Alpha-Win Company Research Report

CUBE SYSTEM INC.
(2335 TSE Prime)

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Alpha-Win Capital Inc. Research Department
http://www.awincap.com/

● Summary

◆ Independent, mid-tier system integrator with long-term, stable growth

・CUBE SYSTEM INC. (hereinafter, the "Company") is an independent, mid-tier system integrator listed on the TSE Prime. Its main customers include the Nomura Research Institute (NRI) and the Fujitsu Group, and it develops systems and provides services mainly for the financial, distribution, transportation, and telecommunication industries. Its strengths are its excellent customer base, extensive experience, high credibility, and the technology and expertise that it has built over the years. Founded in 1972, it has 50 years of history.

・With the exception of one fiscal year, the Company has been continuously increasing sales YoY for the past 21 years. During this period, the annual sales growth rate (simple average of the rate of increase in sales) was +6.1% and the annual recurring profit growth rate (simple average) was +7.3%; it has been steadily expanding its business over the long term and has always maintained a profit. Its recurring margin has stably been around 7% and the increase in sales has been contributing directly to increases in profit, dividend, and market capitalization. In FY 2022 (note that the Company's fiscal year is March-ending, i.e., FY 2022 ended in March 2022), it achieved record-high sales and profits. It also increased dividend for the third year in a row.

・In April 2022, it transited from the TSE First Section to the newly established Prime Market.

◆ Results for the first half of this fiscal year (cumulative through Q2): Sales decreased by 2.1% YoY, and operating profit decreased by 19.9% YoY in a double-digit decline. The main factors were changes in the IT investment policies of some of the customers and delays in the effects of profit-improvement measures.

First Half: Overview

・In the first half of the fiscal year ending March 31, 2023 (April-September 2022; hereinafter, the "first half" or "H1"), sales were Y7,892 million (-2.1% YoY), operating profit was Y598 million (-19.9% YoY), recurring profit was Y598 million (-21.0% YoY), and net profit attributable to owners of the parent (hereinafter, "net profit") was Y388 million (-22.6% YoY) (Figures 1-4 on page 2).

・Results fell short of the plan for the first half made at the beginning of the fiscal year: sales were Y263 million lower (-3.2% compared to the plan), operating profit was Y151 million lower (-20.1%), and net profit was Y117 million lower (-23.1%) (center left column of Figure 1 on page 2).

・The factors behind this were (1) some of the customers changed their IT investment policy (theme), and as a result, the expected sales were not recorded in the first half due to the postponement of large projects (presumably pertaining to upstream process development in the SI Business, whose orders had been received through major SIers) and (2) measures to improve profitability had been less effective than expected (insufficient profit-improving effects from reallocation of projects and resources, automation, and multitasking).

・Despite the lower sales and profits, the Company posted the second highest levels of sales and operating profit for the first half, following the record-high sales and profit of the previous fiscal year's first half.

・The gross margin declined by 0.4 percentage point from 21.3% in the first half of the previous fiscal year to 20.9% in the first half of this fiscal year due to an increase in subcontracting cost and other costs. The SG&A expenses increased by Y81 million (+8.4% YoY) from Y971 million to Y1,053 million (in the same order as above) as the Company strengthened its management foundation (investment in people development and IT), and the SG&A expenses ratio rose from 12.1% to 13.3%. As a result, the operating margin declined by 1.7 percentage points, from 9.3% to 7.6%.

・Regarding the SG&A expenses, personnel expenses increased by about Y30 million (+7.7% YoY) from Y380 million to Y410 million due to the increase in the number of employees, and the ratio of personnel expenses to sales rose by 0.5 percentage point from 4.7% to 5.2%. Non-personnel SG&A expenses also increased by Y51 million (+8.7% YoY), from Y591 million to Y642 million, due to the development of the management foundation

(people development and IT investment).

・There was no significant change in non-operating profit or loss, but there was greater exchange loss on transactions with the subsidiary in Vietnam in the first half of this fiscal year due to the weaker yen (from -Y5 million in the previous first half to -Y9 million in this first half, due to the difference in exchange rate at the time of contract and settlement). Consequently, although a profit of Y5 million was posted in the previous fiscal year's first half, a loss of Y4 million was posted in this first half. With no extraordinary income or loss, net profit resulted in a decline of about 20%, much like the operating and recurring profits.

・Comparing results of the first quarter (April-June 2022; hereinafter "Q1") with Q2 (July-September 2022), the YoY sales decline rate improved by 0.3% from -2.4% to -1.8% in the order of Q1 to Q2. Similarly, the rate of decline in operating profit and net profit improved by 17.0%, from -28.1% to -11.1%, and by 24.5%, from -34.0% to -9.5%, respectively (center right column of Figure 1).

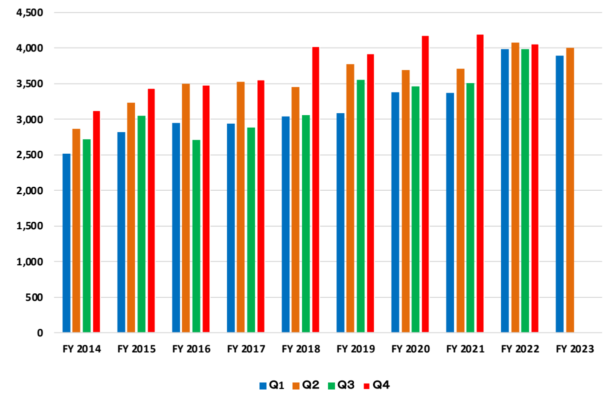
【Figure 1】Summary of Results in the First Half

First-Half Results	First Half FY 2022	First Half FY 2023	YoY Change in Amount / Diff.	% Change	First Half FY 2023	First Half FY 2023	% Diff. from Plan
	A: Results	B: Results	YoY Change: C = B - A	YoY Ratio: C/A	D: Initial Forecast	Diff. from Plan: E = B - D	Ratio of Diff. to Plan : E/D
Unit: million yen, %	Apr-Sept 2021	Apr-Sept 2022	YoY: million yen, %	YoY: %	Apr-Sept 2022	Apr-Sept 2022	%
Consolidated Sales	8,060	7,892	-168	-2.1	8,155	-263	-3.2
Gross Profit	1,718	1,651	-67	-3.9	-		-
Gross Margin (%)	21.3	20.9	-0.4		-		-
SG&A Expenses	971	1,053	81	8.4	-		-
SG&A Expenses Ratio (%)	12.1	13.3	1.3		-		-
Operating Profit	746	598	-148	-19.9	749	-151	-20.1
Operating Margin (%)	9.3	7.6	-1.7		9.2		-
Recurring Profit	752	595	-158	-21.0	754	-159	-21.1
Recurring Margin (%)	9.3	7.5	-1.8		9.2		-
Net Profit	502	388	-113	-22.6	505	-117	-23.1
Net Margin (%)	6.2	4.9	-1.3		6.2		-

