

FAQs for 3Q of FY3/2023

February 6, 2023
UT Group Co., Ltd.

Consolidated financial results

Q1 What contributed to a significant improvement in the record EBITDA in the first nine month of FY3/2023?

A In the current FY3/2023, we are making efforts to raise our top line starting with the number of technical employees accumulated by the end of March 2022. We also have been making efforts to establish a leaner business base and improve profitability in order to realize accelerated growth over the medium to long term.

Effective April 1, 2022, UT Group carried out a major reorganization within the Group. Operating companies with common business characteristics were integrated to enhance the ability to execute each growth strategy of the Medium-term Business Plan. In addition, since April 2022, we have been gradually introducing a new business system to standardize and communize administration and other tasks among the operating companies with the aim of improving labor productivity and further optimizing staffing. Moreover, efforts to improve hiring efficiency have been made by integrating job opportunities held by each operating company and promoting optimal hiring operations.

As a result of these initiatives, in addition to a 12% year-on-year increase in sales, a rise in the gross profit margin, and a significant improvement in the rate of SG&A expenses to sales, we significantly renewed a record high in EBITDA.

Q2 What was the reason for the operating loss in the third quarter of FY3/2023, while a record high was recorded in EBITDA?

A We have made a steady progress in EBITDA in the first nine months of FY3/2023 by making a 80.5% progress against the full-year plan, and we recognize that the probability of achieving our full-year forecast of 15 billion yen has increased sufficiently. The performance condition for the exercise of stock acquisition rights (performance-linked stock acquisition rights) announced on May 20, 2020 is EBITDA of 15 billion yen. Given the increased probability of achieving the condition, we recorded stock-based compensation expenses of 5.5 billion yen (SG&A expenses) in the first nine months of FY3/2023. This has resulted in recording an operating loss for the third quarter. Notably, operating profit excluding the impact of stock-based compensation expenses has reached a record high, similar to EBITDA. Also, this factor has already been incorporated in the full-year earnings forecast for FY3/2023.

Q3 What is the status of dispatched worker demand by sector?

A Although demand for semiconductors is expected to increase over the medium to long term on the back of the expansion of information and communication technology and the acceleration of global decarbonization, capital investment and production activities by semiconductor manufacturing equipment (SME) makers and semiconductor makers have recently been affected by inventory adjustments and other factors and have shown a sign of slowdown. Meanwhile, automobile-related manufacturers have intermittently suspended operation mainly due to shortages of parts supply. Along this backdrop, some clients in the Manufacturing Business postponed to satisfy demand for additional workers, and we had to carry out cautious hiring activities. In the Area Business, which provides community-based human resource services, the sales structure was strengthened, and the number of job offers increased favorably.

Q4 How about the status of your hiring activities?

A Our plan for FY3/2023 is to increase the number of technical employees while focusing on hiring efficiency. Specifically, we plan to reduce the rate of hiring expenses to sales to 3.0% or less, while continuing to hire around 1,200 to 1,300 hires per month. The rate of hiring expenses to sales was 2.1% for the first nine months and the number of hires remained at the level of about 1,200 per month on average.

In the third quarter, the rate of hiring expenses to sales was 1.9%, which was well controlled in line with the demand situation. As stated in Q3, given the stagnant demand for new workers at some clients in the Manufacturing Business, the average number of hires per month was just over 1,000. Over the medium to long term, we will continue to improve the efficiency in hiring operations by utilizing the Group's integrated hiring database, and will expand the functions of our comprehensive job site JOBPAL (enhanced job listings and contacts with job seekers), which was launched on April 1, 2022. We aim to expand earnings by responding to the demand for workers mainly in the Industrial and Commercial Machinery sector and the Electronics sector of the Manufacturing Business segment and to the various job openings in the Area Business segment, with the aim of growing profit.

Q5 Tell me about the status of the new consolidation and sale of companies.

A Meanwhile, as of March 31, 2022, UT System Products Co., a consolidated subsidiary of UT Group, was sold to Taihei Co., Ltd. (Head office: Sosa City, Chiba Prefecture; President: Kenjiro Ota). On April 1, 2020, we acquired shares of UT System Products together with UT Toshiba Co. (current corporate name), which was engaged in a worker dispatch business, from Toshiba Information Systems Co. UT System Products provided purchasing agent services for corporate customers and were engaged in the sales of supply products. However, since the synergies with UT Group's existing businesses were limited, we have decided to divest the shares of UT System Products in order to selectively concentrate our management resources and increase management efficiency toward achieving the Fourth Medium-Term Business Plan.

