Walden Research Japan

URL: www.walden.co.jp
Written by Yoshiyuki Muroya, Yusuke Maeda
E-mail: info@walden.co.jp
Phone：+81 3 3553 3769

KAWANISHI HOLDINGS (2689)

Consolidated Fiscal Year (Million Yen)		Sales	Operating Profit	Recurring Profit	Profit Attributable to Owners of Parent	EPS (Yen)	DPS (Yen)	BPS (Yen)
FY06/2016		101,460	543	556	305	54.5	30.0	818.8
FY06/2017		105,778	1,044	1,112	690	123.1	30.0	942.8
FY06/2018CoE		106,377	1,100	1,109	714	127.3	30.0	-
FY06/2017	YoY	4.3%	92.2%	99.8%	125.9%	-	-	-
FY06/2018CoE	YoY	0.6%	5.3%	(0.3%)	3.4%	-	-	-
Consolidated Half Year (Million Yen)		**Sales**	**Operating Profit**	**Recurring Profit**	**Profit Attributable to Owners of Parent**	**EPS (Yen)**	**DPS (Yen)**	**BPS (Yen)**
Q1 to Q2 FY06/2017		53,184	571	590	377	-	-	-
Q3 to Q4 FY06/2017		52,593	473	522	313	-	-	-
Q1 to Q2 FY06/2018		54,563	704	706	595	-	-	-
Q3 to Q4 FY06/2018CoE		51,813	395	402	118	-	-	-
Q1 to Q2 FY06/2018	YoY	2.6%	23.4%	19.6%	57.6%	-	-	-
Q3 to Q4 FY06/2018CoE	YoY	(1.5%)	(16.4%)	(22.9%)	(62.0%)	-	-	-

Source: Company Data, WRJ Calculation

1.0 Executive Summary (23 March 2018)

Launching New Merchandises

KAWANISHI HOLDINGS, selling medical consumables and equipment to medical institutions represented by major base hospitals heavily involved with acute care, is likely to see a long-term growth. Sales of equipment to see short-term volatility are currently adjusting, but sales as a whole for the Company are steadily increasing because of accelerating sales of consumables or the key driver for the growth of the Company. At the same time, operating profit margin is on the rise due partly to improving efficiency of business operations in line with successful changes of organizational structure. Meanwhile, the Company reveals that it is so keen on beefing up sales of consumables and equipment going forward. At the moment, the Company is launching new merchandises based on an existing scheme, successfully driving sales of consumables, while it is to shortly see emerging sales of equipment stemming from launch of new merchandises based on a new scheme to be involved with distribution of merchandises more than now. Specifically, the Company is on the verge of selling medical simulator robot as the general distributor to exclusively sell them in Japan, which is to carry gross profit margin higher than now. As an integrated medical trader with competitive distribution capability, the Company has been aggressively propelling its operations on so-called “manufacturer-&-seller-driven medical-engineering cooperation”, trying to get increasingly involved with direct procurement and distribution of epoch-making new merchandises developed by start-ups. Going forward, the Company is to keep on launching all those new merchandises based on a new scheme, while particularly looking to emerging benefits associated with system and kit to detect breast cancer at early stage in FY06/2020, i.e., the last year of midterm management plan (FY06/2018 to FY06/2020).

In Q1 to Q2 FY06/2018, sales came in at ¥54,563m (up 2.6% YoY), operating profit ¥704m (up 23.4%) and operating profit margin 1.29% (up 0.22% points). By business segment, Medical Consumables and Equipment to sell medical consumables and equipment saw sales of ¥45,454m (up 1.7%), operating profit of ¥744m (up 25.5%) and operating profit margin of 1.64% (up 0.31% points), having accounted for 83.3% of sales as a whole for the Company and 91.5% of operating profit (before elimination). Thus, business performance as a whole for the Company hinges on those of this business segment to a large extent. In regards to consumables to be estimated to have accounted for some 85% of sales in Medical Consumables and Equipment, the Company saw increases rather larger than before, while sales of equipment (remaining 15%) came down, i.e., up 6.7% over the same period in the previous year for consumables and down 11.7% for equipment. For example, the Company suggests that sales of consumables were driven by increasing sales of expensive new merchandises called “frozen balloon” in regards to catheter ablation (circulatory-organ consumables to cauterize myocardial tissue causing tachycardia to make the heart pulse fast by means of high frequency). Meanwhile, sales of equipment unavoidably suffered from non-reappearance of large-scale special procurement project to have materialized year-on-year increases of sales by 42.2% for equipment during the same period in the previous year. Said project was large in sales and carried high gross profit margin at the same time, having resulted in gross profit margin rather coming down as a whole for the Company. Still, this was more than compensated for by the Company’s measure to well control SG&A expenses, having resulted in operating profit margin rather going up.

FY06/2018 initial Company forecasts have remained unchanged, going for prospective sales of ¥106,377m (up 0.6% YoY), operating profit of ¥1,100m (up 5.3%) and operating profit margin of 1.03% (up 0.05% points). Assumptions of initial Company forecasts were exceeded in above-mentioned Q1 to Q2 results, but the Company remains conservative on its full-year forecasts, given uncertainties on NHI price revision to be implemented in April 2018 and an issue that some expenses were delayed in Q1 to Q2, as far as we could gather. Meanwhile, the Company, advocating stability for its dividend, paid annual dividend of ¥30.0 per share, implying payout ratio of 55.1%, in FY06/2016, which was followed by ¥30.0 per share, implying payout ratio of 24.4%, in FY06/2017, while again going for ¥30.0 per share, implying payout ratio of 23.6%, in FY06/2018 with initial Company forecasts. Still, the Company also advocates target payout ratio of 30% at the same time, suggesting that it should consider increases of dividend when payout ratio less than 30% persists. Thus, it could be the case, eventually, that dividend being raised over the previous year in FY06/2018.