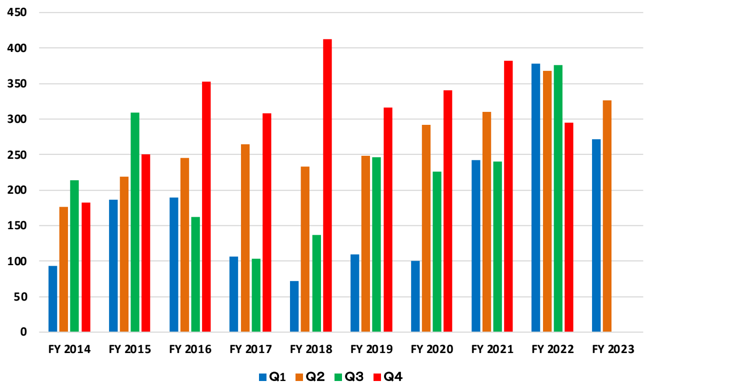
First-Half Results	Q1 FY 2022	Q1 FY 2023	YoY Change in Amount / Diff.	% Change	Q2 FY 2022	Q2 FY 2023	YoY Change in Amount / Diff.	% Change
	F: Results	G: Results	YoY Change: H = G - F	YoY Ratio: H/F	I: Results	J: Results	YoY Change: K = J - I	YoY Ratio: K/I
Unit: million yen, %	Apr-June 2021	Apr-June 2022	YoY: million yen, %	YoY: %	July-Sept 2021	July-Sept 2022	YoY: million yen, %	YoY: %
Consolidated Sales	3,987	3,892	-94	-2.4	4,073	4,000	-73	-1.8
Gross Profit	863	785	-78	-9.0	856	866	10	1.2
Gross Margin (%)	21.6	20.2	-1.4		21.0	21.6	0.6	
SG&A Expenses	483	513	30	6.2	488	540	51	10.5
SG&A Expenses Ratio (%)	12.1	13.2	1.0		12.0	13.5	1.5	
Operating Profit	379	272	-107	-28.1	367	326	-41	-11.1
Operating Margin (%)	9.5	7.0	-2.5		9.0	8.2	-0.9	
Recurring Profit	390	271	-119	-30.5	362	324	-39	-10.7
Recurring Margin (%)	9.8	7.0	-2.8		8.9	8.1	-0.8	
Net Profit	264	173	-91	-34.0	238	215	-23	-9.5
Net Margin (%)	6.6	4.9	-1.7		5.8	5.4	-0.5	

(Note) Figures 1-4 have been prepared by Alpha-Win Research Dept. based on the financial results summary and the financial results briefing supplemental materials. Forecasts are from the Company' plan. Throughout this report, due to processing of data during calculations, values for the same item may slightly differ. The same applies to the rest of this document. Figure 5 is from the financial results briefing supplemental materials, with partial revision.

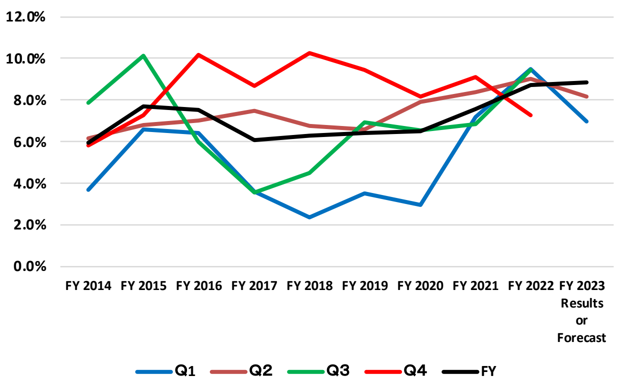
【Figure 2】Quarterly Change in Sales (Unit: million yen)



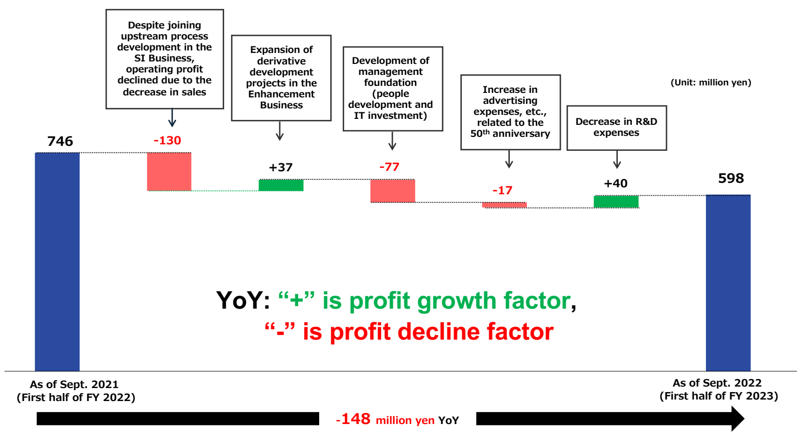
【Figure 3】Quarterly Change in Operating Profit (Unit: million yen)



【Figure 4】Quarterly Change in Operating Margin (Unit: %)



【Figure 5】Factors that Increased/Decreased Operating Profit in the First Half of This Fiscal Year (YoY)



First Half: Factors that Contributed to Increase/Decrease in Operating Profit

・The factors that increased or decreased operating profit in this fiscal year's first half are as shown in Figure 5 on page 2. The decrease in R&D expenses (+Y40 million to profit) and the expansion of derivative development projects in the Enhancement Business (+Y37 million) had a total effect of Y77 million in increasing profit. On the other hand, although the Company joined upstream-process projects in the SI Business, factors including the postponement of project and delays in starting a project caused a large negative impact on profit (-Y130 million). In addition, there was an increase in cost to strengthen the management foundation as part of the strengthened investment in people development and IT (-Y77 million) and an increase in advertising expenses associated with the 50th anniversary commemoration project (-Y17 million), resulting in a decrease in operating profit by Y148 million YoY (-19.9% YoY).

