Walden Research Japan

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EM SYSTEMS (4820)

Consolidated Fiscal Year (Million Yen)		Sales	Operating Profit	Recurring Profit	Profit Attributable to Owners of Parent	EPS (Yen)	DPS (Yen)	BPS (Yen)
FY03/2017		13,676	2,597	3,163	2,116	60.3	15.5	395.5
FY03/2018		13,953	3,063	3,618	2,369	66.7	18.5	446.8
FY03/2019CoE		13,146	2,362	2,993	2,020	56.0	18.0	-
FY03/2018	YoY	2.0%	17.9%	14.4%	12.0%	-	-	-
FY03/2019CoE	YoY	(5.8%)	(22.9%)	(17.3%)	(14.7%)	-	-	-
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 FY03/2018		6,873	1,509	1,825	1,214	-	-	-
Q3 to Q4 FY03/2018		7,080	1,554	1,793	1,155	-	-	-
Q1 to Q2 FY03/2019		6,594	1,468	1,787	1,197	-	-	-
Q3 to Q4 FY03/2019CoE		6,552	894	1,206	823	-	-	-
Q1 to Q2 FY03/2019	YoY	(4.1%)	(2.7%)	(2.1%)	(1.4%)	-	-	-
Q3 to Q4 FY03/2019CoE	YoY	(7.5%)	(42.5%)	(32.7%)	(28.7%)	-	-	-

Source: Company Data, WRJ Calculation (per share data: retroactively adjusted for 1:2 share split, effective on 1 Mar. 2018)

1.0 Executive Summary (21 January 2019)

MAPs

EM SYSTEMS, running operations of development, sale and maintenance for healthcare-related systems, is going for a long-term growth by means of adopting new services for customers based on MAPs (Medical Advance for People, System), i.e., the industry's first shared information system foundation. Sales on the Pharmacies side, basically driving business performance as a whole for the Company, comprise those of one-time-fee business and of subscription-based business. The former represents initial license fees and price of hardware, while the latter monthly fees for the use of systems and of maintenance services. In Q1 to Q2 FY03/2019, sales of one-time-fee business accounted for 38% of total and subscription-based business 62%. Meanwhile, the Company is to introduce a new business model in line with the adoption of new services based on above-mentioned MAPs, where customers pay monthly fees only and initial license fees being completely abolished (hardware to be procured by customers). With this changeover for business model, it will be unavoidable that sales are to come down at the initial stage as the Company is not to see sales of one-time-fee business any more. However, the Company is expected to see steady increases of sales and earnings together with increasing market shares in a long-term view, i.e., 5.3% and 8.2%, respectively, in terms of CAGR over five-year period through FY03/2019 to FY03/2023.

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Company Profile

Development, Sale and Maintenance for Healthcare-related Systems

Company Name	EM SYSTEMS CO., LTD. Website (Japanese) IR Information (English) Share Price (Japanese)
Established	23 January 1980
Listing	13 November 2012: Tokyo Stock Exchange 1st Section (ticker: 4820) 2 May 2003: Tokyo Stock Exchange 2nd Section 15 December 2000: Tokyo Stock Exchange JASDAQ
Capital	¥2,508m (as of the end of September 2018)
No. of Shares	36,516,600 shares, including 1,147,106 treasury shares (as of the end of Sep. 2018)
Main Features	● Leading the market on the Pharmacies side with 32% share, while 3% on the Clinics side and 0.7% on nursing care ● Going for 50%, 10% and 5%, respectively, by FY03/2023 ● Benefiting from launch of MAPs (Medical Advance for People, System)
Business Segments	Ⅰ. Business for Pharmacies and related businesses Ⅱ. Business for Clinics and related businesses Ⅲ. Other business
Top Management	Chairman & CEO : Kozo Kunimitsu President & COO : Kenji Ohishi
Shareholders	Kokko Co., Ltd. 34.93%, MEDIPAL HOLDINGS CORPORATION 9.98% (as of the end of September 2018: the ratio of shares held against the number of shares outstanding but for treasury shares)
Headquarters	Yodogawa-ku, Osaka, JAPAN
No. of Employees	Consolidated: 513, Parent: 409 (as of the end of September 2018)