IR representative: Managing Director, Nobuharu Murata (+81 86 236 1115 murata2@kawanishi-md.co.jp)

2.0 Company Profile

One of the largest Integrated Medical Traders

Company Name	KAWANISHI HOLDINGS, INC. Website IR Information Share Price (Japanese)
Established	2 October 1967 (inaugurated on 1 May 1921)
Listing	21 December 2000: Tokyo Stock Exchange 2nd section (Ticker: 2689)
Capital	¥ 607 m (As of the end of December 2017)
No. of Shares	6,250,000 shares, including 639,347 treasury shares (As of the end of Dec. 2017)
Main Features	● Set up by mergers among three wholesale distributors of medical equipment and medical materials based in Chugoku and Shikoku regions ● Expectations for new mergers preceded by Sansei Medical Materials Co., Ltd. ● In the pursuit of high gross profit margin in Imports and Sales, etc.
Business Segments	Ⅰ. Medical Consumables and Equipment Ⅱ. SPD Ⅲ. Care Supplies Ⅳ. Imports and Sales
Top Management	President COO: Yohei Maeshima
Shareholders	MASP Inc. 15.1%, Treasury shares 10.2%, ESOP 6.1% (As of the end of Dec. 2017)
Headquarters	Kita-ku, Okayama-city, Okayama-prefecture, JAPAN
No. of Employees	Consolidated: 1,158, Unconsolidated: 31 (As of the end of December 2017)

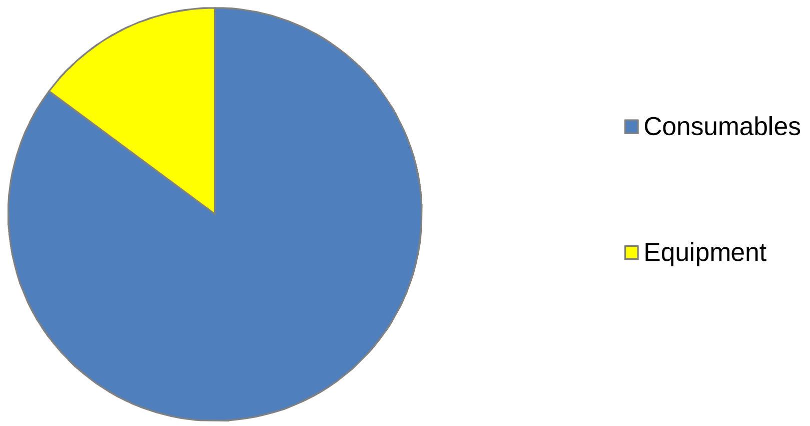
Source: Company Data

3.0 Recent Trading and Prospects

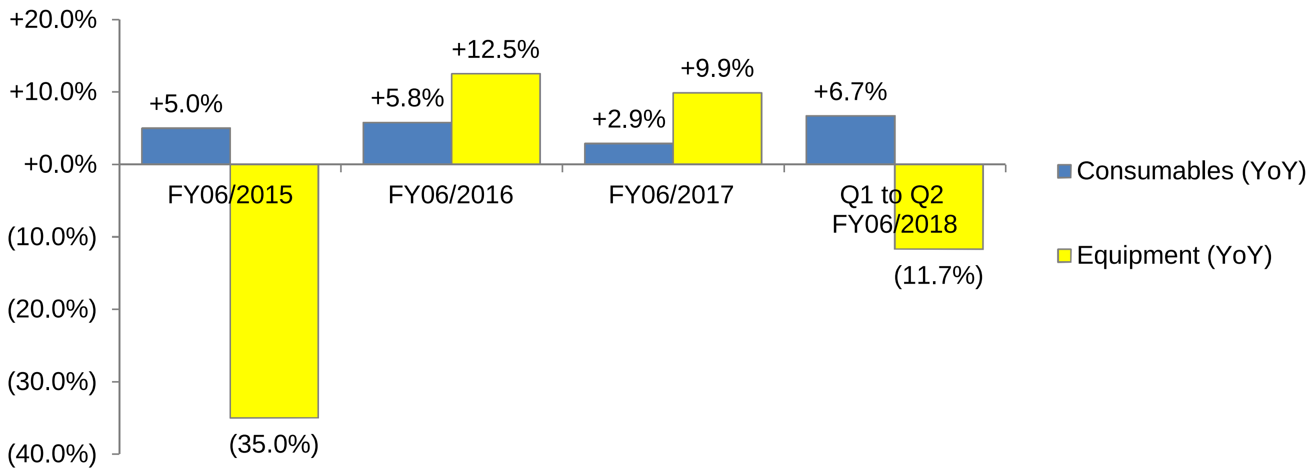
Q1 to Q2 FY06/2018 Results

In Q1 to Q2 FY06/2018, sales came in at ¥54,563m (up 2.6% YoY), operating profit ¥704m (up 23.4%), recurring profit ¥706m (up 19.6%) and profit attributable to owners of parent ¥595m (up 57.6%), while operating profit margin 1.29% (up 0.22% points). The results were better than initially expected by ¥773m (1.4%) in sales, by ¥235m (50.3%) in operating profit, by ¥234m (49.7%) in recurring profit and by ¥286m (92.8%) in profit attributable to owners of parent.

Sales of Medical Consumables and Equipment (Q1 to Q2 FY06/2018)



Medical Consumables and Equipment : Changes of Sales for Consumables and Equipment



