Alpha-Win Company Research Report

PCA CORPORATION
(9629 TSE First Section)

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

● Flash Report on Financial Performance

◆ A major specialized player in enterprise system software; taking a lead in the cloud business as No. 1 in the industry

・PCA CORPORATION (hereinafter referred to as the "Company") sells originally-developed, packaged business software (for accounting, sales management, purchasing and inventory management, payroll, human resources, labor management, etc.) mainly to small- and medium-sized companies as on-premises or via the cloud. It also provides related maintenance services. Its mission is to contribute to society as a "Management Support Company" that supports other companies conduct smooth management and operation. It is taking a lead in the cloud-based business software industry as No. 1 in the industry (PCA Cloud). Going forward, it plans to make a further transition to the subscription business.

・In recent years, thanks to the transition to a subscription-based business model and the event-driven, high market demand, the Company's financial performance has been excellent. Last fiscal year (FY 2020; note that the Company's fiscal year is March-ending, so FY 2020 ended in March 2020), it achieved sales growth and profit growth for the fifth consecutive year as well as record-high profit.

◆ This fiscal year's Q1 results: no surprise – sales and profits seem to have slightly exceeded the Company's plan but had both decreased due to the recoil after the event-driven high demand and the COVID-19 crisis

・In the first quarter of FY 2021 (Apr-June 2020; hereinafter, Q1 = Apr-June), the Company achieved sales of Y2,789 million (-9.2% YoY), operating profit of Y465 million (-20.7% YoY), recurring profit of Y471 million (-21.2% YoY), and net profit of Y272 million (- 25.1% YoY). Faced by a recoil following last fiscal year's great success with the event-driven high demand, sales and profits both decreased (Figure 1).

・However, sales and each of the profits are still high compared to the past Q1 results. Last fiscal year's Q1 results were at a high level due to the high demand caused by the consumption tax revision and the end of support for Windows 7, and this fiscal year's results are being impacted by the COVID-19 crisis. Considering these factors, the rates of decline in sales and profits seem to have been kept low. Due to uncertainties over the impact of COVID-19, many companies listed on the First Section of the TSE have not announced their financial forecasts for the current fiscal year, or have disclosed forecasts upon the announcement of Q1 results that full-year sales and profits will decline significantly, net losses will be posted, and dividend will be reduced or not be paid at all. In contrast, the Company's financial performance seems to be relatively solid.

・The factors behind this Q1's sales decline can be summarized into (1) the recoil from the event-driven high demand and (2) the COVID-19 impact. On the other hand, the cloud business, which the Company has been focusing on, and strategic products such as its subsidiary Xronos's labor management system related to the working style reform have continued to be successful.

[Figure 1] Q1 Results and Full-Year Plan

Q1 Results		Q1 FY 2020	Q1 FY 2021	% Change	Difference	% of Total Sales	FY 2021 Full-Year Company Plan	% Change
Unit: million yen		Apr-June 2019	Apr-June 2020	YoY: %	YoY: million yen	%	Apr 2020 - Mar 2021	YoY: %
Consolidated Sales		3,073	2,789	-9.2	-284	100.0	13,280	-6.9
Sales Category	Products	652	307	-52.9	-345	11.0	2,539	-19.8
	Merchandise	102	77	-24.4	-25	2.8	445	-19.4
	Maintenance Service	865	899	4.0	34	32.2	3,388	-2.4
	Cloud Service	764	957	25.2	193	34.3	4,019	19.1
	Other Operating Revenue	688	546	-20.6	-142	19.6	2,889	-21.9
Gross Profit		1,868	1,756	-6.0	-112	-	8,019	-6.7
	Gross Margin (%)	60.8	63.0		2.2	-	60.4	
SG&A Expenses		1,281	1,290	0.7	9.0	-	5,985	2.9
	SG&A Expenses Ratio (%)	41.7	46.3		4.6	-	45.1	
Operating Profit		587	465	-20.7	-122	-	2,034	-26.9
	Operating Margin (%)	19.1	16.7		-2.4	-	15.5	
Net Profit		364	272	-25.1	-92	-	1358	-25.2
	Net Margin (%)	11.8	9.8		-2.1	-	10.2	