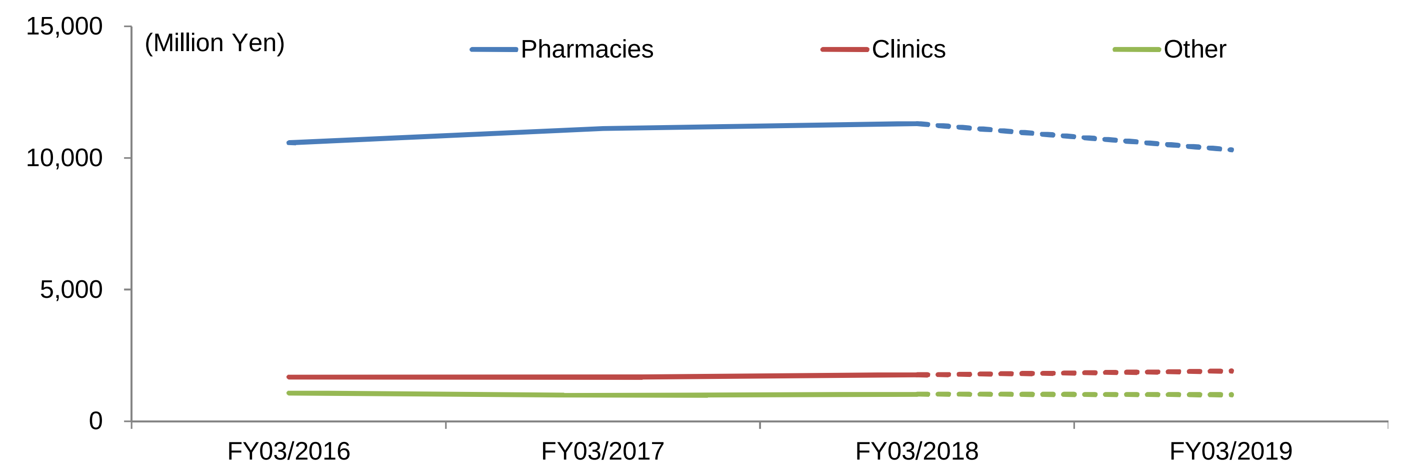
Source: Company Data

3.0 Recent Trading and Prospects

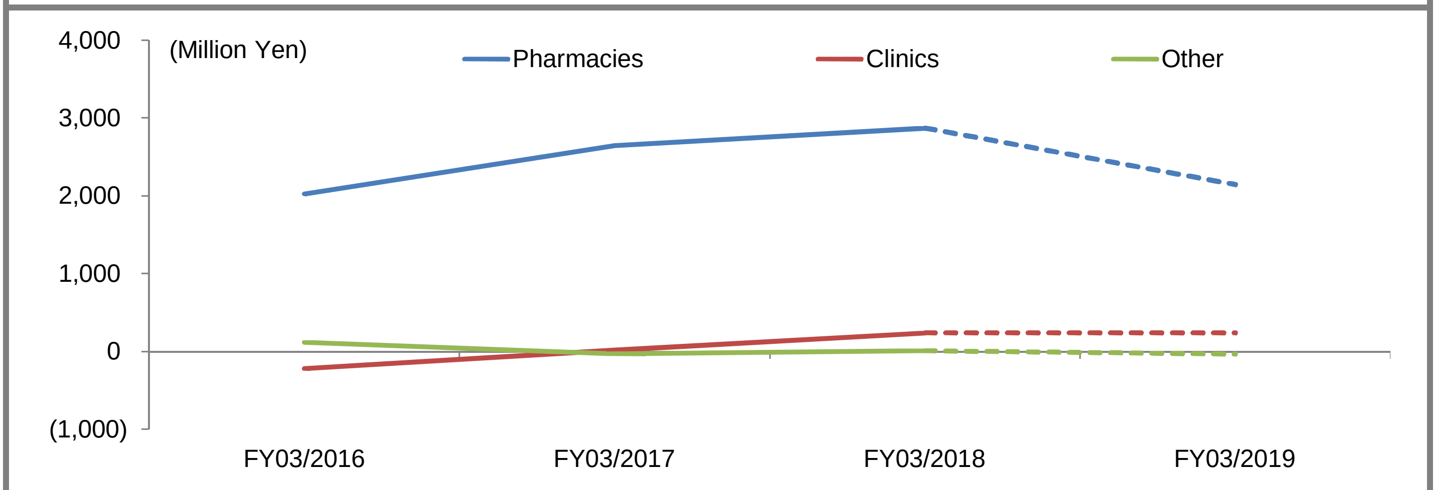
Q1 to Q2 FY03/2019 Results

In Q1 to Q2 FY03/2019, sales came in at ¥6,594m (down 4.1% YoY), operating profit ¥1,468m (down 2.7%), recurring profit ¥1,787m (down 2.1%) and profit attributable to owners of parent ¥1,197m (down 1.4%), while operating profit margin 22.3% (up 0.3% points).