First Half: Progress

・Progress in the first half in terms of the Company's full-year forecast was 45.6% for sales (50.1% in the first half of the previous fiscal year) and 39.1% for operating profit (52.6% in the first half of the previous fiscal year). The simple average of the progress in the first half over the past 10 years, including the previous fiscal year, was 48.8% for sales and 43.5% for operating profit, indicating that the progress with both sales and profit in the first half of the current fiscal year is somewhat slow.

・The Company's financial performance has been characterized by quarterly fluctuations, although the rate of variation has become smaller due to the change in the revenue-recognition standard. Q4 (January-March) has accounted for the highest percentage of the entire year (27.7% and 33.5% of sales and operating profit, respectively, on average over the past nine years, including the previous fiscal year). This is followed by Q2 (July-September; 26.0% and 27.3%, respectively), Q3 (October-December; 23.5% and 23.1%, respectively), and Q1 (April-June; 22.8% and 16.1%, respectively). Consequently, the weight of the second half of the year (October-March) has tended to be higher in past years (averaging 51.2% and 56.5%, respectively, over the same 10-year period). The forecasted progresses in the second half of this fiscal year, which are 54.4% and 60.9%, are 3 to 4 percentage points higher than these averages, respectively (Figures 2 and 3 on page 2).

First Half: Segments

・Overall, sales decreased by Y168 million YoY in the first half. In addition, costs increased and profit margin worsened, and operating profit decreased by Y148 million YoY. Below are the results for the first half by segment.

Results by Service Category (three categories; Figure 6)

・Regarding the System Integration Services (SIS), which is its core business, sales fell by Y333 million YoY (-5.5% YoY) to Y5,734 million. This was because the project for a shipping company in the transportation industry was scaled down, despite the expansion of the system building project for a credit card company in the financial industry. Operating margin fell from 9.7% in the first half of the previous fiscal year to 6.9%, and similarly operating profit fell significantly by Y191 million YoY (-32.4% YoY) to Y398 million.

・In the System Outsourcing Services (SOS), too, although projects for retailers of the distribution industry had expanded, it was not enough to compensate for the scaling down of system building projects for mass retailers. Its sales therefore decreased by Y48 million (-5.1% YoY) to Y888 million and operating margin declined slightly from 7.3% in the first half of the previous fiscal year to 7.1%. Operating profit also decreased slightly by Y6 million (-8.1% YoY) to Y62 million.

・On the other hand, in the Professional Services (ProS), sales increased by Y213 million (+20.2% YoY) to Y1,269 million and operating profit increased by Y49 million (+54.6% YoY) to Y137 million due to the expansion of system building projects for a telecommunications company in the telecommunication industry and for a postal service company. It was the only category in which the operating margin rose, specifically, from 8.4% to 10.8%.

【Figure 6】Change in Results by Service Category in the First Half

Consolidated	First-Half Results		First Half FY 2022	First Half FY 2023	Change in Amount / Diff.	% Change	% of Total Amount of Change	% of Total	Q1 FY 2022	Q1 FY 2023	Change in Amount / Diff.	% Change	% of Total Amount of Change	% of Total	Q2 FY 2022	Q2 FY 2023	Change in Amount / Diff.	% Change	% of Total Amount of Change	% of Total
			A: Results	B: Results	YoY Change: C = B - A	YoY Ratio: C/A	Breakdown of C	Breakdown of B	D: Results	E: Results	YoY Change: F = E - D	YoY Ratio: F/D	Breakdown of F	Breakdown of E	G: Results	H: Results	YoY Change: I = H - G	YoY Ratio: I/G	Breakdown of I	Breakdown of H
	Unit: million yen, %		Apr-Sept 2021	Apr-Sept 2022	YoY: million yen, %	YoY: %	%	%	Apr-June 2021	Apr-June 2022	YoY: million yen, %	YoY: %	%	%	July-Sept 2021	July-Sept 2022	YoY: million yen, %	YoY: %	%	%
Category	Overall Sales	Service Name	8,060	7,892	-168	-2.1	-100.0	100.0	3,987	3,892	-94	-2.4	-100.0	100.0	4,073	4,000	-73	-1.8	-100.0	100.0
By Service Category	Sales	System Integration: SIS	6,067	5,734	-333	-5.5	-197.8	72.7	2,985	2,821	-163	-5.5	-173.4	72.5	3,082	2,913	-169	-5.5	-230.4	72.8
		System Outsourcing: SOS	936	888	-48	-5.1	-28.5	11.3	493	440	-53	-10.9	-56.4	11.3	443	448	5	1.1	6.8	11.2
		Professional: ProS	1,056	1,269	213	20.2	126.5	16.1	508	631	123	24.3	130.9	16.2	548	638	90	16.4	122.7	15.9
	Overall Operating Profit		746	598	-148	-19.9	-100.0	100.0	379	272	-107	-28.1	-100.0	100.0	367	326	-41	-11.1	-100.0	100.0
	Operating Profit	System Integration: SIS	589	398	-191	-32.4	-129.5	66.5	311	172	-138	-44.6	-130.2	63.2	278	226	-52	-18.7	-127.6	83.1
		System Outsourcing: SOS	68	62	-6	-8.1	-4.1	10.4	37	34	-2	-5.6	-1.9	12.5	31	28	-3	-9.7	-7.4	10.3
		Professional: ProS	88	137	49	54.6	33.2	22.9	30	64	34	111.3	32.1	23.5	58	73	15	25.9	36.8	26.8
	Overall Operating Margin		9.3	7.6	-1.7				9.5	7.0	-2.5				9.0	8.2	-0.9			
	Operating Margin (%)	System Integration: SIS	9.7	6.9	-2.8				10.4	6.1	-4.3				9.0	7.8	-1.3			
		System Outsourcing: SOS	7.3	7.1	-0.2				7.5	7.9	0.4				7.0	6.3	-0.7			
		Professional: ProS	8.4	10.8	2.4				6.1	10.3	4.2				10.6	11.4	0.9			

(Note) Prepared by Alpha-Win Research Dept. based on the financial results summary and financial results briefing supplemental materials. "% of Total Amount of Change" is the proportion to the absolute amount of change; the same applies to Figures 7-10.

