Transcript of results briefing
Consolidated Financial Results for 2nd Quarter of Fiscal Year Ending March 2021

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■ Greeting

Greetings, my name is Yasuhiko Oka, and I am a senior executive officer of SCSK Corporation.

■ Contents (slide1)

The agenda for today's presentation can be seen in the contents section on slide 1. I will be discussing the Company's consolidated financial results in the six-month period ended September 30, 2020.

■ Summary of Financial Results（PL/Incoming Orders/Backlog）(slide2)

Please look at slide 2, which displays consolidated performance highlights for the six-month period ended September 30, 2020.

Net sales were ¥189.7 billion, up 1.3% year on year.
Operating profit was ¥21.2 billion, up 4.0%. The operating profit margin was 11.2%.
Profit attributable to owners of parent was ¥14.8 billion, up 2.5%.

I will offer a breakdown of performance by sales segment later on. On a consolidated basis, net sales rose by approximately ¥2.5 billion as we were able to compensate for the decline in packaged software / hardware sales with contributions from the newly consolidated Minori Solutions Co., Ltd., as well as the increase in systems development and system maintenance and operation / services sales.

Gross profit increased thanks to higher sales, lower unprofitable projects, and the profit-boosting effect of recording a provision for performance bonuses on March 31, 2020, and the gross profit margin was 25.8% accordingly.

Selling, general and administrative (SG&A) expenses rose ¥1.0 billion. Factors behind this increase in expenses included a rise in personnel expenses following an influx of new graduates and mid-career hires and revisions to compensation systems from July 2020 which instituted in conjunction with the introduction of new human resource systems as part of the human resource investment strategies delineated in the new medium-term management plan. Another factor was the expenses incorporated through the consolidation of Minori Solutions. These higher expenses outweighed the reductions in expenses stemming from the recording of a provision for performance bonuses on March 31, 2020, and the lower incidental expenses for business trips and entertainment, which were curtailed due to the COVID-19 pandemic.

These factors resulted in a year-on-year increase of 4.0%, or approximately ¥0.8 billion, in operating profit, to ¥21.2 billion.

Next, I would like to discuss incoming orders and order backlog in the six-month period ended

March 31, 2020.

We will also look at order trends by sales segment later on. In the meantime, consolidated incoming orders were up 0.2%, to ¥179.9 billion.

Just like net sales, incoming orders were impacted by the rebound from previously recorded packaged software / hardware sales, and the amount of this impact was nearly ¥7.0 billion. Conversely, orders for systems development and system maintenance and operation / services took an upswing from the year-on-year decline of ¥3.8 billion seen in first quarter of the fiscal year.

Similar to incoming orders, order backlog was impacted by the decline in packaged software / hardware sales while still growing at a rate of 5.7%, which exceeded that rate of increase in 2.1% posted on June 30, 2020, to ¥137.3 billion, due to the rise in systems development and system maintenance and operation / services.

Furthermore, in the six-month period ended September 30, 2020, Minori Solutions contributed ¥7.6 billion to net sales, ¥0.3 billion to operating profit, ¥6.7 billion to incoming orders, and ¥4.3 billion to order backlog.

■ Summary of Financial Results for the Three-Month Period Ended Sep. 30, 2020 （PL/Incoming Orders/Backlog） (slide3)

Moving on to slide 3, this slide provides an overview of performance in the second quarter of the fiscal year ending March 31, 2020.

As shown on this slide, net sales in the second quarter declined 0.6%, to ¥95.3 billion, and operating profit was down ¥8.8 billion, to ¥10.9 billion.

Second-quarter net sales were down by roughly ¥0.5 billion.

Packaged software / hardware sales decreased ¥3.3 billion primarily due to the rebound from previously recorded network equipment sales to the communications industry. Meanwhile, systems development and system maintenance and operation / services sales were up, but this increase was unable to compensate for the decline in network equipment sales.

Second-quarter operating profit was down ¥1.0 billion due to decline in gross profit stemming from lower net sales as well as to the increase in SG&A expenses, which was primarily associated with higher personnel expenses, as I discussed with regard to the six-month net sales.