Q6 Please explain about your subsidiary reorganization that was implemented in April 2022.

A With the aim of enabling flexible, efficient decision making in the One-stop Strategy for Large Manufacturers and the Area Platform Strategy, the reorganization in April 2022 divided the UT Group companies into two groups: subsidiaries engaged in our competitive personnel services business for major manufacturers and subsidiaries engaged in the Area Platform Strategy, which has been promoted in the Fourth Medium-Term Business Plan. Both of these groups have been reorganized so as to promote the acceleration of their growth in keeping with their respective clear strategy. In addition, by consolidating subsidiaries that share common business characteristics in the area platform business, we aim to consolidate common indirect functions and management resources, and thereby increase profitability.

Q7 What is the outline and objective of the business segment change in April 2022?

A From the current first quarter of FY3/2023, the segment classification has been changed from the previous three segments (Manufacturing, Solution, and Engineering) to five segments (Manufacturing, Area, Solution, Engineering, and Overseas). The objective of the new segmentation that corresponds to each of the growth strategies set forth in the ongoing Fourth Medium-Term Business Plan is for us to become more agile and clearer in promoting our business. For a summary of each segment, please refer to the Appendix in Financial Results Briefing Material.

Q8 I am concerned about the impact of the global economic downturn on manufacturing worker dispatch. Any thoughts on this issue?

A Mainly due to semiconductor inventory adjustments and other factors, demand for workers by semiconductor manufacturing equipment (SME) makers and semiconductor makers has shown a sign of slowdown since the fall of 2022. Some clients in the Manufacturing Business are suspending or postponing to satisfy demand for additional workers, and we expect this situation to continue in the short term. Meanwhile, efforts by the Area Business to expand business have worked well and a certain level of order backlogs for the entire UT Group has been secured.

As shown in the 3Q financial results briefing material, looking back on the past, the UT Group has pursued the top share strategy to capture the economic recovery that follows the economic downturn and has increased its market share. Since the global financial crisis (around 2008), we have strongly promoted the top share strategy, which aims to capture the top share in the number of dispatched workers at client factories by being close to clients in service offerings. As a result of strengthening relationships with client companies on a daily basis, we have been asked later than our peers to reduce workers when production declines at client factories and our rate of decline in dispatched workers is much smaller than those of our peers. During the subsequent period of expansion of production volume, we have further expanded our share of the factory by taking advantage of the Group's hiring capability and quickly hiring to fill open spots for dispatched workers. In fact, UT's market share has increased from around 5% in FY3/2020 to 8.5% after the COVID-19 pandemic. In the future, even if demand for dispatch workers decreases for a certain period of time, we believe that the top share strategy will enable us to keep the impact to a minimum. On top of that, we are developing a foundation so that we can demonstrate our strength to further grow during the succeeding economic recovery period.

Manufacturing Business

Q9 What is the outline of the Manufacturing Business?

A In the first nine months of FY3/2023, the "Transportation Equipment" subsegment continued to experience production adjustments by automobile-related manufacturers due to a shortage of parts and materials. The "Industrial and Commercial Machinery" and "Electronics" subsegments have cautiously carried out hiring activities since the beginning of autumn, taking into account customer conditions such as postponing new demand for increased headcount due to the impact of inventory adjustments in semiconductors and other factors. Under these circumstances, the number of technical employees increased slightly year-on-year, and segment sales increased due to the promotion of high-level human resource management and the dispatch of highly-skilled workers who were developed in-house. In terms of expenses, segment profit increased due to successful efforts to reduce SG&A expenses such as streamlining hiring-related expenses.

Q10 What is the impact of the current reduction in automobile production?

A In the Transportation Equipment subsector, although automobile-related manufacturers' production adjustments continued mainly due to shortages in parts supply, the amount of decrease in gross profit has been decreasing from April-June to July-September to October-December and the immediate impact is extremely limited.

Q11 What is the status of the Technology Skill Development Centers?

