Trias Company Memo 2009-09-15

(Securities Code: 2427 / JASDAQ) OUTSOURCING Inc.
Summary of Business Results Meeting for the 2nd Quarter of the Fiscal Year ending December 31, 2009

On August 27, OUTSOURCING Inc. (hereinafter OUTSOURCING or the Company) held a Business Results Meeting for the 2nd quarter of the fiscal year ending December 31, 2009. Attending the meeting were OUTSOURCING Inc. Chairman Haruhiko Doi and Managing Director Kazuhiko Suzuki.

The following is a summary of the presentation made by Chairman Doi.

[Business Results Summary for FY12/09 2Q]

Hit by the recession and ensuing cutbacks in production, 2Q net sales fell by 37% year-on-year, while gross profit declined 47% y-o-y. While the number of onsite workers fell to the lowest level in April and net sales for May also hit bottom, there were indications that the bottom for the automotive and semiconductor industries, which had been the hardest hit, had been reached. As net sales fell, the Company reduced its SG&A expenses by 155 million yen y-o-y. As recommended by our corporate auditor, the Company posted its employment adjustment expenses as a cost of sales, while many of our competitors wrote it off as an extraordinary loss.

As for OUTSOURCING's balance sheets, noncurrent assets increased by 1,508 million year-on-year from the construction of the No. 2 engine test facility, as well as from our post-merger acquisition of property, plant and equipment. Noncurrent liabilities also increased by 1,312 million yen y-o-y due to negative goodwill resulting from mergers and acquisition of subsidiaries.

[Group Operating Environment]

As for Japanese manufacturers in general, the Company sees their inventory adjustment cycle as being completed and moves to reduce workforce as having bottomed out in April. Given the government's economic stimulus packages, the recovery in production levels has exceeded projections. The following industries are recovery-bound:

- Transportation equipment: "Eco-tax" incentive helps buoy industry as the recession bottoms out
- Electronic components: Demand from the transportation equipment industry fuels production upswing
- Consumer electronics: Consumer demand is growing, spurred by the "eco-point" benefit system and shift to digital TV broadcasting

- Semiconductors: Recovery driven by transportation equipment industry production upswing and inventory adjustment turnaround

As production ramps up, an estimated 100,000 new workers will be needed to meet the upswing. Roughly half of all manufacturers will likely opt to hire workers directly, while 30% will choose outsourced contracting; the remaining 20% will come from manufacturing temporary placement. To meet the direct employment needs of that largest group, the OUTSOURCING Group offers outsourced administrative contract services through its subsidiary, ORJ INC. (hereinafter ORJ). The Company can also develop outsourced production contracting proposals to improve the onsite productivity of a client-manufacturer that is being serviced by ORJ. As for makers in need of outsourced contracting, the Company's service proposals and operations are fully cleared by regulators. It also has ORJ, which offers channels to a client base that other competing providers lack. Another major edge is the fact that the Company has a company with production engineering expertise as a member of its Group, serving to further differentiate itself from competitors. Meanwhile, manufacturing temporary placement will continue generating public criticism, but the Company believes it provides a socially meaningful service in which risks over length of employment uncertainty are offset by better wages; it also possesses the expertise to convert production sites using manufacturing temporary placement services to sites that operate on outsourced production contracting.

On August 14, OUTSOURCING acquired the engineering temporary placement division—RPM Co., Ltd.—and pharmaceutical industry service division—Try Angle Co., Ltd.—from AIXEX alpha Co., Ltd., which is filing for bankruptcy protection. Outsourcing providers that lack the business resources to provide both outsourced production contracting services and services meeting makers' needs for direct employment will not be able to survive an industry shakeout. The Company also sees competitors in the realm of engineering outsourcing either losing business or shaken out at a time when clients are cutting back R&D budgets. They are at risk because, having failed to fully utilize their contracted engineers, such providers will experience growing turnover in capable engineers who refuse to remain on standby status for prolonged periods. In addition, the Company will continue to merge with or acquire providers with attractive business resources, including those with blue-chip client accounts and advanced or specialized expertise, with the post-acquisition synergy enabling it to recover earnings quickly.