Results by Industry (four industries; Figure 7)

・Sales and profits decreased for all three industries excluding the financial industry. Regarding the financial industry whose sales accounted for about 30% of the total in the first half, sales increased significantly by 25.5% YoY to Y2,337 million due to the expansion of system building projects for a credit card company as mentioned earlier and for an insurance company. In addition, of all four industries, this was the single industry whose operating margin had improved, rising from 7.7% in the first half of the previous fiscal year to 8.7% in the first half of this fiscal year. Its operating profit also grew significantly by 42.3% YoY (+Y60 million YoY) to Y202 million.

・Regarding the distribution industry, the transportation & telecommunication industry, and other industries, sales decreased due to the scaling down of system building projects. Operating margin also fell, and operating profit resulted in a decline for each. Particularly significant were the decrease in operating profit of the transportation & telecommunication industry, which had contributed significantly to profit in the first half the previous fiscal year, by half from Y285 million to Y147 million, and the decrease in the operating profit of the distribution industry from Y163 million to Y114 million.

【Figure 7】Change in Results by Industry in the First Half

Consolidated	First-Half Results		First Half FY 2022	First Half FY 2023	Change in Amount / Diff.	% Change	% of Total Amount of Change	% of Total	Q1 FY 2022	Q1 FY 2023	Change in Amount / Diff.	% Change	% of Total Amount of Change	% of Total	Q2 FY 2022	Q2 FY 2023	Change in Amount / Diff.	% Change	% of Total Amount of Change	% of Total
			A: Results	B: Results	YoY Change: C = B - A	YoY Ratio: C/A	Breakdown of C	Breakdown of B	D: Results	E: Results	YoY Change: F = E - D	YoY Ratio: F/D	Breakdown of F	Breakdown of E	G: Results	H: Results	YoY Change: I = H - G	YoY Ratio: I/G	Breakdown of I	Breakdown of H
	Unit: million yen, %		Apr-Sept 2021	Apr-Sept 2022	YoY: million yen, %	YoY: %	%	%	Apr-June 2021	Apr-June 2022	YoY: million yen, %	YoY: %	%	%	July-Sept 2021	July-Sept 2022	YoY: million yen, %	YoY: %	%	%
Category	Overall Sales	Industry	8,060	7,892	-168	-2.1	-100.0	100.0	3,987	3,892	-94	-2.4	-100.0	100.0	4,073	4,000	-73	-1.8	-100.0	100.0
By Industry	Sales	Finance	1,861	2,337	475	25.5	282.2	29.6	934	1,128	193	20.7	205.3	29.0	927	1,209	282	30.4	384.5	30.2
		Distribution	1,696	1,658	-37	-2.2	-22.0	21.0	815	785	-29	-3.6	-30.9	20.2	881	873	-8	-0.9	-10.9	21.8
		Telecommunication & Transportation	2,166	1,571	-594	-27.5	-352.9	19.9	1,062	826	-235	-22.2	-250.0	21.2	1,104	745	-359	-32.5	-489.5	18.6
		Manufacturing (other)	657	723	66	10.1	39.2	9.2	318	344	26	7.9	27.7	8.8	339	379	40	11.8	54.5	9.5
		Government (other)	476	427	-49	-10.3	-29.1	5.4	244	206	-38	-15.7	-40.4	5.3	232	221	-11	-4.7	-15.0	5.5
		Other (other)	1,201	1,173	-28	-2.4	-16.6	14.9	610	601	-9	-1.5	-9.6	15.4	591	572	-19	-3.2	-25.9	14.3
	Overall Operating Profit		746	598	-148	-19.9	-100.0	100.0	379	272	-107	-28.1	-100.0	100.0	367	326	-41	-11.1	-100.0	100.0
	Operating Profit	Finance	142	202	60	42.3	40.7	33.8	75	101	26	35.0	24.3	37.1	67	101	34	50.7	83.5	30.9
		Distribution	163	114	-48	-29.5	-32.5	19.0	84	49	-35	-42.2	-32.8	18.0	79	65	-14	-17.7	-34.4	19.9
		Telecommunication & Transportation	285	147	-138	-48.4	-93.5	24.6	148	70	-78	-52.6	-73.0	25.7	137	77	-60	-43.8	-147.3	23.6
		Manufacturing (other)	34	17	-17	-48.5	-11.5	2.8	20	5	-15	-72.1	-14.0	1.8	14	12	-2	-14.3	-4.9	3.7
		Government (other)	40	23	-17	-42.4	-11.5	3.8	24	11	-13	-55.5	-12.2	4.0	16	12	-4	-25.0	-9.8	3.7
		Other (other)	80	91	11	14.4	7.5	15.2	24	34	10	39.8	9.4	12.5	56	57	1	1.8	2.5	17.5
	Overall Operating Margin		9.3	7.6	-1.7		-	-	9.5	7.0	-2.5		-	-	9.0	8.2	-0.9		-	-
	Operating Margin (%)	Finance	7.7	8.7	1.0				8.1	9.0	0.9				7.2	8.4	1.1			
		Distribution	9.6	6.9	-2.7				10.4	6.3	-4.1				9.0	7.4	-1.5			
		Telecommunication & Transportation	13.2	9.4	-3.8				14.0	8.5	-5.5				12.4	10.3	-2.1			
		Manufacturing (other)	5.2	2.5	-2.7				6.5	1.7	-4.8				4.1	3.2	-1.0			
		Government (other)	8.6	5.5	-3.1				10.2	5.4	-4.8				6.9	5.4	-1.5			
		Other (other)	6.7	7.8	1.1				4.0	5.7	1.7				9.5	10.0	0.5			

(Note) Prepared by Alpha-Win Research Dept. based on the financial results summary and financial results briefing supplemental materials.

Results by Business Model (three models; Figure 8)

・Regarding the Enhancement Business, which accounted for 74% of sales and 84% of operating profit, sales increased by +3.2% compared to the previous fiscal year's first half (+Y182 million YoY) to Y5,814 million due to the expansion of projects for a credit card company, a telecommunications company, and retailers. In addition to sales growth, operating margin rose from 8.0% to 8.6%, and operating profit increased by 11.4% YoY (+Y51 million) to Y502 million.