A In December 2020, the UT Group Technology Skill Development Center was established in Kitakami City, Iwate Prefecture, to train manufacturing engineers in the semiconductor field. We then established three centers: in Yokkaichi City, Mie Prefecture, and Kumamoto City, Kumamoto Prefecture in March 2021, and in Osaka City, Osaka Prefecture in May 2021. Using a skill development program specialized for SME engineers, we are developing manufacturing

operators who have experience in the manufacturing process and promoting their advance in career to manufacturing engineers. We are thereby focusing on producing engineers. As of April 30, 2022, manufacturing engineers who graduated from the Technology Skill Development Center surpassed 1,000, and our original plan to "develop and produce 3,000 manufacturing engineers in three years from FY3/2022 to FY3/2024" has been revised upward to "develop and produce 5,000 engineers in four years up to the end of FY3/2025."

Area Business

Q12 What is the outline of the Area Business?

A The Area Business strived to develop new clients and deal with more diversified job openings of its existing clients in each of its operating areas, so that to respond to diverse needs of job applicants. The segment conducted hiring activities accordingly, which resulted in a significant increase in the number of technical employees and sales growth in the first nine months of FY3/2023. Segment profit also increased due to efforts to reduce SG&A expenses, such as commonizing the operating base through the Group's major reorganization on April 1, 2022.

Q13 What is your view on the market expansion potential of the Area Business?

A In the Area Business, we are not limited to the manufacturing industry but also developing and handling projects in a wide range of job categories across Japan. It has been stated that the number of dispatched workers nationwide is approximately 1.4 million (according to the Ministry of Internal Affairs and Communications' Basic Labor Force Survey in FY2021), but we have only approximately 13,000 employees in the Area Business, which accounts for a market share of less than 1%. We therefore believe that there is considerable room for market development in the future, leveraging our Group's strength in hiring and M&A.

Solution Business

Q14 What is the outline of the Solution Business?

A In the first nine months of FY3/2023, the Solution Business segment sales decreased as the positive effects of sales increase from UT FSAS Creative, which became a consolidated subsidiary in October 2021, came to an end and due to the sale of UT System Products Co., Ltd. at the end of March 2022. The segment, however, increased profits due to an increase in the number of technical employees at the existing subsidiaries and an increase in operation at some contract sites.

Q15 Will you explain about the In-house Solution® project for large corporate groups?

A The Solution Strategy, which is one of the growth strategies of the Fourth Medium-Term Business Plan, focuses on supporting personnel mobilization and further expanding UT's business base. Specifically, UT Group takes over operations in non-core businesses, such as manufacturing of non-core products and office worker dispatching, as well as personnel engaged in these areas from large corporate groups which need to reorganize operations due to changes in their business environment and management strategy. Among several schemes, representative ones are 1) to create subsidiaries through M&A; 2) to form joint ventures based on joint investment; 3) carve-outs; and 4) the In-house Solution®. The most unique scheme is the "In-house Solution®", in which UT Group accepts the transfer of employees of a client manufacturing company and receives the outsourced work of its manufacturing line. We have so far accepted a total of about 2,700 employees from 13 clients as our full-time employees, and have enhanced the relationship of trust with these companies by maintaining continuity in these employees' employment and career.

We will continue to expand this business, which will contribute to the resolution of management issues that are unique to large corporate groups, such as an inflexible workforce, a review of the business portfolio, and the reemployment of retiring employees.

Engineering business

Q16 What is the outline of the Engineering Business?

A In first nine months of FY3/2023, approximately 200 new graduates who joined UT Group in April 2022 were assigned and in active operation at an early stage. Profit margin increased as the segment's efforts to develop and assign new graduates have been successful and the new graduates who joined this year were assigned and became operational at an earlier time than those who joined in the previous year. In addition, order booking was favorable for both the construction and IT fields, and the number of technical employees increased y-o-y, resulting in an increase in segment sales and profit.

Overseas business

Q17 What is the outline of the Overseas Business?

A In first nine months of FY3/2023, Vietnam's economy achieved a clear recovery, as COVID-19 restrictions were lifted and GDP maintained high growth. The Overseas Business has expanded its business areas from the southern region centering on Ho Chi Minh City, Vietnam, where it has offices, to the northern region centering on Hanoi, and made efforts to acquire contracts from Japanese companies. The number of technical employees tends to seasonally decrease around the time of the Tet Lunar New Year holiday (from late January to mid- February) in Vietnam, but the relaxation of COVID-19 restrictions in October 2021 led to lifting of restrictions in production activities. As a result, a higher number of technical employees continued be active in operation in 2022 compared to the previous year, and the Overseas Business increased sales and profit.