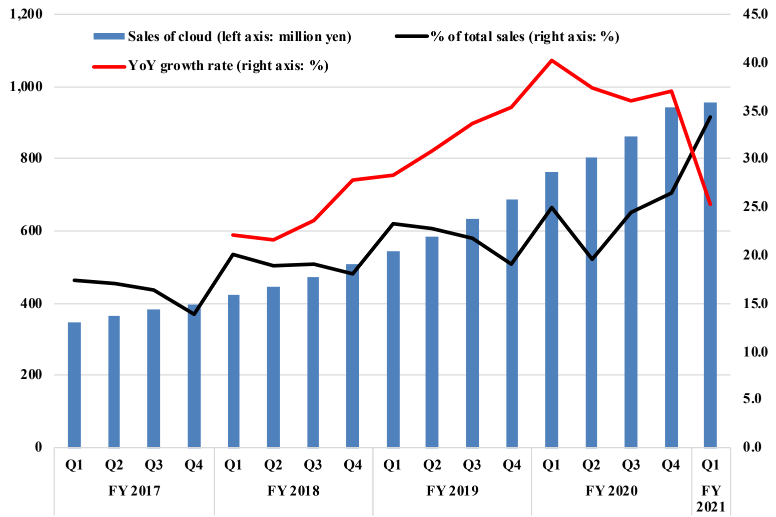
(Ref) Prepared by Alpha-Win Research Dept. based on the financial results summary

・Of the total decrease in sales of Y284 million, decline in sales of products accounted for Y345 million and other operating revenue accounted for Y142 million. On the other hand, sales of maintenance increased slightly by Y34 million, while the sales of cloud service increased by Y193 million.

・Sales by category (sales categories defined by the Company) were as follows:

1. Sales of the products (conventional packaged software: on-premises) were largely impacted by the recoil from the high demand for replacement by users of stand-alone software. Consequently, from last Q1 ⇒ this Q1 (the same order applies below), sales decreased by half from Y625 million ⇒ Y307 million (-52.9% YoY; percent of total sales changed from 21.2% ⇒ 11.0%). Of all the categories, this category experienced the largest rate of drop in sales and was the most responsible factor for the overall sales decline. It was most likely the most responsible factor for the profit decline as well.
2. With the continued trend of going paperless through digitalization, sales of merchandise (ledger sheets, etc.) decreased from Y102 million ⇒ Y77 million (-24.4% YoY; 3.4% ⇒ 2.8% of total sales).
3. Maintenance service, which accounted for 32.2% of total sales this Q1 (last Q1: 28.1%), has always been a stable source of revenue. Thanks to contracts remaining from the previous fiscal year and the acquisition of new maintenance contracts, sales were solid and increased by 4.0% YoY, from Y865 million ⇒ Y899 million.
4. By category, sales of the maintenance service had been the largest, but this Q1, sales of the cloud service beat this and became the largest for the first time (24.9% ⇒ 34.3% of total sales). In the order of Q1 of the year before the previous ⇒ last Q1 ⇒ this Q1, the cloud service's sales increased from Y544 million ⇒ Y764 million ⇒ Y957 million. Its growth has somewhat slowed down compared to the past (growth rate: 28.3% ⇒ 40.3% ⇒ 25.2%), but this category is still continuing to show a high growth. As a result, the percent of sales of the subscription-based business (the cloud and maintenance services) over the total increased significantly from last Q1's 53% to 66.5%. Also, as shown in Figure 2, quarterly sales have been continuously increasing YoY and QoQ regardless of seasonal variations. The number of users of the cloud service (all current users) has been steadily increasing, reaching 12,313 companies in March 2019 and 14,388 companies in March 2020 (the number of users as of the end of June 2020 has not been disclosed). The Company seems to be gaining new users at a net rate of 130-140 companies per month, which is a somewhat slower pace compared to the past when the Company was gaining 150-170 companies per month. However, despite concerns about the impact of COVID-19, the Company has been steadily increasing the number of users, which has helped support its overall sales. Since this business is highly sustainable and has a high marginal profit ratio, it has mostly likely been contributing significantly to the profits as well.
5. Sales of other operating revenue decreased largely from Y688 million ⇒ Y546 million (-20.6% YoY). Sales decreased because of difficulties in providing on-site implementation support service for various systems (through the consolidated subsidiary KEC) due to COVID-19. Another reason is that since the other companies' products are mostly sold in combination with the Company's products, their sales are highly linked to the Company's products.

