Below Ordinary Income is as shown on the slide.

Shareholder Returns

Shareholder return. The graph on the slide shows the dividend amount for the past few years, but this year it is expected to reach 5 billion yen. We plan to increase the year-end dividend by ¥10 to ¥30. Since we are paying 20 yen in the first half of the fiscal year, we plan to pay an annual dividend of 50 yen.

Third Medium-Term Management Plan/ FY21 Management Indicators

This is an indicator for the Third Medium-Term Business Plan. The goal set three years ago was to increase operating income to a CAGR20 percentage. At that time, it was 2.5 billion yen, but we set a target of 4.3 billion yen again, and this time we are predicting it at 5 billion yen. By chance, we expect to achieve our operating profit target just twice that of the time.

As for BIT, CIT, which is our strategic business area, we currently account for more than 48% of our total sales. However, as this will accumulate in the fourth quarter of the fiscal year, we believe that it will exceed 50%. ROE has already been achieved in the previous fiscal year, and we are aiming to achieve the same level. The third medium-term management plan is expected to be largely achieved.

Environmental Initiatives at the Time of Formulation of the Third Medium-Term Management Plan (FY18)

Next, the fourth medium-term management plan. As for the perfectly determined one, we would like to report it at the time of the announcement of the settlement in April, but I would like to talk a little

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about the direction.

The story may go back a little, but the topic of restructuring the Tokyo Stock Exchange was rising when the Third Medium-Term Management Plan was formulated. In terms of standards, various stories emerged, such as a market capitalization of ¥50 billion or more, or ¥100 billion, and a sales scale of ¥50 billion. I remember that the situation at that time was that we announced in the spring of 2019 in order to eventually apply it in April 2021.

To this end, we considered it necessary to increase our corporate value in order to remain firmly in the Prime Market. As a background to this, in 2018 the parent company transitioned from SoftBank Group International LLC to SoftBank Corp. At this point, we shifted from a holding company to an operating company, so we needed to create synergies with SoftBank Corp.

In addition to increasing sales and earnings, we also chose vendor management projects in order to make SB technology a seed for further growth in the future. Softbank Corp. already manages and standardizes the partners it serves, at our discretion.

Compared to the number of partners we have been involved in, we have decided to store an overwhelmingly large number of partners. In addition, by storing large-scale partners, we have an increasing number of partner options that support our business. In addition, amid a growing number of 5G stories, we became a consolidated subsidiary of telecom companies, the major source of 5G. We believe that synergies from the collaboration of leading-edge cases will lead to development in the direction of external sales that we are aiming for.

Another background at that time was a new accounting standard. In other words, they were asked to respond to the new revenue recognition standard. At the time, we had sales of about 50 billion yen, and we were in the midst of making our sales mix more SI from product sales.

As EC businesses continue to grow in the future, they will be presented on a net basis, which will have a negative impact of approximately ¥17 billion on net sales at the time, and will be recognized as net sales of ¥33 billion.

If the Prime Market benchmark was to be ¥50 billion, one of the challenges was that if we did not add ¥20 billion within the next two years, we would drop below ¥50 billion upon adoption.

Third, as SI (System Integration) was progressing steadily, it became clear that it would be quite difficult for SI alone to generate profits. In addition, there was a debate about the need to expand

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services. This was amid the trend toward a shift from ownership to use. Three years have passed since the Third Medium Account, with the goal of achieving all of this goal, or to make it possible to achieve the goal.

With a View to 2030

At that time, nearly 1000 employees were working, but almost all of them participated in a company-wide workshop on what happened in 2030, and what we should focus on to make SB technology a society-friendly company.

We also carried out analyses for our customers. Nevertheless, within one year, new Corona Viruses were generated, and in these two years they were in Corona flaws, so there were parts that were largely different from the expectations.

Engineers in the Information Systems Division are now in the business IT domain, and the business IT solution is becoming increasingly advanced. But with the spread of the new coronaviruses, the engineers are returned to IT department, and they are spending hours preparing for remote work and talking into the security zone, and this situation is still ongoing.