(Please note that the Overseas Business recorded its results for the January-September 2022 period in the first nine months of FY3/2023 with a delay of three months because its settlement date was the last day of December.)

Q18 What is the positioning and objective of the Overseas Business?

A Japan's domestic labor population is on a declining trend, and we believe it is certain that the shortage of manpower will become more serious in the future. In the manufacturing industry, there is a trend to utilize non-Japanese workers, including foreign technical interns, and the number of non-Japanese working in Japan is on an increasing trend (despite a temporary decline caused by the COVID-19 pandemic). However, it is also true that after returning from Japan, these workers who have acquired skills in Japan have no job or are unable to work in a job that demonstrates their skills.

In Japan, UT Group has been engaged in the foreign technical interns' management agency business in the Manufacturing Business. By connecting this with the Overseas Business, we will support the career formation of foreign technical interns and aim to create a workplace where they can reliably work in their home country.

Q19 Please tell us the details of the stock-based compensation expenses that was recorded at this time.

A In light of the increased probability of achieving the performance conditions for the exercise of stock acquisition rights (performance-linked stock acquisition rights) announced on May 20, 2020 (EBITDA of 15 billion yen to be achieved in FY3/2023), we recorded stock-based compensation expenses of 5.5 billion yen in the consolidated statements of income for the first nine months of FY3/2023. They are recognized as expense for accounting purposes and do not involve cash-out. After exercising the rights, they will be transferred to stated capital and additional paid-in capital on the balance sheet. They are temporary and do not affect the consolidated statements of income for FY3/2024 and thereafter.

Q20 Please explain about the revision of the Fourth Medium-Term Business Plan which was announced on May 13, 2022.

A The Fourth Medium-term Business Plan started amid the uncertain outlook due to the continued spread of COVID-19 infections. However, UT Group managed to minimize the COVID-19 impact in FY3/2021, the first year of the plan, and implemented aggressive hiring activities during the subsequent period of a sharp recovery in personnel demand. This resulted to realize its sales target for FY3/2023 one year ahead of schedule in FY3/2022. In addition, we have steadily advanced the three growth strategies to significantly increase the number of technical employees and sales. In April 2022, we implemented measures to improve profitability, such as the corporate reorganization, including the integration of operating companies, and the establishment of a new hiring infrastructure. As a result of these efforts, we believe that the probability of reaching EBITDA of 15 billion yen in FY3/2023, one year ahead of the initially planned year of FY3/2024, is increasing.

As for the future business environment, despite the immediate concerns about resource price rises and inflation, the labor shortage in the manufacturing industry is expected to continue for the foreseeable future, and the supply and demand balance for personnel will continue to be tight.

In light of the above-mentioned establishment of our growth base and business environment outlook, we have decided to revise our earnings targets as shown below, anticipating sufficient opportunities to further expand our share of existing businesses by continuing to promote the three business strategies of the Fourth Medium-term Business Plan. The sales target for FY3/2023 has incorporated the impact of the sale of the operating company as of March 31, 2022, as stated in Q5.

		Fourth Medium-Term Business Plan					
		FY3/2020	FY3/2021	FY3/2022	FY3/2023E	FY3/2024E	FY3/2025E
Net sales (Billion yen)	Initial plan	-	103.8	130.0	150.0	180.0	200.0
	Actual*/Revised	101.1*	115.1*	156.7*	180.0	220.0	270.0
EBITDA (Billion yen)	Initial plan	-	4.9	10.0	12.0	15.0	20.0-30.0
	Actual*/Revised	8.6*	7.9*	7.5*	15.0	19.0	25.0

Q21 Will you talk about your shareholder return policy and how you think about the return to shareholder for FY3/2023?

A Our policy is to “achieve sustainable growth in corporate value, driven by aggressive business development and based on financial stability.” We regard returning profits to shareholders as

an important management issue. We are committed to appropriately returning profit to shareholders, in consideration of the level of UT Group's stock price, business environment, etc., and our base is a total return ratio of 30% or more via dividend payment and acquisition of own shares, which contribute to enhancing capital efficiency.

As for the return to shareholders for FY3/2023, we plan to return to shareholders the amount equivalent to 30% of the estimated net profit of 8.7 billion yen excluding the above-mentioned stock-based compensation expenses, and to make a total shareholder return ratio to be 81%.

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