[Figure 2] Quarterly Change in Sales of the Cloud Business



(Ref) Prepared by Alpha-Win Research Dept. based on the financial results summary

・Regarding profit, since the Company's business model has a high marginal profit ratio, fluctuations in sales greatly affect the profit margins and the amount of change in profit. In addition, due to the sales growth of the highly profitable cloud business and the consequent rise in its percent over the total sales, the product mix was improved and the cost of sales was reduced. As a result, the gross margin improved from 54.9% in the Q1 of the year before the previous to 60.8% last Q1 and then to 63.0% (+2.2% YoY) this Q1. Since sales declined while the SG&A expenses stayed about the same, having increased only by Y9 million or 0.7% YoY, the SG&A expenses ratio worsened by 4.6% from 41.7% ⇒ 46.3%. The Company has been continuing to cut down its general expenses, but expenses related to COVID-19 countermeasures, the rise in personnel expenses, and upfront investment costs seem to have caused this change. Consequently, the operating margin fell by 2.4% from 19.1% to 16.7%. Q1's operating margin, though, was greater than the Company's full-year forecast of 15.3%. With no significant non-operating profit/loss or extraordinary profit/loss posted, the decline in operating profit caused net profit to decrease.

・There were no significant changes in the balance sheet as of the end of this Q1 compared to the same period of the previous fiscal year. The profit growth helped increase the cash and deposits (from last Q1 ⇒ this Q1: Y8,134 million ⇒ Y10,176 million) and the net assets (Y12,375 million ⇒ Y13,824 million in the same order). The ratio of cash and deposits over this fiscal year's forecasted sales or the total assets was 76.6% (equivalent to 9.2 months of average monthly sales) or 46.6%, respectively. Clearly, the Company has ample liquidity on hand. Its financial standing is also firm, with an equity ratio of 62.7% and current ratio of 269.9%.

◆ Progress Against Financial Forecast and Forecast for This Fiscal Year and Onward

・The Company has announced its full-year financial forecast for this fiscal year. It is expecting sales of 13,280 (+6.9% YoY), an operating profit of 2,034 (-26.9% YoY), a net profit of 1,358 (-25.2%), and ordinary dividend to be kept at 34 yen. Forecast for H1 has not been disclosed. Q1's progress rate against the Company's full-year forecast was 21.0% for sales (as reference, last Q1 was 21.5%, the Q1 of the year before the previous was 20.5%, and the simple average of the past 15 years' Q1 is 21.6%) and 22.9% for operating profit (in the same order, 21.1%, 4.6%, and not available since there were a few fiscal years with a net loss), which are about the same as last fiscal year.

・The Q1 results seem to have somewhat exceeded the Company's rather conservative forecast (not disclosed; it has always tended to be conservative), but since the contribution of Q1 to the full-year results has always been small and the H2 situation still needs to be carefully evaluated, the full-year forecast has not been changed.

・Although the products and other operating revenue will most likely be especially hit by the recoil from the event-driven high demand, we believe that the subscription-based business (cloud + maintenance) with high profitability and sustainability will continue to grow so that financial performance in Q2 (June-Aug 2020) will again mostly be as expected. However, the second wave of the COVID-19 outbreak has been graver than expected in Japan and has become the largest risk factor to the Company's financial performance in Q3 (Sept-Dec 2020) and onward. If the situation becomes prolonged, although with some time lag, the Company will most likely be affected in terms of new negotiations, sales expansion of new products, and operation efficiency.