・In the SI Business (Lift & Shift: moving from the legacy environment to the cloud environment in "Lift," and stepwise system restructuring with optimization for the cloud environment in "Shift"), which accounted for 23% of sales and 15% of operating profit, the Company placed a focus on collaborating with cloud vendors. However, due to the scaling down of the system building project for a shipping company, sales decreased by 19.9% (-Y455 million) compared to the first half of the previous fiscal year to Y1,833 million and operating profit decreased significantly by 69.4% YoY (-Y204 million) to Y90 million. Operating margin fell sharply from 12.8% to 4.9%.

・The Digital Business is small in scale, accounting for only 3% of total sales. However, due to new orders for DX projects in the distribution industry, new projects gained through the collaborative consultation business, and expansion of projects in the existing areas of business, its sales grew by 75.0% YoY (+Y104 million) to Y243 million. Operating profit/loss was close to zero in the first half of the previous fiscal year (profit of Y1 million), but the profit slightly increased to Y5 million in the first half of this fiscal year.

・Both the Digital Business and the Enhancement Business are performing well, with both sales and profits increasing. The overall decline in sales and profits in the first half of this fiscal year was mainly due to the SI Business and its postponement of large projects as mentioned above.

【Figure 8】Change in Results by Business Model in the First Half

Consolidated	First-Half Results		First Half FY 2022	First Half FY 2023	Change in Amount / Diff.	% Change	% of Total Amount of Change	% of Total	Q1 FY 2022	Q1 FY 2023	Change in Amount / Diff.	% Change	% of Total Amount of Change	% of Total	Q2 FY 2022	Q2 FY 2023	Change in Amount / Diff.	% Change	% of Total Amount of Change	% of Total
			A: Results	B: Results	YoY Change: C = B - A	YoY Ratio: C/A	Breakdown of C	Breakdown of B	D: Results	E: Results	YoY Change: F = E - D	YoY Ratio: F/D	Breakdown of F	Breakdown of E	G: Results	H: Results	YoY Change: I = H - G	YoY Ratio: I/G	Breakdown of I	Breakdown of H
	Unit: million yen, %		Apr-Sept 2021	Apr-Sept 2022	YoY: million yen, %	YoY: %	%	%	Apr-June 2021	Apr-June 2022	YoY: million yen, %	YoY: %	%	%	July-Sept 2021	July-Sept 2022	YoY: million yen, %	YoY: %	%	%
Category	Overall Sales	Business Model	8,060	7,892	-168	-2.1	-100.0	100.0	3,987	3,892	-94	-2.4	-100.0	100.0	4,073	4,000	-73	-1.8	-100.0	100.0
By Business Model	Sales	Digital Business	139	243	104	75.0	61.8	3.1	64	102	37	58.3	39.4	2.6	75	141	66	88.0	90.0	3.5
		SI Business	2,289	1,833	-455	-19.9	-270.3	23.2	1,082	854	-228	-21.1	-242.6	21.9	1,207	979	-228	-18.9	-310.9	24.5
		Enhancement Business	5,632	5,814	182	3.2	108.1	73.7	2,840	2,936	96	3.4	102.1	75.4	2,792	2,878	86	3.1	117.3	71.9
	Overall Operating Profit		746	598	-148	-19.9	-100.0	100.0	379	272	-107	-28.1	-100.0	100.0	367	326	-41	-11.1	-100.0	100.0
	Operating Profit	Digital Business	1	5	4	454.1	2.7	0.8	0	-4	-4	To loss	-3.7	-1.5	1	9	8	800.0	19.6	2.8
		SI Business	294	90	-204	-69.4	-138.3	15.0	125	34	-91	-72.6	-85.2	12.5	169	56	-113	-66.9	-277.4	17.2
		Enhancement Business	451	502	51	11.4	34.6	83.9	253	242	-11	-4.4	-10.3	89.0	198	260	62	31.3	152.2	79.6
	Overall Operating Margin		9.3	7.6	-1.7		-	-	9.5	7.0	-2.5		-	-	9.0	8.2	-0.9		-	-
	Operating Margin (%)	Digital Business	0.7	2.1	1.3		-	-	0.0	-3.9	-3.9				1.3	6.4	5.0			
		SI Business	12.8	4.9	-7.9		-	-	11.6	4.0	-7.6				14.0	5.7	-8.3			
		Enhancement Business	8.0	8.6	0.6		-	-	8.9	8.2	-0.7				7.1	9	1.9			

(Note) Prepared by Alpha-Win Research Dept. based on the financial results summary and financial results briefing supplemental materials.

Sales by Customer Group (five customer groups; Figure 9)

・Sales to NRI, which accounted for about 48% of total sales, declined by Y375 million (-9.0% YoY) from Y4,184 million in the first half of the previous fiscal year to Y3,809 million in the first half of the current fiscal year. This decline accounted for 223% of the overall amount of sales decline (absolute amount of decline of Y168 million) and was the largest downside factor (presumably due to the SI Business for the transportation industry). Sales to the AEON Group also declined by Y23 million YoY.

・In contrast, sales to the Fujitsu Group (hereinafter, "G" stands for Group) were solid, increasing by Y74 million. Sales to the Mizuho G also increased by Y37 million and sales to other customers increased by Y118 million.

【Figure 9】Change in First-Half Sales by Customer Group

Group	First Half FY 2021	First Half FY 2022	First Half FY 2023	Percent of Total for the First Half of FY 2023	Change in Amount	% Change	% of Total Amount of Change
Unit	Million yen	Million yen	Million yen	%	Million yen	%	%
NRI	3,457	4,184	3,809	48.3	-375	-9.0	-223.2
Fujitsu	1,325	1,539	1,613	20.5	74	4.8	44.0
Aeon	394	380	356	4.5	-23	-6.1	-13.7
Mizuho	268	297	334	4.2	37	12.5	22.0
Other	1,637	1,659	1,778	22.5	118	7.1	70.2
Total	7,083	8,060	7,892	100	-168	-2.1	100.0

(Note) Prepared by Alpha-Win Research Dept. based on the financial results briefing supplemental materials.

