Transcript of results briefing
Consolidated Financial Results for Fiscal Year Ended March 2022 and Financial Forecasts for Fiscal Year Ending March 2023

Yasuhiko Oka
Managing Executive Officer, SCSK Corporation

■ Contents (slide 1)

Greetings, my name is Yasuhiko Oka.
So now, let me start today's presentation along the agenda on page 1.

■ Summary of Financial Results (PL/Incoming Orders/Backlog) (slide 2)

Please look at slide 2, which displays consolidated performance highlights.

As shown on this slide, in the fiscal year ended March 31, 2022, SCSK Corporation posted net sales of ¥414.1 billion, an increase of 4.4% year on year; operating profit of ¥47.5 billion, an increase of 3.7% and profit attributable to owners of parent of ¥33.4 billion, an increase of 0.1%.
As stated by President Takaaki Touma, we set new record highs for net sales and operating profit, effectively making for our 10th consecutive year of higher sales and profit.

We are currently facing an unprecedented environment, plagued with challenges such as the COVID-19 pandemic and Russia's invasion of Ukraine. The sense of uncertainty from such developments lingered throughout the fiscal year, causing semiconductor shortages, inflation, and other concerns. Meanwhile, the operating environment for SCSK, specifically, was supported by the plans for increased software investment among companies indicated in the Bank of Japan's quarterly economic survey.

In this environment, we fell just short of our initial target of net sales of ¥420.0 billion. Operating profit, meanwhile, was close to our initial target, at ¥47.5 billion as mentioned. We incurred one-time integration costs for merging subsidiaries as well as increased business investment costs in conjunction with the strategies of the medium-term management plan. In addition, downward pressure was placed on performance by loss-making projects. However, we were able to compensate for these negative factors with improvements in productivity and profitability.

The slight growth rate for profit attributable to owners of parent was a result of the low income tax burden in the fiscal year ended March 31, 2021, that stemmed from the application of tax exemptions for wage increases.

As shown on this slide, incoming orders were up 3.6% year on year, to ¥427.9 billion. This increase was seen regardless of the absence of the batch orders for network equipment received from the communications industry in the Packaged Software / Hardware Sales segment during the previous fiscal year. Order backlog also rose, increasing 8.5%, to ¥177.0 billion, as a result of higher orders in all three sales segments.

■ Summary of Financial Results from Jan. to Mar. 2022 (PL/Incoming Orders/Backlog) (slide 3)

Moving on, slide 3, which displays consolidated performance highlights for the three-month period ended March 31, 2022.

In the fourth quarter of the fiscal year ended March 31, 2022, net sales increased 5.1% year on year, to ¥111.3 billion; operating profit was up 7.6%, to ¥12.7 billion; and profit attributable to owners of parent declined 4.6%, to ¥9.2 billion.

Despite the increases in net sales and operating profit, profit attributable to owners of parent was down as a result of the aforementioned application of tax exemptions for wage increases in the previous equivalent period.

There were no significant changes to IT investment demand trends in the fourth quarter of the fiscal year, and strong growth was seen in systems development inquiries of a substantive scale. At the same time, however, the time required to conclude contracts based on these inquiries was longer than we had anticipated.

Due to these factors, we were able to achieve robust performance with a year-on-year increase of 5.1% in fourth-quarter net sales. However, we cannot deny that fourth-quarter net sales were a bit lower than anticipated because of the time lag in concluding contracts in the Systems Development segment. The Packaged Software / Hardware Sales segment, meanwhile, was impacted by the supply restrictions and semiconductor shortages that stemmed from the supply chain disruptions seen amid the COVID-19 pandemic as we entered into the fourth quarter.

As a result, fourth-quarter net sales were lower than anticipated during the third quarter, causing full-year net sales to fall slightly below our initial forecast of ¥420.0 billion.

Gross profit was up 5.0% year on year in the fourth quarter. This outcome was a result of our ability to counteract the impacts of business investment-related expenses and loss-making projects with the benefits of high net sales and a gross profit margin maintained through ongoing efforts to improve development quality and productivity.

At the risk of repeating myself, we incurred business investment-related expenses in line with our initial plans. Another result of this factor was a 3.1% year-on-year increase in selling, general and administrative (SG&A) expenses, to ¥16.1 billion, in the fourth quarter.

Due to the aforementioned factors, fourth-quarter operating profit rose 7.6%, to ¥12.7 billion.

Despite increased orders in the System Maintenance and Operation / Services segment, incoming orders decreased 2.3%, to ¥129.8 billion, in the fourth quarter as a result of the extended amount of time needed to conclude contracts for orders in the Systems Development segment coupled with the absence of the network equipment orders received from the communications industry during the previous equivalent period in the Packaged Software / Hardware Sales segment. Fourth-quarter order backlog showed an increase of 8.5% year on year, to ¥177.0 billion, following backlog growth in all sales segments. The order backlog in the Systems Development segment, specifically, rose 9.3%, to ¥40.6 billion. With these large backlogs, we find ourselves in a steady position going into the fiscal year ending March 31, 2023.