Sales



Operating Profit



Source: Company Data, WRJ Calculation

By business segment, Pharmacies saw sales of ¥5,263m (down 6.4%), operating profit of ¥1,365m (down 3.9%) and operating profit margin of 25.9% (up 0.5% points). Having accounted for 79.8% of sales as a whole for the Company and 92.9% of operating profit (before adjustments), this business segment is crucially important for business performance as a whole for the Company. Meanwhile, sales of one-time-fee business came in at ¥2,020m (down 18.7%) and sales of subscription-based business ¥3,242m (up 3.3%). In regards to one-time-fee business, the Company saw sales on large-scale project of hardware associated with medical fee revision on an OEM basis (for another business in the industry) during the same period in the previous year, which did not reappear. In regards to sales of subscription-based business, the Company saw increases in line with the increases of customers.

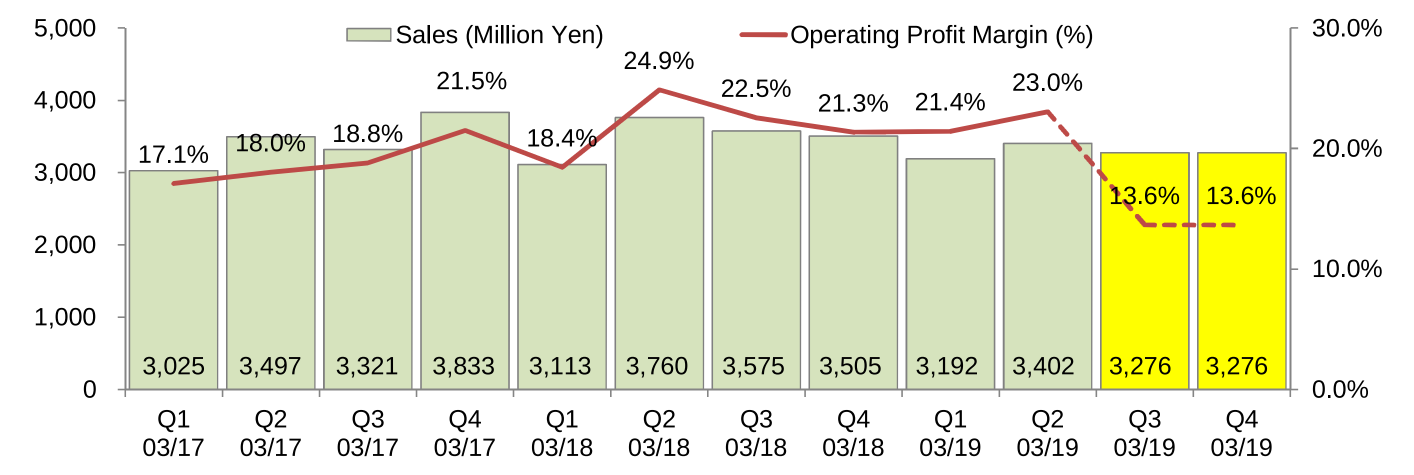
On the Pharmacies side, the Company provides customers, i.e., pharmacies with solutions. Pharmacies prescribe medication in exchange for self-pay burden regulated by health insurance to be computed through medical remuneration points based on prescription brought by patients, while gaining the remainder but for self-pay burden by means of insurance claim based on receipt (medical fee bill). Meanwhile, the Company is in charge of providing pharmacies, mainly those of sole proprietorship, with systems to cope with expertise and complicated computation indispensable in all those operations in regards to both the former and the latter. More than half of the number of contracts is of sole proprietorship (the rest: major chain stores), while the Company leads the market with 32% share. Own sales representatives are keen on speaking to pharmacies run on a sole proprietorship basis all the time, which is one of the strengths with the Company. Generally speaking, competitors are inclined to sales promotions based on outsourcing mainly targeting pharmacies of major chain stores, according to the Company.

Clinics saw sales of ¥871m (up 2.3%), operating profit of ¥122m (up 59.7%) and operating profit margin of 14.0% (up 5.1% points). Sales of one-time-fee business came in at ¥430m (up 1.8%) and sales of subscription-based business ¥441m (up 2.8%). Here, the Company is in charge of providing non-bed clinics (almost 100,000 run in Japan) with solutions based on integrated systems to cope with both receipt and electronic health record. On top of this, Other saw sales of ¥513m (up 6.5%), operating profit of negative ¥17m (versus ¥3m during the same period in the previous year) and operating profit margin of negative 3.3% (down 4.0% points). The Company sees favorable business performance in regards to operations to run own pharmacies, but having been in the middle of reconsiderations on strategy for nursing care systems for some time.