Number of Employees and Productivity

・In the Company's business model, sales growth is generally directly correlated with the number of employees. Its human resource capacity has been expanding, with the total number of employees in Japan and overseas steadily increasing from 791 in September 2020 (end of month; the same applies to the rest) → 815 in September 2021 (+24 or +3.0%) → 869 in September 2022 (+54 or +6.6%). However, since there is still strong potential demand for system development (DX businesses and non-face-to-face businesses such as those related to remote work, EC, and AI), the Company is somewhat short of staff. Since human resources seem to be the main bottleneck to further growth, it has been working on increasing the number of employees through strengthened new-graduate and mid-career recruitment. It has also been improving productivity by raising the staff operation rate, based on management indicators of sales per employee in Japan (in the order of H1 FY 2021 → H1 FY 2022 → H1 FY 2023: 10,033 thousand yen / person → 11,164 thousand yen / person → 10,494 thousand yen / person) and operating profit per employee in Japan (in the same order: 782 thousand yen / person → 1,034 thousand yen / person → 795 thousand yen / person).

Balance Sheet

・There has been no significant change in the balance sheet as of the end of the first half. The Company has ample liquidity on hand, with cash & deposits of Y5.0 billion (3.5 months' worth of average monthly sales; its debt is Y240 million and therefore it is essentially debtless). With also a current ratio of 384.0% and an equity ratio of 73.4%, its financial standing is firm. Going forward, the key points will be the enhancement of the return of profit to shareholders and the effective utilization of its excess capital for future growth through, for instance, M&As, business alliances, investments, and financing.

◆No change to the full-year forecast since the beginning of the fiscal year. Planning for a large dividend hike including commemorative dividend.

Second Half: Company Forecast

・The Company expects a large increase in sales and profit in the second half of the fiscal year, with sales of Y9,408 million (+Y1,369 million or +17.0% YoY), operating profit of Y932 million (+Y261 million or +38.9% YoY), operating margin of 9.9% (+0.8 percentage point YoY), and net profit of Y612 million (+Y169 million or +38.1% YoY) (Figure A on page 8; "FY 2023 H2 CE"). In the second half of the fiscal year, the Company expects to post record highs for sales and each of the profit consecutively, following the previous fiscal year.

・The order backlog at the end of this first half was Y4,506 million (+Y325 million or +7.8% YoY), having increased from the previous fiscal year. The Company expects orders to remain strong in the second half due to strong demand. By segment, the order backlog has been increasing in all business models, including the Digital Business, and for all industries except the transportation & telecommunication industry (Figure 10 on page 6).

Full Year: Company Forecast

・The Company has not changed its full-year forecast since the beginning of the fiscal year. It plans to achieve sales of Y17,300 million (+7.5% YoY), operating profit of Y1,530 million (+7.9% YoY), net profit of Y1,000 million (+5.9% YoY), and operating margin of 8.8% (8.8% in the previous fiscal year; no change) (Figure A on page 8; "FY 2023 CE"). Continuing from the previous fiscal year, it expects sales and profits to increase during this full fiscal year to hit consecutive record highs for both.

・In terms of the full-year sales forecast by industry, it expects to especially see sales growth in businesses with the financial industry in which orders from banks and insurance companies have been strong (Y3,909 million ⇒ Y4,420 million; +Y510 million or +13.1% YoY; 42.5% of overall sales growth) and with the other industries in which orders for energy- and education-related projects are expected (Y4,562 million ⇒ Y5,420 million; +Y857 million or +18.8% YoY; 71.4% of overall sales growth) (Figure 10).

・Similarly, by business model, sales are expected to increase for all industries. The Digital Business, whose number of orders are increasing, and the SI Business, whose demand has been strong, will be the growth drivers.

・It plans to increase the annual dividend to 50 yen per share, which includes the initially planned annual ordinary dividend of 26 yen per share (11 yen in the first half and 15 yen at the end of the fiscal year) with an additional commemorative dividend of 12 yen per share in both the first and the second half (a total of 24 yen per share) for the celebration of its 50th anniversary on July 5, 2022.

【Figure 10】Orders Received in Each Segment and Full-Year Sales Plan

Unit: million yen		Order Received				Order Backlog				Sales (company plan for FY 2023)				
Segment		First Half FY 2022	First Half FY 2023	Change	% Change	First Half FY 2022	First Half FY 2023	Change	% Change	FY 2022	FY 2023	Change	% Change	% of Total Amount of Change
By Industry	Finance	1,890	2,407	516	27.3	1,094	1,269	174	16.0	3,909	4,420	510	13.1	42.5
	Distribution	1,699	1,897	198	11.7	952	1,177	225	23.6	3,342	3,550	207	6.2	17.3
	Telecommunication & Transportation	2,168	1,436	-731	-33.7	991	669	-321	-32.4	4,285	3,910	-375	-8.8	-31.3
	Other	2,179	2,380	201	9.2	1,142	1,390	247	21.6	4,562	5,420	857	18.8	71.4
	Total	7,937	8,122	184	2.3	4,181	4,506	325	7.8	16,099	17,300	1,200	7.5	100.00
By Business Model	Digital	174	326	151	86.6	91	271	180	198.6	350	780	429	122.6	35.8
	SI Busines	2,317	2,164	-153	-6.6	1,123	1,221	98	8.8	4,645	5,140	494	10.6	41.2
	Enhancement	5,445	5,631	186	3.4	2,966	3,012	46	1.6	11,103	11,380	276	2.5	23.0
	Total	7,937	8,122	184	2.3	4,181	4,506	325	7.8	16,099	17,300	1,200	7.5	100.0

(Note) Prepared by Alpha-Win Research Dept. based on the financial results briefing supplemental materials.

Full Year: Alpha-Win Research Department's Forecast

・Due to concerns over another outbreak of COVID-19 (the eighth wave) and uncertainty over the global situation, some companies with deteriorating business performance have been holding down their IT investments. On the other hand, there are many companies with strong financial performance and that are actively making strategic DX investments (business and process transformation). There seems to be a polarization in IT investment.

・In this environment, the Company has been strategically strengthening efforts to receive orders for system-related projects from the latter group of companies. It has also been shifting to high-profit projects and improving resource efficiency. As a result, the amount of orders received and the order backlog in the first half were solid and have been exceeding those of the same period of the previous fiscal year, as mentioned above.

・The Company has generally been seeing no sign of slowdown regarding negotiations or in receiving orders. There has also been a recovery in demand from the previously stagnant industries such as the financial industry, and the Company has been receiving more new orders for DX and upstream-process projects. It seems to have some leeway in terms of controlling its results, and it has a stable business model based on orders received. Therefore, we had believed that the downside risk is limited for both sales and profit this fiscal year. However, considering the macroeconomic risk factors, we had made a somewhat cautious forecast for the full year compared to the Company (Figure A on page 8; "FY 2023 CE" and "FY 2023 Old E"; "Old E" stands for Alpha-Win's previous forecast).