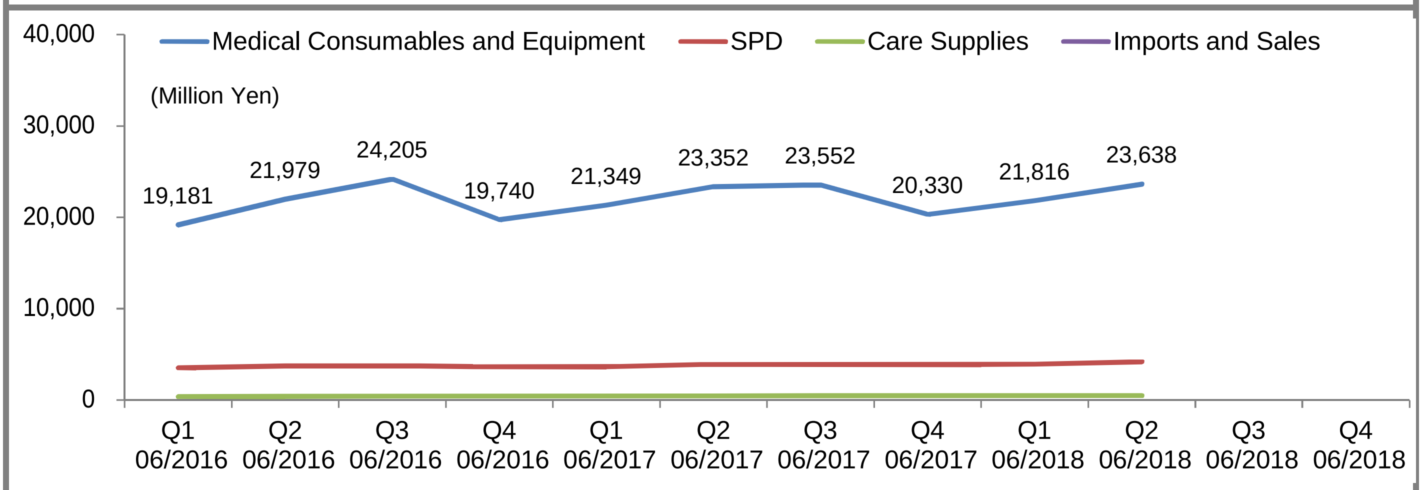
Source: Company Data, WRJ Calculation

The Company is running operations to sell medical consumables and equipment to medical institutions represented by major base hospitals heavily involved with acute care in Medical Consumables and Equipment to drive sales and earnings as a whole for the Company.

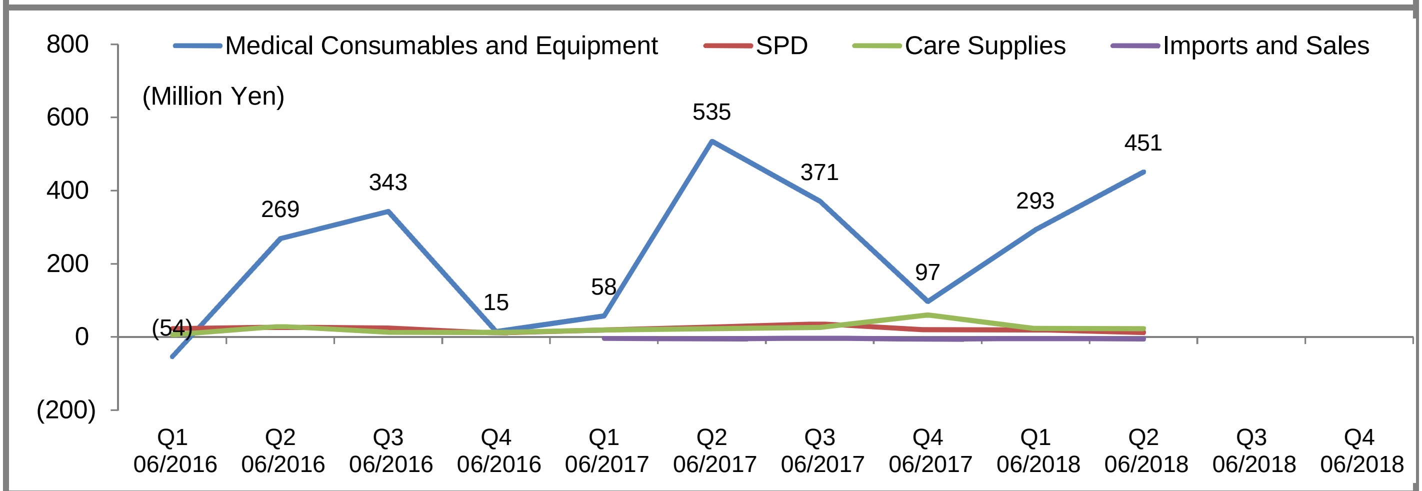
As far as the mainstay consumables are concerned, the Company deals in wide variety of merchandises, while sales are stably and always increasing both in a short-term view and in a long-term view, basically in line with said trends of everyday medical care, e.g. surgery, etc. Still, in Q1 to Q2, the Company saw sales having increased by 6.7% over the same period in the previous year versus by 5.0% in FY06/2015, by 5.8% in FY06/2016 and by 2.9% in FY06/2017, suggesting sales are currently accelerating.

Consumables mainly comprise those of surgery, orthopedics and circulatory organ, each of which saw steady increases of sales over the same period in the previous year, i.e., up 8.4%, up 11.0% and up 10.2%, respectively. Due to successful sales promotion measures, the Company made favorable progress for cultivating new customers, implying that the Company is seeing own market share currently increasing, while one of the sales promotion measures was to launch new merchandises. For example, the Company suggests that sales of consumables were driven by increasing sales of expensive new merchandises called “frozen balloon” in regards to catheter ablation (circulatory-organ consumables to cauterize myocardial tissue causing tachycardia to make the heart pulse fast by means of high frequency).

Sales



Operating Profit



Source: Company Data, WRJ Calculation

In regards to consumables, it appears that the Company sees stability of gross profit margin on top of stable increases of sales. Nevertheless, the Company sees some volatility of sales on a quarterly basis and a lot of volatility in operating profit as a whole for Medical Consumables and Equipment, which has a lot to do with business performance of equipment, i.e., the other constituent of this business segment. In regards to equipment, sales per project are large, generating volatility of sales in a short-term view, while gross profit margin of each project depends to more than a certain extent.

Both consumables and equipment have customers in common, being sold to medical institutions represented by major base hospitals heavily involved with acute care as mentioned earlier, but demand for equipment, including MRI, cineangiography, CT, ultrasonic diagnostic equipment and operating room equipment such as artificial respirator as merchandises to deal in, is determined by something totally different from that of consumables, i.e., capital expenditures to put up new building, to renew existing building and to expand or replace facilities. Meanwhile, in a short-term view, sales are apt to concentrate in Q3 and to adjust sharply in Q4 to follow because of seasonal factor that Q3 (January to March) includes March when the customers execute their budgets. On top of this, short-term sales in a period hinges of whether the Company sees sales associated with large-scale special procurement project or not, while gross profit margin of each project depends on whether the Company is just simply involved with pure distribution of all those equipment or for internal own qualified architect of the first class being heavily involved with installation, etc. of equipment.