Even so, it was very fortunate that we were able to extend BIT sector. We recognize the evolution to service providers set forth in the Third Medium-Term Plan and the creation of consulting & business IT, which we still believe to have a certain level of response, as well.

Toward Improving Profitability1

We are considering the goal of improving profitability as a theme for the next medium-term plan. We also receive information from investors. In reality, although profits have been rising, the operating income margin, which was about 8% 10 years ago, has remained almost unchanged and sales have expanded, we do not think this situation is good.

The companies we compare range from 10% to around 15% operating margin. Of course, we are aware that not only SI (System Integrator) but also some of our services or our own products. However, we believe that we must have highly profitable services as soon as possible.

Toward Improving Profitability2

We should add actual results from various perspectives regarding the next medium-term calculation. Today, however, we would like to explain several topics from SB Technology alone.

Regarding SI, we see that "Support for cloud-based promotion of customers' DX" will continue.

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The term DX may also become worn out over time, but I believe that this part will continue as it has progressed in earnest over the past year to two years.

In addition, we may end this Coronal flaw. However, since the manufacturing industry has recovered considerably in terms of both budgetary and business terms, we believe that we need to further refine and propose IT consulting.

We currently have about 10 consultants. It is also said to be a qualification CBAP for a consultant. Approximately 50 people have passed it. In addition, we will refine the points of loading carriers and actually how we can provide consultation using our cloud and security technologies.

On the other hand, we must build a development system that can improve profitability, such as by providing standardization and solutions. I think that the style of continuing to make things that can fit only specific customers will be ineffective. In addition, to "strengthen checking functions and systems to reduce unprofitable projects," we recently created a system to assist PM and introduced a mechanism to support and check actual project managers, mainly for PM of young employees. In the next term, we would like to be able to move this more fully.

For the services, slide shows "providing security measures and services requiring advanced expertise." The service name is "MSS (Managed Security Service)" and the local government information SC (Security Cloud). First, we were able to receive orders from local governments in ten prefectures. This is a service type for a long time. The greatest value of a municipal intelligence SC ever developed was when it became operational. It was, of course, depreciated from there to reduce its value.

Since the evolution of technology will be as much as 10 times in five years, it will be a tenth of the power in five years when it is operated in the same system. Based on this style, we would like to convert to a form of further refinement of services that do not depreciate by using clouds, as in the case of the "price-increasing accumulation type" in our recent story. Also, we would like to make the way we provide this service our direction.

Another is the electronic application service provided by the Ministry of Agriculture, Forestry and Fisheries, as we introduced last time. I would like to digitize what I used to apply for in paper, but the Ministry of Agriculture, Forestry and Fisheries has about 4000 such applications. So, the way we used to digitize is to create a cloud-based platform, and the actual application, or each and every procedure, is to be created by the staff within the province. Even those who have never done IT or programming, such as LowCode development or NoCode development, can see this.

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As a result, we have been able to train over 3600 staff members by last year under the collaboration of our group company, Kan, and we have over 1200 applications that we have created by ourselves, making a total of 4000 applications.

The government's policy is to digitize most of them by 2025. There are three to four years later, but there are some sort of plans to shift to that time.　Probably, how to make such an application will be a measure in the future.　I believe that IT experts like ours will take on a heavy role and will provide a platform that allows people on the front lines to learn from themselves and create applications more easily.　I would like to proceed with the medium-term management plan that anticipates these two things.

The slide's "redefinition of services for the hard-to-differentiate use of clouds" means that anything that needs SE must be no longer straightforward.　Otherwise, we must expand as a service in the future.　Furthermore, we are reviewing our "sales expansion system through sales partners."

Finally, EC part of the contract will be continued due to a change in NortonLifeLock's policy, but in the future we will only deal with the Auto Renewal portion.　This means that we will only perform automatic updates, not just new acquisition campaigns and other activities that we have been involved in up to now.　As a result, we are likely to see a decline in profits from ¥300 million to ¥400 million in the next fiscal year. However, as we have not changed our thinking about formulating the plan for the next fiscal year due to increases in sales and profits as a whole, I would like to report this once again.

Now let me finish the explanation.　Thank you for your attention.