・We have now revised our full-year forecast slightly downward, though, considering the underachievement of results in the first half of this fiscal year and because the Company's goals for the second half of the fiscal year seem to be somewhat high for sales, operating margin, and operating profit. In the order of our previous forecast ⇒ current forecast, we revised our forecasts from sales of 17,200 ⇒ 17,100 million yen (-100 ⇒ -200 million yen compared to the Company's plan), operating profit of 1,520 ⇒ 1,480 million yen (similarly, -10 ⇒ -50 million yen), net profit of 1,000 ⇒ 970 million yen (0 ⇒ -30 million yen), and operating margin of 8.8% ⇒ 8.7% (the Company's plan is 8.8%) (Figure A on page 8; "FY 2023 Old E" and "FY 2023 New E"). However, even after this revision of financial performance, we believe that Company may be able to achieve a YoY increase in sales and profit, as well as consecutive record highs for both.

Medium Term: Forecast

・Over the medium to long term, the Company intends to build a stable and sustainable business foundation through its proposal-based and contract-based businesses, and shift its business portfolio to the Digital Business and the SI Business in which high growth is expected. In FY 2024, the final year of the current medium-term management plan, the Company plans to achieve sales of Y19.0 billion (+Y1.7 billion from the forecasted sales of the current fiscal year) and operating profit of Y1.71 billion (similarly, +Y180 million).

・We have not changed our medium-term outlook and evaluation of the Company's financial performance, predicting that IT investments will continue to be solid in the next fiscal year onward too. We also have not changed our medium-term forecast of dividend starting next fiscal year (annual increase of +2 yen/share for ordinary dividend).

・IT investments are expected to continue to increase as customers develop new business model to adapt to DX and life co-exiting with COVID-19, strengthen their competitive edge, work on solving employee shortages, and streamline and speed up operations. Therefore, the Company's growth potential is large. We believe that the Company will be able to continue a stable sales and profit growth trend of about 6-10% growth per year, if economic conditions normalize, through the expansion of its areas of business, acquisition of new customers, and improvement of productivity through various measures.

◆ Stock price and characteristics: a domestic-demand-oriented and stable growth stock that has been significantly outperforming the TOPIX over the long term. The level of valuation is about average.

Performance

・Over the past approximately 13 years, the Company's stock price has increased by about 5.2x thanks to its solid financial performance, significantly outperforming the TOPIX (by about +286%). This fiscal year, its stock has been outperforming the TOPIX by 4.5% since the announcement of dividend hike due to commemorative dividend in July. After the announcement of the first-half results (after the closing price on November 2), too, the stock price has been relatively solid compared to the TOPIX, fluctuating around Y1,000 (Figure C on page 9).

Comparison of Valuation and Results

・The current average valuations of all companies listed on the TSE Prime are as follows: forecasted P/E of 13.54 (based on company plans), P/B of 1.17 (based on actual BPS), and forecasted dividend yield (simple average) of 2.35%. The Company's valuation is about average in terms of the P/E and the actual dividend yield based on ordinary dividend (2.3%).

・Compared to its competitors listed on the TSE Prime Market (HIMACS and Toho System Science; see Figure 11 on page 8), its valuation quite varies regarding the major valuation measures. P/E is about average, while the other valuation measures are somewhat high excluding P/S. In general, though, its stock price does not seem overpriced.

・Its stock price and stock performance presumably reflect the evaluation that the Company has had solid profit growth over the long term, has relatively low volatility in financial performance, and has high liquidity.

Stock Price Outlook

・Is stock price will likely be affected by the situation with orders received in response to the IT investment trends of its end users (companies), its financial performance (especially the final results for this fiscal year and forecasted level of profit for next fiscal year), and whether there will be a share buyback. Over the medium term, the following should also be noted as key factors: numerical goals (sales, profit, and profit margin) of the second medium-term management plan (which will start in FY 2025) as well as its strategies and contents; the amount of contribution by the SI and the Digital Business to the results; and measures for returning profit to shareholders (level of dividend, share buybacks, and stock splits).

・We believe that if the Company continues to show stable, double-digit annual profit growth rate as a domestic-demand-oriented, defensive, small-cap, and stable growth stock, then its stock price may rise over the medium to long term due to the adjustment for the level of P/E and the increase in EPS.

【Figure 11】Comparison of Valuation and Results with Competitors

Item	Company Name	CUBE SYSTEM (CS: consolidated)	HIMACS (HM: consolidated)	Toho System Science (TS: non-consolidated)
Stock Information	Code (P: TSE Prime Market)	2335 P	4299 P	4333 P
	Stock Price (at 11/11 closing)	1,000	1,518	1,013
	Market Cap (million yen)	14,500	18,843	14,046
Valuation	P/E (forecasted price-to-earnings ratio)	13.53	14.53	13.02
	P/B (price-to-book ratio)	1.80	1.79	1.46
	Dividend Yield (%)	5.00	2.77	3.46
	EV/EBITDA	14.94	11.96	6.95
	P/S (price-to-sales ratio)	0.84	1.06	0.94
Liquidity	Daily Average Trading Value (million yen)	29	23	11
This First Half's Results	Sales (million yen)	7,892	8,794	7,527
	Operating Profit (million yen)	598	871	740
	YoY Sales Growth Rate (%)	-2.1	11.3	8.8
	YoY Operating Profit Growth Rate (%)	-19.9	16.2	7.9
	Operating Margin (%)	7.6	9.9	9.8
	This First Half's Progress with Sales Compared to Full-Year Forecast (%)	45.6	49.5	50.2
	Similarly, Progress with Operating Profit (%)	39.1	49.2	54.0
Full-Year Results for This Fiscal Year (company forecast)	Sales (million yen)	17,300	17,750	15,000
	Operating Profit (million yen)	1,530	1,770	1,370
	YoY Sales Growth Rate (%)	7.5	6.4	5.6
	YoY Operating Profit Growth Rate (%)	7.9	3.1	3.2
	Operating Margin (%)	8.8	10.0	9.1