[Earnings Outlook for FY12/09 2H]

As for the Outsourced Production Contracting Business, orders are firm until October but things are a little less certain in November. As a result, the Company expects net sales of 14.1 billion yen and an operating income of 898 million yen in the 2H. The 3Q will see zero operating income due to a one-time M&A expense being incurred, but order inflows, spurred by the automotive industry's recovery, will rise and, as a result, earnings will turn positive in September and projected to jump from

October onwards.

Meanwhile, ORJ is expected to post a major gain in net sales in the 4Q as the peak for temp contract expirations take place in October. With the economy recovering, demand for its worker recruitment related administrative services is expected to soar as client-manufacturers, especially those in the transportation equipment industry, scramble to meet their production ramp-up needs. That will lead to a per capital administration service fee of 50,000 yen/month, which is far higher than originally projected. As a result, the Company expects ORJ's net sales to reach 2,168 million yen and 611 million yen in operating income.

The OUTSOURCING Group as a whole expects net sales of 16,573 million yen and 1,527 million yen in operating income for the 2H.

[Q&A Session]

Q1: What specifically is happening in the Outsourced Production Contracting Business?

A1: We have firm orders until October. The automotive industry has generated the most orders in October, with seven manufacturers looking to add some 650 workers. In addition, FULLCAST CENTRAL CO., LTD.—in which the Toyota Group was an investor and was renamed OUTSOURCING CENTRAL CO., LTD. from July 1, 2009—had orders from the automaker's group frozen after the previous parent company, Fullcast Co., Ltd., was involved in a scandal. But with its acquisition by OUTSOURCING, Toyota orders have since been resumed as it prepares to ramp up production from fall.

Q2: Is there any client who wants to start ramping up production with the Company's outsourced contracting service?

A2: Only 30% of manufacturers looking to ramp up production will opt for outsourced production contracting, a figure far below our expectations. As a result of the public backlash over makers firing temporary workers en masse, half the companies are opting to hire workers directly. But because a maker seeking to change back to hiring temps after direct employment will face considerable difficulty, they really have no choice but to convert to outsourced production contracting in the end.

Q3: Any example of OUTSOURCING winning a contract at the expense of a struggling competitor?

A3: ORJ provides outsourced administrative services for a manufacturer converting from temporary placement to direct employment. While the larger providers such as NIKKEN SOGYO CO., LTD. and NISSO CORPORATION have provided manufacturing temporary placement services, ORJ is now replacing them through its outsourced service contracts. ORJ's 2H earnings outlook in operating income is 611 million yen—that is the equivalent of some 20 billion yen in temporary placement contract sales.

Q4: Any plans to offer your services overseas?

A4: We see Japan's outsourced production contracting market stagnating over the mid- to long-term as the nation's population continues to contract. At the same, the market is expected to grow overseas, especially in developing countries with expanding populations. We are now working with our affiliate, TECHNOSMILE, INC., to move into those countries, with the goal of providing the services of some 3,000 engineers per year by fiscal 2011.

Q5: What is the ratio for conversion to outsourced production contracting at present?

A5: The ratio stands at over 90%, excluding cases in which manufacturers have been hit with product recalls and must therefore rely on temporary workers to meet the contingency.

Q6: Is it possible for ORJ's profit to exceed that posted by the Company's outsourced production contract business?

A6: It is possible, but only temporarily. Given that direct employment sites will eventually be converted to outsourced production contracts, we do not see ORJ's profits exceeding the Company's over the long term.

Q7: When did ORJ and OUTSOURCING CENTRAL become consolidated subsidiaries?

A7: ORJ was launched in October 2008, while OUTSOURCING CENTRAL became a consolidated subsidiary in June 2009.

Q8: What is the net sales forecast for OUTSOURCING CENTRAL?

A8: We expect net sales of 1.5 billion yen and profitability by 4Q. Having adjusted its inventory and spurred by the government's economic stimulus packages, the Toyota Group's factories are ramping up production and orders have begun placed with OUTSOURCING CENTRAL.

Q9: What is the earnings outlook beyond fiscal 2010—will it simply follow the sales trend from the 2nd half of this term?

A9: Our goal is to double profit in the mid-term and target 20% growth per year after that. However, ORJ's profit trend will not continue because its 4Q profit was inordinately high as it coincided with the cooling-off period for makers committed to manufacturing temporary placement contracts.