In Q2 FY06/2017, the Company saw operating profit of no less than ¥535m in Medical Consumables and Equipment. As far as we could gather, this had a lot to do with booking of sales on large-scale special procurement project associated with disaster recovery in Tohoku region. Said project was large in sales and carried fairly high gross profit margin, given heavy involvement with installation, etc. of equipment by the Company.

Meanwhile, sales of equipment came down by 11.7% over the same period in the previous year in Q1 to Q2 as sales associated with above-mentioned large-scale special procurement project did not reappear, while gross profit of equipment must have come down sharply. Still, as a whole for the Company, gross profit came in at ¥5,522m (up 1.2%), while SG&A expenses ¥4,817m (down 1.4%), having resulted in operating profit of ¥704m (up 23.4%). In terms of ratio to sales, they are 10.12% (down 0.14% points), 8.83% (down 0.36% points) and 1.29% (up 0.22% points), respectively.

Thus, gross profit margin came down somewhat over the same period in the previous year, but gross profit in value increased due to accelerating sales of consumables as far as we could see. Meanwhile, it appears that gross profit margin as a whole for the Company remains roughly unchanged but for impacts stemming from above-mentioned large-scale special procurement project. In regards to decreases of SG&A expenses, the Company refers to delayed spending on expenses in H1 (Q1 to Q2) to H2 as a factor as well as to goodwill write-off charges having disappeared from the past mergers and to improving efficiency of business operations as a result of changes of organizational structure. In regards to delayed spending on expenses, the Company mentions examples such as those of office renovation and R&D expenses associated with Imports and Sales, while also mentioning that it reversed some allowance for doubtful accounts. All those factors account for a part of overshoot for operating profit.

Meanwhile, Company forecasts for profit attributable to owners of parent were exceeded much more, which was attributable to a one-off factor to a large extent. As a result of review on probability for the Company to retrieve deferred tax assets, tax rate came down according to the Company. Still, on a full-year basis, this issue is not to generate major impacts.

Income Statement (Cumulative, Quarterly)

Income Statement (Million Yen)	Cons.Act Q1 06/2017	Cons.Act Q1 to Q2 06/2017	Cons.Act Q1 to Q3 06/2017	Cons.Act Q1 to Q4 06/2017	Cons.Act Q1 06/2018	Cons.Act Q1 to Q2 06/2018	Cons.Act Q1 to Q3 06/2018	Cons.Act Q1 to Q4 06/2018	YoY Net Chg.
Sales	**25,459**	**53,184**	**81,105**	**105,778**	**26,227**	**54,563**	**-**	**-**	**+1,378**
Cost of Sales	22,953	47,727	72,832	94,879	23,538	49,041	-	-	+1,313
Gross Profit	2,506	5,456	8,273	10,898	2,689	5,522	-	-	+65
SG&A	2,464	4,885	7,313	9,854	2,419	4,817	-	-	(68)
Operating Profit	**41**	**571**	**960**	**1,044**	**269**	**704**	**-**	**-**	**+133**
Non Operating Balance	11	19	66	68	0	1	-	-	(17)
Recurring Profit	**52**	**590**	**1,026**	**1,112**	**270**	**706**	**-**	**-**	**+115**
Extraordinary Balance	5	14	17	1	31	24	-	-	+10
Profit before Income Taxes	57	604	1,044	1,114	301	731	-	-	+126
Income Taxes	38	231	388	432	98	139	-	-	(91)
NP Belonging to Non-Controlling SHs	(1)	(4)	(5)	(8)	(1)	(3)	-	-	0
Profit Attributable to Owners of Parent	**20**	**377**	**661**	**690**	**204**	**595**	**-**	**-**	**+217**
Sales YoY	+10.2%	+8.0%	+4.5%	+4.3%	+3.0%	+2.6%	-	-	-
Operating Profit YoY	-	+193.3%	+79.6%	+92.2%	+557.3%	+23.4%	-	-	-
Recurring Profit YoY	-	+205.2%	+91.6%	+99.8%	+413.4%	+19.6%	-	-	-
Profit Attributable to Owners of Parent YoY	-	+312.9%	+121.7%	+125.9%	+880.2%	+57.6%	-	-	-
Gross Profit Margin	9.84%	10.26%	10.20%	10.30%	10.25%	10.12%	-	-	(0.14%)
(SG&A / Sales)	9.68%	9.19%	9.02%	9.32%	9.23%	8.83%	-	-	(0.36%)
Operating Profit Margin	0.16%	1.07%	1.18%	0.99%	1.03%	1.29%	-	-	+0.22%
Recurring Profit Margin	0.21%	1.11%	1.27%	1.05%	1.03%	1.29%	-	-	+0.18%
Profit Attributable to Owners of Parent Margin	0.08%	0.71%	0.82%	0.65%	0.78%	1.09%	-	-	+0.38%
Total Income Taxes / Profit before Income Taxes	67.0%	38.3%	37.2%	38.8%	32.7%	19.1%	-	-	(19.1%)