・Even if sales end up being somewhat short of the plan, we believe that the possibility of a large, downward revision in full-year profit should be small since the subscription-based business will most likely continue to support the overall financial performance and there seems to be potential for further cost control. Therefore, we have predicted that the profits will be about the same as the Company's forecast.

・This fiscal year, due to the recoil from the event-driven high demand and the COVID-19 impact, a temporary profit decline is inevitable. However, since the subscription-based business will likely continue to be a stable driver of high growth, especially with the cloud service, we believe that the annual EPS growth rate will be 8-10% over the medium term based on normalized figures after the event-driven high demand. Also, medium- to long-term positive financial performance may lead to the enhancement of shareholder return such as dividend hikes, flexible buybacks of shares, and stock splits.

◆ Recent Topics

・As measures against COVID-19, the Company has been improving its employees' work-from-home environment (about 70% of the entire company and nearly 100% of the system development and verification divisions work from home), postponing negotiations/seminars/events, shifting them online or to web seminars, and improving the call center and support system (planning to make remote work possible by this year's fall).

・The software subscription service (PCA Subscription: service where the Company's software can be used for a fixed price per period) has become available starting in May 11 and two options for PCA Accounting Hyper targeting mid-tier companies (Receivables Management Option and Debt Management Option) has been released on July 22. Both are new businesses and products, and they seem to be facing a slow start due to COVID-19.

・Since this fiscal year is the Company's 40th anniversary, in celebration, it plans to grant shares to all employees from a part of its treasury shares through the Employee Stock Ownership Plan (40 shares per person; a total of approx. 17,000 shares or Y67 million; equivalent to 0.22% or 1.63% of all outstanding or treasury shares, respectively). The aim is to raise its employees' awareness of being involved in company management through the possession of the Company's shares as well as sharing the rise in shareholder value over the medium to long term with its shareholders.

◆ Stock Price

・The Company's stock is seen as a defensive, domestic-demand-related, and small-cap growth stock with a subscription-based business. In recent years, it has been significantly outperforming the TOPIX. Although there was seemingly no surprise with the Q1 results, the Company's stock price had continued to rise since around the announcement of the Q1 results even as the market continued to face a downturn and has been outperforming the market in the most recent period as well.

・Due to the difficulty in comparing valuation with the average of the First Section of the TSE (since many companies still have not disclosed their financial forecast), we compared the Company with its competitors Obic Business Consultants and Miroku Jyoho Service. Excluding dividend yield and P/S, the major indicators – this fiscal year's forecasts for P/E, P/B, and EV/EBITDA – show that the Company's valuation is low compared to the two competitors. Since the rate of decline (YoY) in operating in profit in Q1 was also the smallest, the Company's valuation seems to still be relatively cheap (Figure 3). We should continue to take note of the Company's progress as a stable, medium- to long-term growth stock.

[Figure 3] Comparison of Valuation with Competitors

Company Name	PCA (consolidated)	Obic Business Consultants (OBC: non-consolidated)	Miroku Jyoho Service (MJS: consolidated)
Code	9629	4733	9928
Stock Price (at 7/31 closing)	4,570	6,190	2,122
Market Cap (million yen)	35,189	499,558	73,859
P/E (price-to-earnings ratio)	22.4	50.8	28.1
P/B (price-to-book ratio)	2.2	3.9	3.5
Dividend Yield (%)	0.7	0.8	1.8
EV/EBITDA	8.1	29.5	9.7
P/S (price-to-sales ratio)	2.6	16.4	2.1
This FY's Q1: YoY Sales Growth Rate (%)	-9.2	-12.8	-7.6
This FY's Q1: Operating Profit Growth Rate (%)	-20.7	-24.1	-32.6

Market cap = shares outstanding x market stock price [at 7/31 closing]
The companies' estimated EPS values for FY 2021 were used in all P/E calculations. BPS values used in P/B calculations reflect this FY's Q1 results.
EV/EBITDA = (market cap + interest-bearing debt - cash & deposits) / (O.P. + depreciation + intangible fixed assets)
Note: Interest-bearing debt and cash & deposits reflect Q1 FY 2021 results
P/S = market cap / sales [the companies' estimate for FY 2021]