(Note) Prepared by Alpha-Win Research Dept. based on each company's financial results summary
Market cap= (shares outstanding) x (market share price [at 11/11/2022 closing])
The companies' planned EPS values for FY 2023 were used in all P/E calculations. Actual BPS values of the first half of FY 2023 were used in P/B calculations.
EV/EBITDA = (market cap + interest bearing debt - cash & deposits)/(operating profit + depreciation + intangible fixed asset amortization, etc.)
Interest bearing debt and cash & deposits are actual values of the first half of FY 2023.
Operating profit, depreciation, and intagible fixed asset amortization, etc., are each company's full-year forecast for FY 2023.
P/S=market cap / sales [the companies' forecasts for FY 2023]
Daily Average Trading Value: estimated daily average trading value over the past approx. nine months (million yen)

【 2335 CUBE SYSTEM Sector: Information & Communication 】 Figure A

FY		Sales (million yen)	YoY (%)	O.P. (million yen)	YoY (%)	R.P. (million yen)	YoY (%)	N.P. (million yen)	YoY (%)	EPS (Y)	BPS (Y)	Dividend (Y)
2020		14,708	2.7	959	4.1	976	1.7	525	-11.9	38.69	411.96	18.0
2021		14,788	0.5	1,174	22.5	1,295	32.7	844	60.7	62.11	476.52	20.0
2022		16,099	8.9	1,417	20.7	1,432	10.6	944	11.9	69.82	531.14	23.0
2023	Initial Mid-Term Plan CE	17,200	-	1,340	-							
2023	CE	17,300	7.5	1,530	7.9	1,545	7.8	1,000	5.9	73.91	Not disclosed	50.0
2023	Old E	17,200	6.8	1,520	7.3	1,535	7.2	1,000	5.9	73.90	580.79	50.0
2023	New E	17,100	6.2	1,480	4.4	1,495	4.4	970	2.8	71.69	578.57	50.0
2024	Initial Mid-Term Plan CE	18,500	7.6	1,480	10.4							
2024	Revised Mid-Term Plan CE	19,000	9.8	1,710	11.8	(Operating margin of 9.0%; ROE of 13% or more)						
2024	E	18,700	9.4	1,700	14.9	1,715	14.7	1,100	13.4	81.29	612.08	28.0
2025	E	19,600	4.8	1,800	5.9	1,820	6.1	1,180	7.3	87.21	671.29	30.0
2022	Q1	3,987	18.2	378	56.5	390	57.1	262	59.0	19.35	487.51	0.0
2023	Q1	3,892	-2.4	272	-28.1	271	-30.5	173	-34.0	12.84	543.58	0.0
2022	Q2	4,073	9.8	368	18.7	362	2.0	239	1.7	15.95	509.03	8.0
2023	Q2	4,000	-1.8	326	-11.4	323	-10.8	215	-10.0	15.89	556.76	23.0
2022	H1	8,060	13.8	746	35.1	752	24.6	501	25.3	35.30		8.0
2023	H1	7,892	-2.1	598	-19.9	594	-21.0	388	-22.6	28.73		23.0
2022	H2	8,039	4.3	671	7.9	680	-1.7	443	-0.2	34.52		15.0
2023	H2 CE	9,408	17.0	932	38.9	951	39.9	612	38.1	45.18		27.0

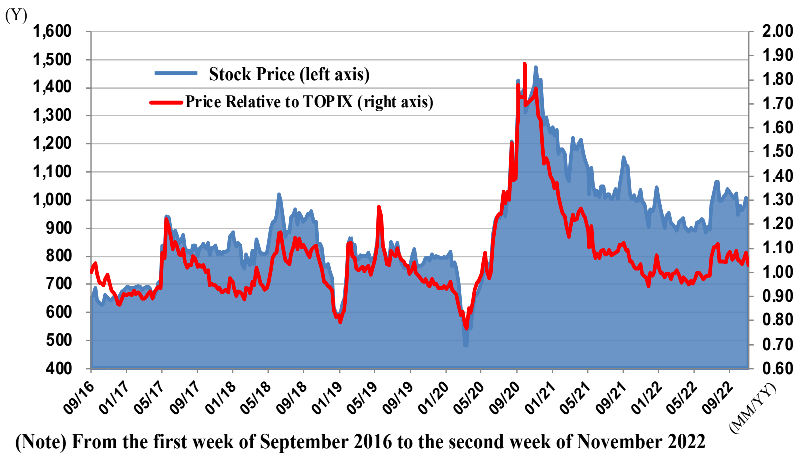
(Note) CE: the Company's forecast/estimate. Old E: Alpha-Win Research Dept.'s previous forecast/estimate. New E: Alpha-Win Research Dept.'s current forecast/estimate. "Initial Mid-Term Plan" is the plan announced on June 11, 2021. "Revised Mid-Term Plan" is the plan announced on May 11, 2022. Q1: Apr-June. Q2: July-Sept. H1 (first half): Apr-Sept. H2 (second half): Oct-Mar.

【 Stock Price and Valuation Indicators: 2335 CUBE SYSTEM 】 Figure B

Item	11/11/2022	Item	P/E	P/B	Dividend Yield	Dividend Payout Ratio
Stock Price (Y)	1,000	Last FY (actual)	14.3	1.9	2.3%	32.2%
Shares Outstanding (thou.)	14,500	This FY (est.)	13.9	1.7	5.0%	69.7%
Market Capitalizatoin (million yen)	14,500	Next FY (est.)	12.3	1.6	2.8%	34.4%
Dilutive Shares (thou.)	0	Equity Ratio at End of This FY's First Half		73.4%	Last FY's ROE	13.8%

(Note) Estimates have been made by Alpha-Win Research Department.

【 Stock Chart (end-of-week prices): 2335 CUBE SYSTEM 】 Figure C



(Note) From the first week of September 2016 to the second week of November 2022

【Performance】

Period	Return	vs. TOPIX
1 month	0.0%	-2.5%
3 months	-4.2%	-5.0%
6 months	6.0%	2.6%
12 months	11.4%	8.8%

(Note)
・Reflects stock and index prices through the closing price on 11/11/2022. "Vs. TOPIX" is the relative value after subtracting the TOPIX's performance from the performance of the Company's stock.
・Performance for the 1-month period is the comparison between the closing price on the last day of October and the closing price on November 11 (the same applies to the other periods).

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