FY03/2019 Company Forecasts

FY03/2019 Company forecasts (revised on 9 November 2018) are going for prospective sales of ¥13,146m (down 5.8% YoY), operating profit of ¥2,362m (down 22.9%), recurring profit of ¥2,993m (down 17.3%) and profit attributable to owners of parent of ¥2,020m (down 17.7%), while operating profit margin of 18.0% (down 4.0% points). At the same time, Company forecasts are going for prospective dividend of ¥18.0 per share, implying payout ratio of 32.2%.

Sales and Operating Profit Margin



Source: Company Data, WRJ Calculation (Q3 and Q4 FY03/2019: H2 Company forecasts pro rata)

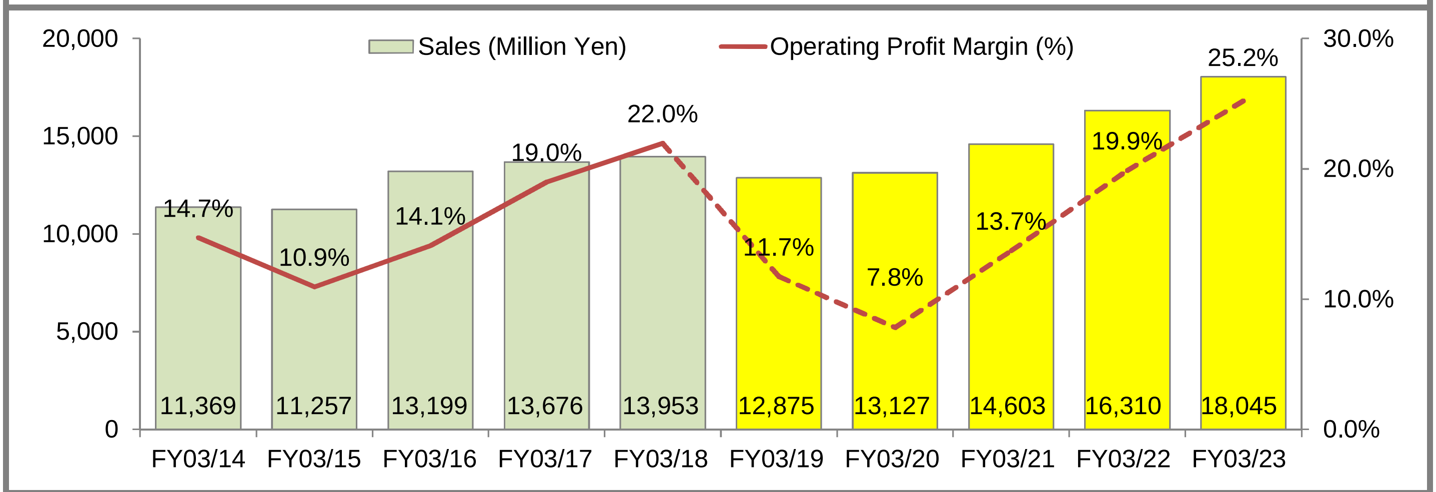
When compared with initial Company forecasts, prospective dividend has remained unchanged, but sales and earnings upgraded at the release of Q1 to Q2 results. Sales have been upgraded by ¥271m (2.1%) and operating profit by ¥854m (56.6%). Sales are driven by a trend that replacement from existing hardware to new hardware is making progress rather more quickly than initially expected, while expenses are falling short because of unexpected capitalization for some parts of R&D expenses associated with MAPs (Medical Advance for People, System).

By business segment, Company forecasts assume prospective sales of ¥10,311m (down 8.8%), operating profit of ¥2,144m (down 25.3%) and operating profit margin of 20.8% (down 4.7% points) on the Pharmacies side. Also in H2, sales are to be negatively affected by non-reappearance of aforementioned large-scale project associated with medical fee revision over the same period in the previous year. Meanwhile, on 4 January 2019, the Company launched "MAPs for CLINIC" on the Clinics side, which is the first MAPs series, prior to the mainstay Pharmacies. This is another negative factor on the Pharmacies side in that the Company currently focuses own sales promotion resources on "MAPs for CLINIC".

Long-Term Prospects

On 9 May 2018, the Company released 5-year projection or new midterm management plan (FY03/2019 to FY03/2023), calling for prospective sales of ¥18,045m, operating profit of ¥4,552m and operating profit margin of 25.2% in the last year of the plan, i.e., FY03/2023. When based on FY03/2018 results, the plan is calling for CAGR of 5.3% for sales and 8.2% for operating profit during the same period.