■ Business Performance by Reportable Segment (Sales/Operating Profit/Operating Profit Margin) (slide 4)

Moving on, I would now like to talk about performance by segment in the fiscal year ended March 31, 2022. Please look at slide 4.

The graph on this slide shows segment performance through graphs, with the graph on the top displaying net sales while the graph on the bottom contains information on segment profit and the operating profit margin.

I will be explaining the factors behind changes in net sales and segment profit by segment beginning from the left and working toward the right. Accordingly, we will start with the Industrial IT Business segment.

Net sales in the Industrial IT Business segment rose 2.7%, or ¥3.5 billion, year on year. Performance in this segment benefited from growth in IT investment for strengthening customer contact points in the communications industry, higher demand for strategic investment in the automotive industry, and increased sales of verification services. These benefits outweighed the impacts of the conclusion of systems upgrade projects for the gas industry. Segment profit was up 2.9%, or ¥0.4 billion, despite the impacts of loss-making projects and investment costs for Commercialization of DX.

Next, the Financial IT Business segment posted growth of 7.1%, or ¥3.7 billion, in net sales following upward trends in global core system projects and systems development projects using international calculation packages for banks and in DevOps projects for securities, credit, and leasing companies. Similar to the Industrial IT Business segment, profit in this segment was impacted by loss-making projects, nevertheless the higher net sales enabled the segment to achieving a year-on-year increase in segment profit of 6.6%, or ¥0.4 billion.

I would next like to talk about the IT Business Solutions segment, which is responsible for our enterprise resource planning (ERP), contact center, and business process outsourcing (BPO) operations. This segment saw a slight decrease in segment profit despite an increase in net sales.

Net sales in this segment were up 3.8%, or ¥0.2 billion, year on year due to growth in BPO operations, a result of the transition to business practices prefaced on non-face-to-face and contact-free operations amid the COVID-19 pandemic, as well as the acquisition of ERP development projects from the service and machinery industries. The benefits of these factors counteracted the downturns from the absence of package license sales recorded in the previous fiscal year as well as the conclusion of ERP development projects for the distribution industry.

Segment profit, meanwhile, was at a similar level to the previous fiscal year, down only 0.4%, as a result of upfront investments in base expansion conducted to grow further contact center businesses.

I would now like to look at the IT Platform Solutions segment, which houses our hardware and software sales and maintenance support operations.

The sales of certain new products in this segment were delayed until the fiscal year ending March 31, 2023, as a result of supply limitations stemming from semiconductor shortages and supply chain disruptions. Nevertheless, net sales were up 8.4%, or ¥6.5 billion, and segment profit rose 9.0%, or ¥0.9 billion. These increases can be attributed to strong performance in network equipment sales to the communications industry and large-scale hardware sales to the automotive industry and to academic research institutions.

Let us move on to the IT Management Service segment. This segment is in charge of our data center businesses as well as the supply of cloud infrastructure and management services.

This segment increased in both net sales and segment profit, despite a decrease in platform development projects for the distribution industry, due to ongoing strong performance of data center businesses. These businesses felt the benefits of brisk demand for cloud services as companies continued to shift toward cloud systems and transition existing systems to cloud infrastructure in response to aging hardware and the need to upgrade core systems.

Lastly, let me touch on the Others segment, which houses SCSK Minori Solutions Corporation; Gran Manibus Co., Ltd.; and SCSK Nearshore Systems Corporation. Net sales in this segment declined only slightly, despite the impacts on the hardware sales of SCSK Minori Solutions from the supply chain disruptions seen amid the COVID-19 pandemic.

Segment profit was also down, decreasing in part as a result of one-time expenses for the integration of three subsidiaries to form SCSK Minori Solutions.

■ Business Performance by Reportable Segment (Incoming Orders/Backlog) (slide 5)

On the next slide, we look at incoming orders and order backlog by segment. The graph on the top shows incoming orders while the graph on the bottom displays order backlog.

Looking first at the Industrial IT Business segment, this segment posted year-on-year increases of ¥4.0 billion and ¥2.5 billion in incoming orders and order backlog, respectively, following growth in demand for strategic investments from the automotive industry as well as in orders for verification services.

In the Financial IT Business segment, incoming orders were up ¥7.1 billion while order backlog increased ¥3.7 billion. These increases were attributable to higher DevOps orders from securities, credit, and leasing companies. We also acquired orders for the fiscal year ending March 31, 2023, thanks to robust IT investment demand from banks and securities, credit, and leasing companies as well as international calculation systems development demand.

Incoming orders in the IT Business Solutions segment rose ¥1.3 billion year on year. Although this segment was impacted by the absence of large-scale license sales recorded in the previous fiscal year, overall orders were up as a result of increases in ERP systems development orders and BPO service orders.

Order backlog in this segment increased ¥2.3 billion, as a result of the same factors that affected incoming orders.