Income Statement (Million Yen)	Cons.Act Q1 06/2017	Cons.Act Q2 06/2017	Cons.Act Q3 06/2017	Cons.Act Q4 06/2017	Cons.Act Q1 06/2018	Cons.Act Q2 06/2018	Cons.Act Q3 06/2018	Cons.Act Q4 06/2018	YoY Net Chg.
Sales	**25,459**	**27,725**	**27,920**	**24,673**	**26,227**	**28,336**	**-**	**-**	**+610**
Cost of Sales	22,953	24,774	25,104	22,047	23,538	25,503	-	-	+728
Gross Profit	2,506	2,950	2,816	2,625	2,689	2,832	-	-	(118)
SG&A	2,464	2,420	2,427	2,541	2,419	2,397	-	-	(23)
Operating Profit	**41**	**530**	**388**	**84**	**269**	**435**	**-**	**-**	**(95)**
Non Operating Balance	11	7	46	2	0	1	-	-	(6)
Recurring Profit	**52**	**537**	**435**	**86**	**270**	**436**	**-**	**-**	**(101)**
Extraordinary Balance	5	9	3	(16)	31	(6)	-	-	(15)
Profit before Income Taxes	57	547	439	70	301	429	-	-	(117)
Income Taxes	38	192	156	44	98	41	-	-	(151)
NP Belonging to Non-Controlling SHs	(1)	(2)	(1)	(2)	(1)	(1)	-	-	0
Profit Attributable to Owners of Parent	**20**	**356**	**283**	**29**	**204**	**390**	**-**	**-**	**+33**
Sales YoY	+10.2%	+6.1%	(1.7%)	+3.6%	+3.0%	+2.2%	-	-	-
Operating Profit YoY	-	+98.1%	+14.5%	+843.1%	+557.3%	(17.9%)	-	-	-
Recurring Profit YoY	-	+103.7%	+27.3%	+309.7%	+413.4%	(18.9%)	-	-	-
Profit Attributable to Owners of Parent YoY	-	+117.4%	+37.2%	+299.9%	+880.2%	+9.4%	-	-	-
Gross Profit Margin	9.84%	10.64%	10.09%	10.64%	10.25%	10.00%	-	-	(0.65%)
(SG&A / Sales)	9.68%	8.73%	8.69%	10.30%	9.23%	8.46%	-	-	(0.27%)
Operating Profit Margin	0.16%	1.91%	1.39%	0.34%	1.03%	1.54%	-	-	(0.38%)
Recurring Profit Margin	0.21%	1.94%	1.56%	0.35%	1.03%	1.54%	-	-	(0.40%)
Profit Attributable to Owners of Parent Margin	0.08%	1.29%	1.02%	0.12%	0.78%	1.38%	-	-	+0.09%
Total Income Taxes / Profit before Income Taxes	67.0%	35.2%	35.7%	62.7%	32.7%	9.6%	-	-	(25.6%)

Source: Company Data, WRJ Calculation

Segmented Information (Cumulative, Quarterly)

Segmented Information	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	
	Q1	Q1 to Q2	Q1 to Q3	Q1 to Q4	Q1	Q1 to Q2	Q1 to Q3	Q1 to Q4	YoY
(Million Yen)	06/2017	06/2017	06/2017	06/2017	06/2018	06/2018	06/2018	06/2018	Net Chg.
Medical Consumables and Equipment	21,349	44,702	68,254	88,584	21,816	45,454	-	-	+752
SPD	3,666	7,583	11,452	15,316	3,915	8,111	-	-	+527
Care Supplies	442	899	1,397	1,877	496	997	-	-	+98
Imports and Sales	0	0	0	0	0	0	-	-	-
Sales	**25,459**	**53,184**	**81,105**	**105,778**	**26,227**	**54,563**	**-**	**-**	**+1,378**
Medical Consumables and Equipment	58	593	965	1,062	293	744	-	-	+151
SPD	19	47	84	103	20	33	-	-	(14)
Care Supplies	19	41	67	128	22	45	-	-	+4
Imports and Sales	(4)	(9)	(13)	(20)	(4)	(9)	-	-	0
Segment Profit	**92**	**672**	**1,103**	**1,274**	**331**	**814**	**-**	**-**	**+141**
Elimination	(51)	(101)	(143)	(230)	(61)	(109)	-	-	(7)
Operating Profit	**41**	**571**	**960**	**1,044**	**269**	**704**	**-**	**-**	**+133**
Medical Consumables and Equipment	0.27%	1.33%	1.41%	1.20%	1.34%	1.64%	-	-	+0.31%
SPD	0.53%	0.62%	0.74%	0.67%	0.52%	0.41%	-	-	(0.21%)
Care Supplies	4.30%	4.60%	4.84%	6.85%	4.43%	4.58%	-	-	(0.02%)
Imports and Sales	-	-	-	-	-	-	-	-	-
Operating Profit Margin	**0.16%**	**1.07%**	**1.18%**	**0.99%**	**1.03%**	**1.29%**	**-**	**-**	**+0.22%**

Segmented Information	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	YoY
(Million Yen)	06/2017	06/2017	06/2017	06/2017	06/2018	06/2018	06/2018	06/2018	Net Chg.
Medical Consumables and Equipment	21,349	23,352	23,552	20,330	21,816	23,638	-	-	+286
SPD	3,666	3,917	3,869	3,863	3,915	4,195	-	-	+278
Care Supplies	442	456	498	479	496	501	-	-	+45
Imports and Sales	0	0	0	0	0	0	-	-	-
Sales	**25,459**	**27,725**	**27,920**	**24,673**	**26,227**	**28,336**	**-**	**-**	**+610**
Medical Consumables and Equipment	58	535	371	97	293	451	-	-	(84)
SPD	19	27	36	19	20	12	-	-	(15)
Care Supplies	19	22	26	60	22	23	-	-	+1
Imports and Sales	(4)	(5)	(3)	(6)	(4)	(5)	-	-	0
Segment Profit	**92**	**580**	**430**	**170**	**331**	**482**	**-**	**-**	**(97)**
Elimination	(51)	(50)	(41)	(86)	(61)	(47)	-	-	+2
Operating Profit	**41**	**530**	**388**	**84**	**269**	**435**	**-**	**-**	**(95)**
Medical Consumables and Equipment	0.27%	2.29%	1.58%	0.48%	1.34%	1.91%	-	-	(0.38%)
SPD	0.53%	0.71%	0.95%	0.49%	0.52%	0.30%	-	-	(0.41%)
Care Supplies	4.30%	4.89%	5.28%	12.70%	4.43%	4.72%	-	-	(0.17%)
Imports and Sales	-	-	-	-	-	-	-	-	-
Operating Profit Margin	**0.16%**	**1.91%**	**1.39%**	**0.34%**	**1.03%**	**1.54%**	**-**	**-**	**(0.38%)**

Source: Company Data, WRJ Calculation

Balance Sheet (Quarterly)