New Midterm Management Plan



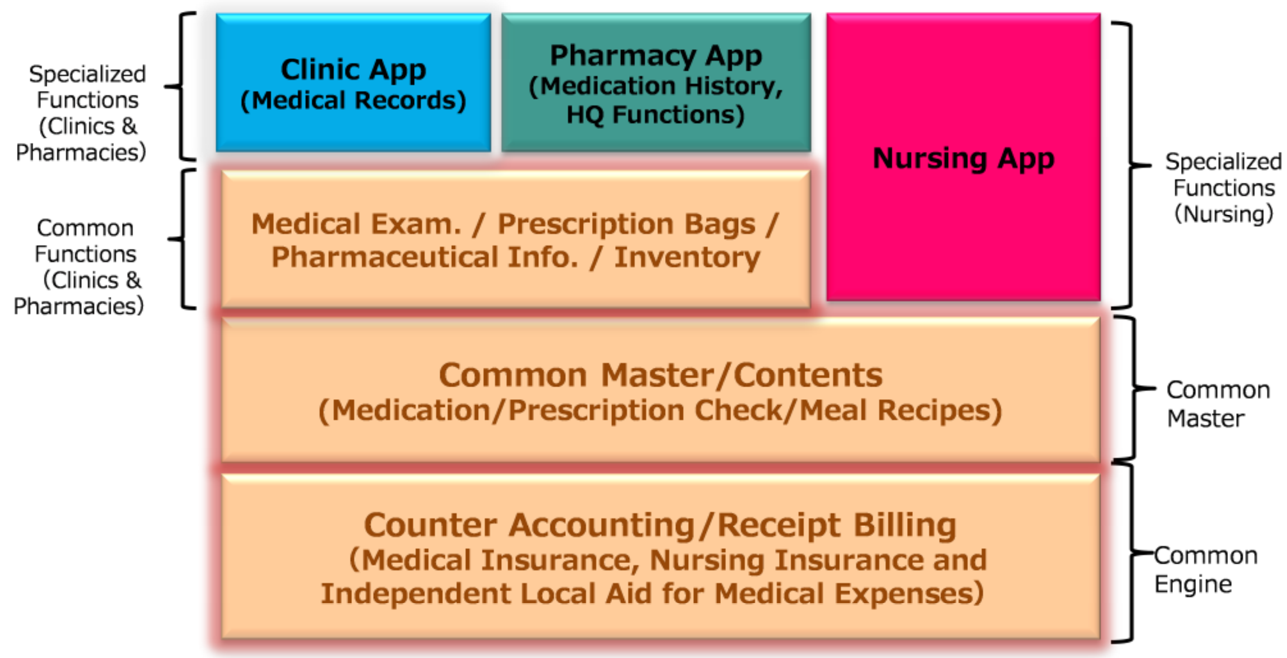
Source: Company Data, WRJ Calculation

As subsequent events, the Company mentions that some parts of R&D expenses associated with MAPs (Medical Advance for People, System) are now capitalized. Thus, expenses are to get smaller in FY03/2019 as mentioned earlier, while prospective expenses in the following years are to get larger to the same extent. Meanwhile, in line with changeover to MAPs series, sales of one-time-fee business are to disappear and thus short-term business performance is expected to adjust. Still, longer-term, this changeover is expected to drive own market shares not only on the mainstay Pharmacies side but also on the Clinics side and for nursing care.

In regards to “MAPs for PHARMACY”, currently developed on the Pharmacies side, the Company is trying to get at the launch as early as possible towards the end of FY03/2020, which is expected to be followed by launch of “MAPs for NURSING CARE” for nursing care systems belonging to Other by business segment.

Prior to the mainstay Pharmacies, the Company developed and launched MAPs series on the Clinics side with a reason that this should eventually lead to business performance more favorable. As is recognized in the history of separation of dispensary from medical practice, it used to be the case that medical institutions are in charge of preparing a medicine. Give this fact, the Company believes it should be more efficient to make progress with those on the Clinics side as the basic frame first of all and then moving on to Pharmacies as the former is more integrated than the latter. In other words, being appreciated on the Clinics side should naturally result in appreciation on the Pharmacies side, driving the Company’s strategy to increase market shares across the board.

Shared Information System Foundation: MAPs (Medical Advance for People, System)



Source: Company Data

Meanwhile, the factor to make MAPs as shared information system foundation is that each application is developed based on the common engine with its structure. By means of standardizing engine of systems for clinics, pharmacies and nursing care (counter accounting / receipt billing of medical insurance, nursing insurance and independent local aid for medical expenses) as well as master / contents at the same time, the Company is able to make changes in line with law amendment, etc. in a lump for each application. Given the fact that the Company has been doing this one by one for each engine, etc., the changeover of business model this time is to also beef up efficiency of operations with the Company.

Disclaimer

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