Incoming orders in the second quarter rose 4.5%, or ¥4.1 billion, to ¥96.1 billion, an upswing from the decrease of 4.4%, or ¥3.8 billion, in the first quarter. This rise was primarily a result of a ¥6.0 billion increase in systems development and system maintenance and operation / services orders, which offset the ¥2.0 billion decrease in packaged software / hardware sales that was largely due to the rebound from network equipment sales orders from the communications industry that also impacted the first quarter.

■ Comparison by Sales Segment （Sales/Incoming Orders/Backlog） (slide4)

Systems Development

Please look next at slide 4, which displays performance by sales segment.

In the Systems Development segment, net sales increased 2.9%, to ¥78.4 billion. This increase was achieved thanks to demand for electrical machinery core systems redevelopment projects and to manufacturing industry demand for next-generation systems development from food product manufacturers and for strategic business investment by automobile manufacturers. This demand offset the rebound from previously recorded orders from the banking and power industries.

Incoming orders were up 4.1% year on year, to ¥80.2 billion. Although we felt the impacts of the rebound from previously recorded large-scale orders from the securities industry, an overall increase in orders was achieved by concluding contracts with regard to subsequent phases of core systems redevelopment projects that are previously underway for the distribution industry.

Order backlog rose 7.0% year on year, to ¥38.1 billion, due to the same factors that impacted incoming orders.

■ Comparison by Sales Segment（Sales/Incoming Orders/Backlog）(slide5)
System Maintenance and Operation/Services

Please turn now to slide 5.

Net sales in the System Maintenance and Operation / Services segment increased 6.4% year on year, to ¥74.5 billion, due to the strong performance of managed services for the manufacturing and financial industries and of data center and business process outsourcing businesses.

Incoming orders were up 7.2% year on year, to ¥64.9 billion, because of higher orders in data center businesses targeting the service industry and in business process outsourcing businesses, which offset a decrease in verification service orders from the manufacturing industry.

Order backlog was impacted by the same factors that affected incoming orders, rising 6.8%, to ¥83.5 billion.

■ Comparison by Sales Segment（Sales/Incoming Orders/Backlog）(slide6)
Packaged Software/Hardware Sales

We will look next at the Packaged Software / Hardware Sales segment on slide 6.

Net sales decreased 10.2% year on year, to ¥36.7 billion. Although sales of hardware for academic research institutions were up, this increase was outweighed by impacts of the shift to next-generation models for certain products in sales of network equipment to the communications industry as well as the rebound from previously recorded large-scale hardware sales to automobile manufacturers.

Incoming orders decreased 17.2% year on year, to ¥34.6 billion, as the conditions that impacted sales of network equipment to the communications industry also affected orders and because of a decrease in orders for hardware from academic research institutions.

Order backlog was down 2.5% year on year, to ¥15.5 billion, due to declines in large-scale hardware orders from automobile manufacturers and in hardware orders from academic research institutions.

With this, I conclude this explanation of performance by sales segment.

■ Sales Comparison by Customer Industry (slide7)

We will next look at sales by customer industry.

In the six-month period ended September 30, 2020, sales were up or unchanged year on year for all customer industries with the exception of the communications and transportation industries. Sales to the communications decreased as a result of the aforementioned impacts of trends in sales of network equipment to this industry.

I would now like to take a moment to explain the primary reasons behind the increase in sales to the manufacturing, distribution, financial, and service industries.

Sales to the manufacturing industry rose ¥3.0 billion year on year. This sales growth was a result of systems development projects acquired thanks to demand for strategic IT investment demand from automobile manufacturers coupled with investment demand from precision equipment manufacturers and system upgrade demand from food product and electrical machinery manufacturers.

Sales to the distribution industry were up due to demand for developing next-generation systems and core system redevelopment projects, increases in sales of network and security products following growth in demand for remote work applications.

Sales to financial institutions rose, despite the rebound from previously recorded systems development sales, as a result of increases in system maintenance and operation / services sales stemming from higher demand for managed services and in data center businesses as projects advanced past the systems development phase and on to the maintenance phase.