Balance Sheet	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	YoY
(Million Yen)	06/2017	06/2017	06/2017	06/2017	06/2018	06/2018	06/2018	06/2018	Net Chg.
Cash and Deposit	2,435	3,063	2,775	2,220	2,791	2,223	-	-	(840)
Accounts Receivables	19,328	21,412	21,688	18,726	20,899	22,939	-	-	+1,526
Inventory	4,576	4,792	4,581	4,331	4,539	4,808	-	-	+16
Other	900	745	738	937	941	874	-	-	+128
Current Assets	**27,240**	**30,013**	**29,784**	**26,215**	**29,171**	**30,845**	**-**	**-**	**+831**
Tangible Assets	3,741	3,714	3,671	3,668	3,709	3,772	-	-	+58
Intangible Assets	215	184	178	212	243	270	-	-	+85
Investments and Other Assets	1,443	1,479	1,430	1,678	1,566	1,669	-	-	+190
Fixed Assets	**5,401**	**5,377**	**5,280**	**5,558**	**5,519**	**5,712**	**-**	**-**	**+334**
Total Assets	**32,641**	**35,391**	**35,064**	**31,774**	**34,690**	**36,557**	**-**	**-**	**+1,165**
Accounts Payables	21,174	23,627	23,807	21,089	21,723	24,543	-	-	+915
Short Term Debt	3,554	3,414	2,574	1,535	4,110	2,985	-	-	(429)
Other	1,318	1,372	1,510	1,815	1,506	1,254	-	-	(118)
Current Liabilities	**26,048**	**28,415**	**27,892**	**24,440**	**27,339**	**28,783**	**-**	**-**	**+367**
Long Term Debt	797	729	630	546	502	444	-	-	(285)
Other	1,242	1,278	1,284	1,362	1,405	1,459	-	-	+180
Fixed Liabilities	**2,040**	**2,008**	**1,915**	**1,908**	**1,908**	**1,903**	**-**	**-**	**(104)**
Total Liabilities	**28,089**	**30,423**	**29,807**	**26,349**	**29,248**	**30,686**	**-**	**-**	**+263**
Shareholders' Equity	**4,467**	**4,827**	**5,111**	**5,140**	**5,177**	**5,567**	**-**	**-**	**+739**
Other	84	140	145	285	265	303	-	-	+162
Net Assets	**4,552**	**4,968**	**5,256**	**5,425**	**5,442**	**5,870**	**-**	**-**	**+902**
Total Liabilities and Net Assets	**32,641**	**35,391**	**35,064**	**31,774**	**34,690**	**36,557**	**-**	**-**	**+1,165**
Equity Capital	4,435	4,827	5,117	5,289	5,308	5,738	-	-	+911
Interest Bearing Debt	4,352	4,143	3,205	2,081	4,612	3,429	-	-	(714)
Net Debt	1,917	1,080	429	(138)	1,821	1,206	-	-	+125
Equity Capital Ratio	13.6%	13.6%	14.6%	16.6%	15.3%	15.7%	-	-	+2.1%
Net Debt Equity Ratio	43.2%	22.4%	8.4%	(2.6%)	34.3%	21.0%	-	-	(1.4%)
ROE (12 months)	9.0%	12.5%	13.4%	14.0%	18.0%	17.2%	-	-	+4.7%
ROA (12 months)	2.1%	2.8%	2.9%	3.5%	4.0%	3.4%	-	-	+0.6%
Days for Inventory Turnover	18	18	17	18	18	17	-	-	-
Quick Ratio	84%	86%	88%	86%	87%	87%	-	-	-
Current Ratio	105%	106%	107%	107%	107%	107%	-	-	-

Source: Company Data, WRJ Calculation

Cash Flow Statement (Cumulative)

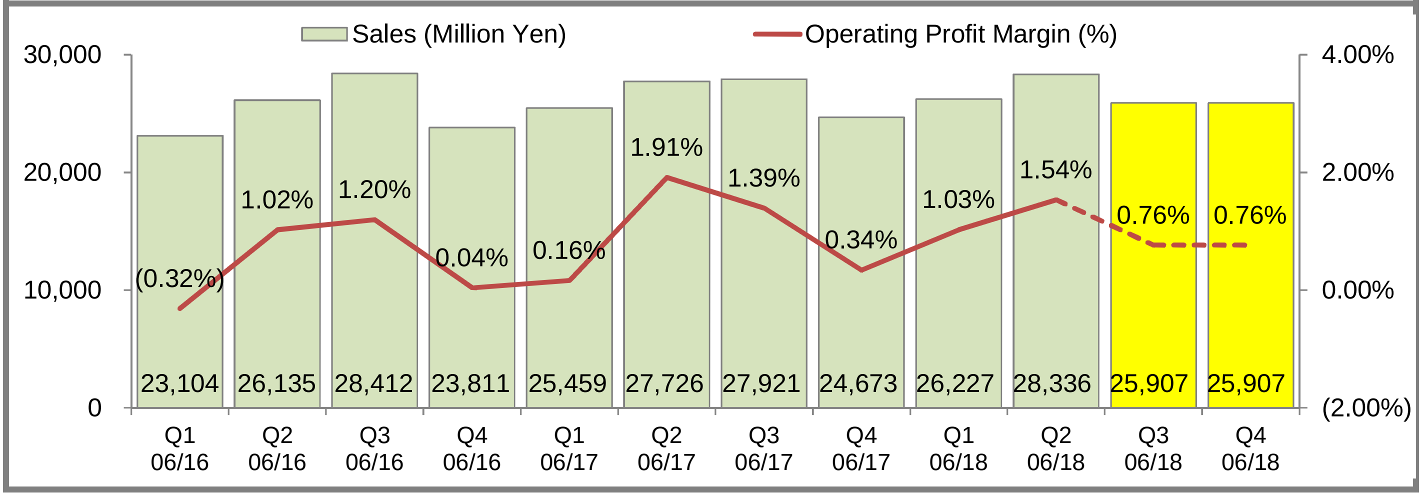
Cash Flow Statement	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	
	Q1	Q1 to Q2	Q1 to Q3	Q1 to Q4	Q1	Q1 to Q2	Q1 to Q3	Q1 to Q4	YoY
(Million Yen)	06/2017	06/2017	06/2017	06/2017	06/2018	06/2018	06/2018	06/2018	Net Chg.
Operating Cash Flow	-	(423)	-	871	-	(1,038)	-	-	(614)
Investing Cash Flow	-	(39)	-	(99)	-	(124)	-	-	(84)
Operating CF & Investing CF	**-**	**(463)**	**-**	**771**	**-**	**(1,162)**	**-**	**-**	**(698)**
Financing Cash Flow	-	1,337	-	(741)	-	1,165	-	-	(172)

Source: Company Data, WRJ Calculation

FY06/2018 Company Forecasts

FY06/2018 initial Company forecasts have remained unchanged, going for prospective sales of ¥106,377m (up 0.6% YoY), operating profit of ¥1,100m (up 5.3%), recurring profit of ¥1,109m (down 0.3%) and profit attributable to owners of parent of ¥714m (up 3.4%), while operating profit margin of 1.03% (up 0.05% points). Meanwhile, prospective annual dividend has also remained unchanged at ¥30.0 per share, implying a payout ratio of 23.6%.