(Ref) Prepared by Alpha-Win Research Dept. based on each company's securities report and stock data

【 9629 PCA 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)
2018		9,785	4.5	807	86.8	834	79.9	441	174.1	64.37	1,644.39	31.00
2019		11,439	16.9	1,248	54.7	1,277	53.0	906	105.5	133.25	1,789.76	31.00
2020		14,266	24.7	2,781	122.8	2,808	119.9	1,816	100.4	272.92	2,027.42	54.00
2021	CE	13,280	-6.9	2,034	-26.9	2,055	-26.8	1,358	-25.2	204.70	-	34.00
2021	E	12,840	-10.0	2,050	-26.3	2,060	-26.6	1,360	-25.1	204.36	2,177.77	34.00
2022	E	13,500	5.1	2,215	8.0	2,230	8.3	1,470	8.1	220.89	2,364.67	34.00
2023	E	14,300	5.9	2,460	11.1	2,470	10.8	1,630	10.9	244.94	2,575.60	36.00
2018	Q1	2,108	5.6	175	626.2	185	435.0	98	—	14.37	1,579.92	—
2019	Q1	2,346	11.3	57	-67.1	69	-62.3	34	-64.6	5.09	1,624.69	—
2020	Q1	3,073	31.0	587	917.5	598	754.6	364	945.3	54.76	1,848.46	—
2021	Q1	2,789	-9.2	465	-20.7	471	-21.2	272	-25.1	40.99	2,029.56	—

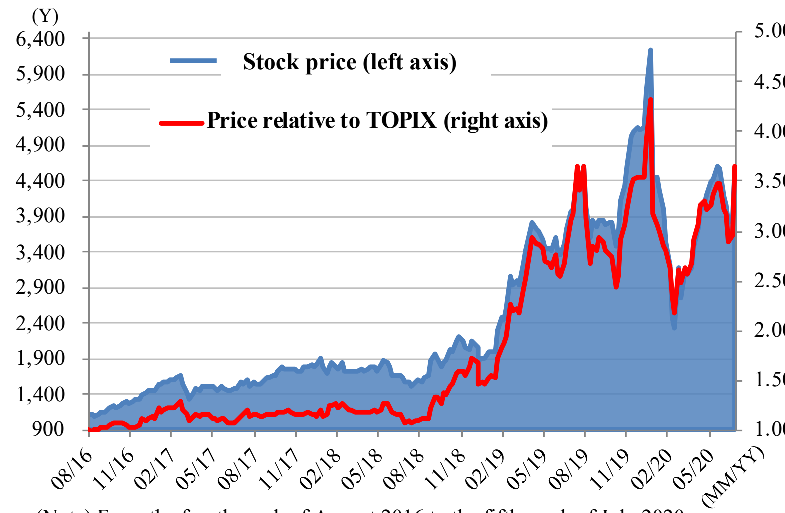
(Note) CE: the Company's forecast/estimate. E: Alpha-Win Research Dept.'s forecast/estimate. Q1: Apr-June.

【Stock Price and Valuation Indicators: 9629 PCA】 Figure B

Item	7/31/2020	Item	P/E	P/B	Dividend Yield	Dividend Payout Ratio
Stock Price (Y)	4,570	Last FY (actual)	16.7	2.3	1.2%	19.8%
Shares Outstanding (thou.)	7,700	This FY (est.)	22.4	2.1	0.7%	16.6%
Market Capitalization (million yen)	35,189	Next FY (est.)	20.7	1.9	0.7%	15.4%
Dilutive Shares (thou.)	0	Equity Ratio at Last FY-End	58.7%	Last FY's ROE		14.3%

(Note) Estimates were made by Alpha-Win Research Dept.

【Stock Chart (end-of-week prices) : 9629 PCA】 Figure C



(Note) From the fourth week of August 2016 to the fifth week of July 2020

【Performance】

Period	Return	vs. TOPIX
1 month	2.2%	6.5%
3 months	24.5%	21.9%
6 months	2.2%	15.1%
12 months	12.4%	17.6%

(Note) Reflects stock price and index values through the closing price on 7/31/2020.

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