Q10: What trends are developing in your pool of worksite employees?

A10: We expect the number will exceed 10,000 by the end of December. To achieve this, we need to recruit more than 2,000 workers/month and we have already laid out the framework to do so.

Q11: Are your competitors also expected to recover as the outsourcing industry itself recovers?

A11: We have ORJ, with its outsourced administrative service business, and our own ability to convert worksites manned by temporary workers into outsourced production contract operations. Competitors lacking in such business resources are not likely to prosper.

Q12: You estimate that some 100,000 new workers are needed to ramp up production. To what level did the manufacturing workforce decline to before it rebounded, and can this rebound trend be sustained?

A12: At one point, it fell to 400,000 workers. Today, we are getting inquiries from the automotive industry, which is experiencing boom sales in hybrid cars, and consumer electronics makers, which is being buoyed by the "eco-point" benefit system. While automakers are ramping up production to introduce new car models next year, there are concerns that the replacement demand is only being brought forward and cannot be sustained. Thus, the outlook for a genuine economic recovery remains somewhat uncertain.

Q13: How large of a profit increase do you expect, including that generated from the companies the OUTSOURCING Group as acquired?

A13: Under the traditional recovery model, orders recovered as manufacturers opted for temporary workers rather than hiring workers directly. But we believe that model is not applicable this time because of the mass firing of temp workers mentioned earlier. Instead, we see ORJ and its outsourced administrative services as being the primary beneficiaries of the current recovery phase. In addition, we intend to convert orders for ORJ services into outsourced production contracts over time. Our goal is to double our group profits.

Q14: What is the difference in compensation between temporary hires and that offered to workers hired to perform outsourced production contracting services?

A14: Because temp hires fall under the supervision of the client-manufacturer, OUTSOURCING can neither evaluate their performance nor provide them with training. Thus, temps are generally locked in their initial compensation package. Under outsourced production contracting, however, workers can improve their skills and contribute to onsite productivity improvements, enhancing both their careers and compensation.

【Reference】

OUTSOURCING Inc. (2427)

Key Financial Data and Business Results (Consolidated)

Consolidated (¥million)	Net Sales	Operating Income	Ordinary Income	Net Income	EPS (¥)	Dividend per Share (¥)
FY12/05	17,881	95	103	34	273.5	300.00
FY12/06	21,197	119	118	97	783.3	300.00
FY12/07	24,321	1,013	1,004	583	4,917.3	492.00
FY12/08	24,148	1,113	1,134	641	5,412.3	644.00
FY12/09 1HF	7,733	△ 374	△ 306	△ 401	△ 2,940.5	−
FY12/09 est.	24,300	1,150	1,200	670	4,326.2	644.00

Note: FY12/09 est. is the Company's forecast announced on Augut 13 2009.

Key Stock Indicators (Consolidated)		
No. of Shares Issued	Dec. 08	128,220
No. of Treasury Stock	Dec. 08	15,740
Market Value (¥million)	Sep.11 2009	9,232
BPS (¥)	Dec. 08	22,524.6
ROE (%) ※1	Dec. 08	27.6
ROA (%) ※2	Dec. 08	11.0%
PER (times)	FY12/09 est.	16.6
PCFR(times) ※3	Dec. 08	11.5
PBR (times)	Dec. 08	3.2
Share Price (¥)	Sep.11 2009	72,000

Key Financial Data (Consolidated)		
Total Assets (¥million)	Dec. 08	6,051
Shareholders' Equity (¥million)	Dec. 08	2,533
Interest-Bearing Debt (¥million)	Dec. 08	1,141
Equity Ratio (%)	Dec. 08	41.9
Ratio of Interest-Bearing Debt (%) ※4	Dec. 08	45.1%
Free Cash Flows (¥million) ※5	Dec. 08	△ 380

※1 ROE=Current Net Income÷Averaged Shareholders' Equity of beginning of term and term end

※2 ROA=Cureent Net Income÷Averaged Total Assets of beginning of term and term end

※3 PCFR=Maket Value÷(Current Net Income+Depreciation)

※4 Ratio=Interest-Bearing Debts÷Shareholders' Equity

※5 Free Cash Flows=Operating CF+Investment CF