Sales to the service industry and other customers were up due to large-scale hardware sales to academic research institutions and increased performance in data center businesses.

■ Business Performance by Reportable Segment (slide8)

Next, I would now like to discuss performance by reportable segment.

Today, I will be focusing specifically on the Industrial IT Business segment, which represents a particularly large portion of total net sales; the Financial IT Business segment, which posted operating profit in line with the previous equivalent period despite a decrease in sales, and the IT Platform Solutions segment, which saw a decrease in net sales but an increase in operating profit.

In the Industrial IT Business segment, net sales were up due to increases in systems development sales to the automotive and food product industries, which offset the decreases from the absence of previously recorded systems development orders for the power industry and a one-time rise in hardware sales demand. Operating profit also rose due to higher sales coupled with the benefits of the absence of the unprofitable projects that detracted from profit in the previous equivalent period.

The Financial IT Business segment suffered a decline in net sales following the conclusion of multiple systems development projects for the banking industry and the fact that such projects have been declining since they peaked. Operating profit, meanwhile, was relatively unchanged year on year as certain unprofitable projects that took place in the previous equivalent period have ended.

As for the IT Platform Solutions segment, net sales were down primarily as a result of the shift to next-generation models for certain products in sales of network equipment to the communications industry. However, these products had relatively low profit margins to begin with, a fact that, combined with the increase in sales of other products and the higher earnings from product maintenance services, resulted in a rise in operating profit.

■ Operating Profit Analysis (slide9)

Looking now at slide 9, I would like to offer an explanation of the factors that influenced operating profit.

The rise in net sales boosted operating profit by ¥0.6 billion while the improved gross profit margin raised operating profit by ¥1.2 billion.

In the six-month period ended September 30, 2020, losses from unprofitable projects were nearly ¥0.1 billion. Losses from such projects in the previous equivalent period, were over ¥0.5 billion. This difference led to a year-on-year increase of almost ¥0.5 billion in operating profit.

Meanwhile, SG&A expenses rose ¥1.0 billion. One factor behind this rise was a net increase of ¥0.4 billion in personnel expenses stemming from the combined effect of the expenses associated with the influx of new employees and the transition to new human resource systems and the reduction in expenses from recording provisions for performance bonuses on March 31, 2020. Other factors included expenses associated with the consolidation of Minori Solutions and the amortization of intangible assets connected to this acquisition. These factors outweighed the reduction in entertainment, travel, and other expenses that stemmed from the COVID-19 pandemic.

The combined impact of these factors was a year-on-year increase of approximately ¥0.8 billion in operating profit, which came to ¥21.2 billion, and a rise in the operating profit margin from 10.9% to 11.2%.

■ Consolidated Financial Forecasts (slide10)

Moving on, I would like to discuss our performance forecasts.

The initially projected rebound from previously recorded network equipment and other sales was more or less as expected in the six-month period ended September 30, 2020. Meanwhile, the newly consolidated Minori Solutions contributed to performance; sales of systems development and system maintenance and operation / services were up; and productivity did not decline significantly. We have thus judged that performance was slightly better than had been initially anticipated.

However, there is currently no sign of the end of the global COVID-19 pandemic. Although IT investment trends are recovering, we cannot deny that conditions are remaining weak and opaque as a result of the ongoing pandemic.

We have therefore chosen not to revise the previously announced forecasts for the fiscal year ending March 31, 2021, of net sales of ¥380.0 billion, operating profit of ¥41.0 billion, and profit attributable to owners of parent of ¥29.0 billion.

Nevertheless, we are committed to pursuing performance that exceeds these forecasts, as was stated by President Tanihara.

As for the interim dividend, as shown on this slide, we intend to issue an ordinary dividend of ¥65 per share, the same amount as the interim dividend from the previous fiscal year when combining the ordinary dividend of ¥55 per share with the commemorative dividend of ¥10 per share issued in commemoration of the 50th anniversary of SCSK’s founding.

This concludes my presentation. SCSK looks forward to your ongoing support and encouragement.