Sales and Operating Profit Margin



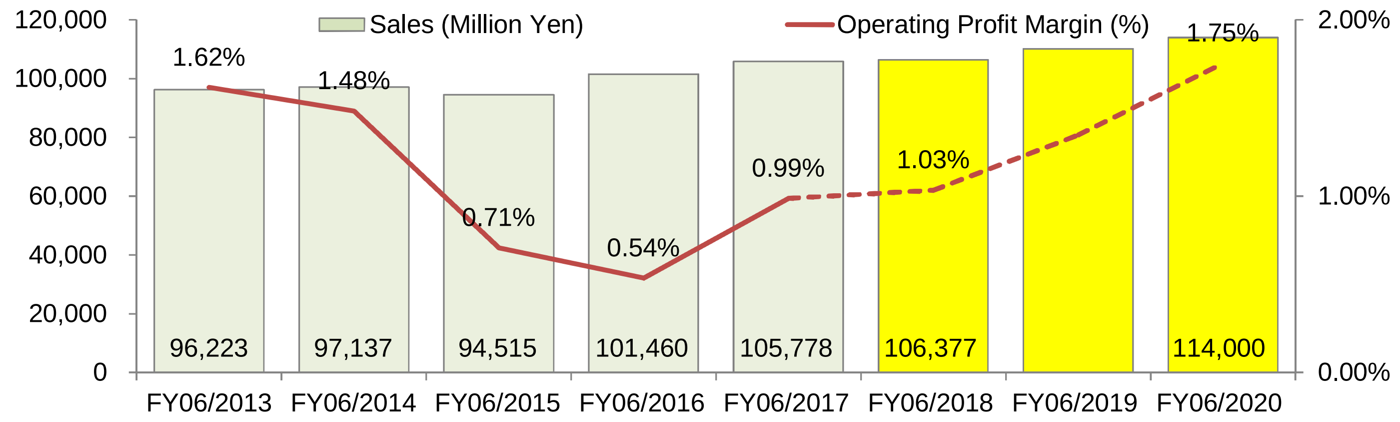
Source: Company Data, WRJ Calculation (Q3 and Q4 FY06/2018: H2 Company forecasts pro rata)

Initial Company forecasts assume limited increases of sales for Medical Consumables and Equipment and thus as a whole for the Company too. It appears that sales of the mainstay consumables are on the rise but sales of equipment are to come down with the assumptions. The Q1 to Q2 results showed a trend in this manner, but collective sales in value were marginally better than initially expected as far as we could see.

Long-Term Prospects

At the release of FY06/2017 results on 9 August 2017, the Company also released midterm management plan (FY06/2018 to FY06/2020), which was followed by disclosure of details in results meeting to have been held on 25 August 2017. As prospective business performance target, midterm management plan is calling for sales of ¥114,000m, operating profit of ¥2,000m and operating profit margin of 1.75% in FY06/2020, i.e., the last year of the plan, implying CAGR of 2.5% for sales and 24.2% for operating profit during the three-year period after FY06/2017 results, while operating profit margin improving by 0.77%.

Midterm Management Plan



Source: Company Data, WRJ Calculation

As the key themes of new midterm management plan, the Company mentions “acquisition of new earnings pillars”, “rationalization and efficiency” and “work style reform”. As far as we could see, the Company is looking to “acquisition of new earnings pillars” in particular as the driver to achieve above-mentioned prospective business performance target. The Company is to set up a new scheme to be involved with distribution of merchandises more than now so that it should be able to beef up sales with gross profit margin higher than now.

Specifically, the Company is on the verge of selling medical simulator robot as the general distributor to exclusively sell them in Japan. As an integrated medical trader with competitive distribution capability, the Company has been aggressively propelling its operations on so-called “manufacturer-&-seller-driven medical-engineering cooperation” by means of frequently holding sales support conferences for start-ups whose distribution capability is limited. Going forward, the Company is to persistently launch promising new merchandises as a result of this.

For example, it was disclosed through the release on 18 August 2017 that MICOTO Technology Inc., based in Yonago-city of Tottori-prefecture, and EXSOLA MEDICAL Inc. or one of the operating companies under the management of the Company reached basic agreement to conclude the general distributor contract in regards to medical simulation robot ‘mikoto’. Based on this basic agreement, the Company is currently planning to exclusively sell said merchandise across Japan as well as providing solutions for introduction and maintenance services, etc.

Medical Simulator Robot 'mikoto': You can feel "life" with the Robot 'mikoto'

Source: Company Data

Since a few years ago, it has been increasingly important in doctors' training to practically take part in medical treatment rather than just watching in order to further facilitate acquisition of clinical skills and to understand medical safety. Thus, there has been changeover of the contents of the training so that practical knowledge should be enhanced more than before. One of the tools for this is practice-oriented simulation education to take advantage of simulators, favorably driving the market for medical simulation equipment. In order to cope with increasing needs here, MICOTO Technology Inc. has developed 'mikoto'. i.e., medical simulator robot being equipped with features of quasi-real appearance, structure and response having never been materialized before, making an impression as if it were real human being, while planning to propel sales promotions through the general distributor contract with the Company.

Meanwhile, in FY06/2020, sales of system and kit to detect breast cancer at early stage by means of analyzing exhalation are to take off on a full-fledged basis. On 16 February 2016, the Company concluded exclusive distributor agreement in Japan on all those merchandises with a medical equipment start-up based in Israel, while having been making progress of demonstrations at medical institutions as well as booking SG&A expenses stemming from here to date. At the end of the day, the Company is planning to launch them in Japan by the end of FY06/2019 after clinical trial and approval.