Moving on to the IT Platform Solutions segment, incoming orders were up ¥0.7 billion as the increase from the acquisition of large-scale hardware orders from the automotive industry and academic research institutions and from orders for maintenance support services outweighed the decrease from the absence of network equipment orders from the communications industry recorded in the previous fiscal year. Order backlog, meanwhile, rose ¥2.9 billion due to similar trends.

As for the IT Management Service segment, factors impacting orders mirrored those affecting sales, with order growth being seen as a result of demand for cloud services counteracting the rebound from previously recorded platform development orders from the distribution industry. Accordingly, incoming orders and order backlog rose ¥1.7 billion and ¥2.5 billion, respectively.

Lastly, I would like to talk about the Others segment. Incoming orders in this segment were relatively unchanged year on year. Order backlog, however, was impacted by the transference of transactions between SCSK Minori Solutions and certain financial industry customers to the Financial IT Business segment.

With this, I conclude our discussion of SCSK's business performance in the fiscal year ended March 31, 2022.

■ Business Performance by Reportable Segment Analysis (slide 6 to 7)

Slides 6 and 7 offer a summary of the factors affecting segment performance that I just explained. I will not be offering any additional comments on these slides.

■ Consolidated Financial Forecasts/ Dividends Forecasts (slide 8)

Next, we will look at the Company's consolidated performance and dividend forecasts for the fiscal year ending March 31, 2023, on slide 8.

As shown on this slide, in the fiscal year ending March 31, 2023, we project net sales of ¥450.0 billion, an increase of 8.7% year on year; operating profit of ¥54.0 billion, an increase of 13.6% that will make for an operating profit margin of 12.0%; and profit attributable to owners of parent of ¥38.0 billion, an increase of 13.5%.

Looking ahead, the global economy is expected to remain in a state of disarray due to the geopolitical risks stemming from Russia's invasion of Ukraine. Economic growth will also be sluggish in Japan, which will be impacted by rapid yen depreciation and rising commodity prices. Nevertheless, we anticipate ongoing growth in demand for IT investment for promoting digital transformation as a result of the digitization trend, although investments will become more selective and focused on specific areas.

As for business trends in the fiscal year ending March 31, 2023, we are seeing the backlog of systems development orders on March 31, 2022, showed nearly double-digit growth in comparison to March 31, 2021. In addition, we are also witnessing the emergence of investment in ERP systems for enhancing the functions of digital transformation platforms, giving rise to projects of substantive scale. On a solutions basis, trends in inquiries have been brisk, supported by strong demand from the manufacturing and financial industries. These trends indicate that customers are coming to seek out the market-oriented perspective and services of a digital transformation enabler that were included in the business policies presented by President Touma. These developments are expected to contribute to top line growth in the fiscal year ending March 31, 2023.

Trends have also been firm with regard to BPO and verification services, and demand for cloud services is expected to remain brisk, as companies seek to upgrade their systems. These developments will likely continue to support favorable trends in BPO, data center, and other businesses. Furthermore, we have completed the construction of our third data center in Chiba Prefecture, so as we are preparing to develop our business as a cloud service integrator.

As for our platform-related operations, we continue to face concerns in terms of supply. Regardless of these concerns, demand for implementing cloud security measures and reinforcing network environments is strong. And SCSK is taking a product-oriented approach toward addressing environmental issues and contemporary needs in this area.

In light of this operating environment, order backlogs, and the strong trend in inquiries, we are anticipating business conditions that are more favorable than those seen in the fiscal year ended March 31, 2022. Accordingly, we are forecasting net sales of ¥450.0 billion in the fiscal year ending March 31, 2023.

The gross profit margin is expected to rise following higher sales as well as improvements in production capacity and development quality. These improvements will be a result of the benefits of the S-Cred+ platform, which is in the rollout phase, being incorporated into our ongoing initiatives pertaining to the SE+ development standard and of our commencing reforms to our business portfolios.

SG&A expenses are projected to rise ¥4.3 billion in the fiscal year ending March 31, 2023, as we have once again increased the budgeted amount for strategic business investments. However, we should be able to absorb this rise in expenses through increased sales and improved productivity, leading to an operating profit margin of 12.0% and operating profit of ¥54.0 billion.

In regard to dividends, we intend to issue dividend payments of ¥46.67 per share for the fiscal year ended March 31, 2022.

As for the fiscal year ending March 31, 2023, we plan to raise the amount of dividends by ¥5.33 per share in reflection of the aforementioned performance forecasts, which will make for annual dividend payments of ¥52.00 per share, our 11th consecutive year of dividend increases, and a dividend payout ratio that once again exceeds 40%.

Slides 10 and beyond constitute an appendix containing the information on net sales by sales segment and customer industry that we have provided at past financial results briefings. Please feel free to use this appendix as a reference.

This concludes my portion of today’s presentation. SCSK looks forward to your ongoing support and encouragement.

We greatly appreciate you taking the time to join us today.