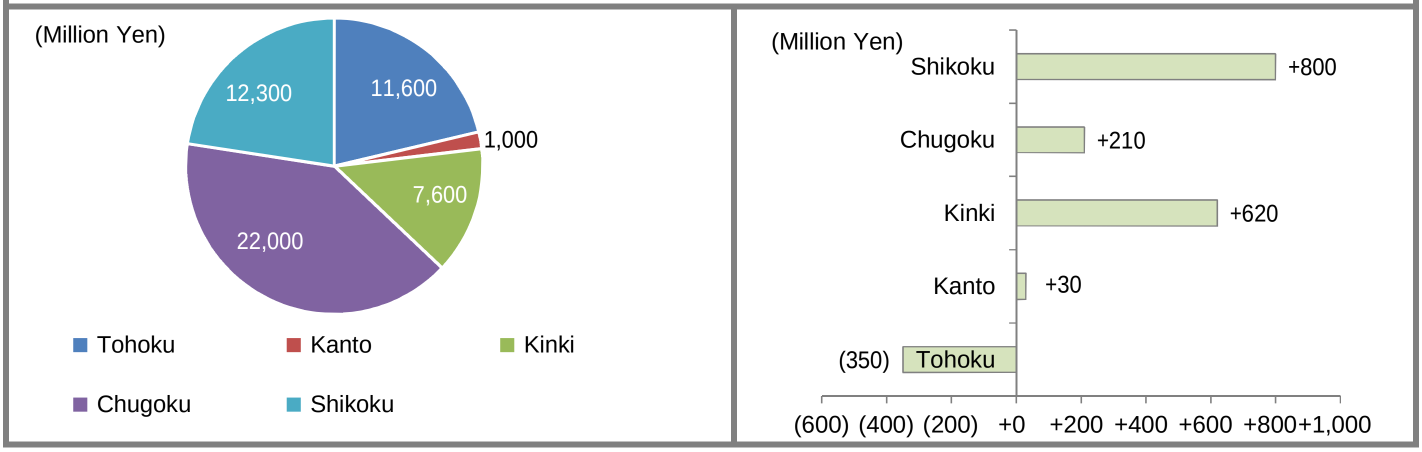
At the moment, mammography and ultrasonic diagnostic equipment are used as the key devices to detect breast cancer. The 2014 survey by Ministry of Health and Welfare estimates 5.6m medical examinees pa seeing doctor for detection based on mammography, implying the penetration rate of 20% out of the potential market of 28.2m (the number of Japanese females in their forties, fifties and sixties). Meanwhile, the Company is going for detection by said merchandises to reach collective 1.0m in terms of the number of medical examinees within the first three to 5 years. Seeing doctor in the existing way unavoidably incurs some invasive pains, etc. for medical examinees, while just analyzing exhalation does not do so at all. Thus, the latter is expected to get increasingly adopted as preliminary process prior to the former.

4.0 Business Model

Medical Consumables and Equipment

In the mainstay Medical Consumables and Equipment, the Company sells medical consumables and equipment to medical institutions represented by major base hospitals heavily involved with acute care. Just roughly speaking, this business domain in Japan has market size of ¥2.8 trillion pa and CAGR of 5% going forward. Meanwhile, the number of players in the market stands at more than 1,000, implying a large room remaining for consolidation in the foreseeable future.

Sales by Region and Net Changes over the Same Period in the Previous Year (Q1 to Q2 FY06/2018 Results)



Source: Company Data, WRJ Calculation

In terms of sales by region, the Company, based in Okayama-city, has the largest exposure to Chugoku region where Okayama-city is included as a part. Meanwhile, the Company acquired and merged with Sansei Medical Materials Co., Ltd., having made this operating company under management of the Company since Q3 FY06/2012. Driven by this, exposure of the Company to Tohoku region surged, while that of Kanto region having newly started up. Thus, the Company made remarkable progress of sales enhancement in geographical territory having had remained uncultivated, while beefing up own market share at the same time together with the acquisition and merger with peer. Meanwhile, recent circumstances of sales by region suggest that there are good opportunities for the Company to implement acquisition and merger in Kanto region in particular.

On top of Medical Consumables and Equipment, the Company is also involved with Imports and Sales, SPD and Care Supplies by business segment. Still, each of them has remained insignificant in terms of impacts to earnings as a whole for the Company and thus the earnings hinging on Medical Consumables and Equipment to a large extent.

Imports and Sales refers to operations of aforementioned EXSOLA MEDICAL Inc. or one of the operating companies under the management of the Company. To date, no sales have been booked and operating loss equating to SG&A expenses here.

SPD (Supply Processing and Distribution) is run by business model that is effectively the same as that of Medical Consumables and Equipment but for the key difference that it also collects commissions from medical institutions to be supplied by the Company through being in charge of management of inventory, information and purchasing on behalf of them on top of selling merchandises to them. In terms of gross profit, it appears that some 80% comes from said commissions.

Merchandises of Medical Consumables and Equipment (Image Pictures)

Source: Company Data

Care Supplies refers to operations of sales and rental services of nursing-care beds and supplies. The mainstay operations here are those of rental services of nursing-care beds, accounting for some 80% of sales here and carrying gross profit margin of some 50%. In all the business segments but for Care Supplies, the Company is exclusively exposed to medical institutions as own customers, while Care Supplies to local elderly people and their families, which is the distinguished feature for this business segment.

Disclaimer

Information here is a summary of “IR Information” of the Company, compiled by Walden Research Japan, from a neutral and professional standing point, in the form of a report. “IR Information” of the Company comprises a) contents of our interview with the Company, b) contents of presentations for institutional investors, c) contents of timely disclosed information and d) contents of the homepage, etc.

Company name: Walden Research Japan Incorporated
Head office: 4F Hulic Ginza 1-chome Building, 1-13-1 Ginza, Chuo-city, Tokyo 104-0061 JAPAN
URL: www.walden.co.jp
E-mail: info@walden.co.jp
Phone：+81 3 3553 3769