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TSE 1st

OUTSOURCING Inc.

1H FY12/15 Financial Results and Follow-up Interview

OUTSOURCING Inc., hereafter the "Company" or "the OS Group", announced its 1H FY12/15 (Jan-Jun) financial results on July 30, and Trias Corporation conducted an interview with Chairman and CEO Haruhiko Doi. The following is a summary of the interview.

Summary of 1H FY12/15 Consolidated Financial Results

Consolidated financial results for 1H topped the Company's initial forecasts, with both net sales and incomes up sharply from 1H FY12/14. Domestic dispatching business of engineers was stronger than the Company's expectations. As is shown in Table 1, consolidated net sales were ¥36,022 million (+28.3% YoY), gross profit ¥7,074 million (+28.1% YoY), operating income ¥937 million (+31.5% YoY), ordinary income ¥1,003 million (+32.0% YoY) and net income ¥488 million (+30.3% YoY). Operating income in Q2 was strong enough to cover the restrained increase of 1.8% YoY in Q1 when one-time expenses were booked.

【Table 1】Summary of 1H FY12/15 Consolidated Financial Results

(¥ million)	1H FY12/14		1H FY12/15			YoY Changes	
	Actual	Ratio to Net Sales	Initial Forecasts	Actual	Ratio to Net Sales	Amount	Ratio
Net sales	28,070	100.0%	35,700	36,022	100.0%	7,952	28.3%
Cost of sales	22,549	80.3%	-	28,947	80.4%	6,398	28.4%
Gross profit	5,521	19.7%	-	7,074	19.6%	1,553	28.1%
SG&A expeneses	4,807	17.1%	-	6,136	17.0%	1,329	27.6%
Operating income	713	2.5%	830	937	2.6%	224	31.5%
Ordinary income	759	2.7%	800	1,003	2.8%	243	32.0%
Net income	375	1.3%	430	488	1.4%	113	30.3%

Source: Compiled by Trias Corporation from the Company IR materials

Gross profit margin decreased slightly to 19.6% from 19.7% in 1H FY12/14. While the tight domestic labor market led to much larger recruiting expenses and weighed on profitability, this was mostly offset by staff increases in the Engineering Outsourcing Business which has a high unit contract price, as well as by the Company's measures to enhance added value through training/educating its dispatched personnel.

SG&A expenses rose by ¥1,329 million, or up 27.6% YoY, partially consisting of a ¥500 million increase in personnel expenses including annual salary hikes, a nearly ¥200 million increase in new staff recruiting expenses, and a ¥120 million increase in goodwill amortization. One-time expenses totaling ¥260 million also weighed on. This includes preparatory outlay for the transition to IFRS (the International Financial Reporting Standards) accounting, start-up expenses for a special subsidiary company for employing disabled persons, and M&A fees charged for unrealized deals, none of which was posted in 1H FY12/14.

Operating income jumped 31.5% YoY, leading operating income margin to rise to 2.6% from 2.5% in 1H FY12/14. Excluding the abovementioned one-time expenses, adjusted operating income actually increased by 68% YoY, and operating income margin improved by 0.8pp to 3.3%. Ordinary income resulted in a similar growth to operating income after flattish non-operating balance.

Table 2 shows operating segment results compared with initial forecasts, and indicates net sales were stronger by ¥322 million and operating income by ¥107 million. Most significant was the Engineering Outsourcing Business, with net sales exceeding its initial forecast by ¥774 million. In addition to strong demand, the number of newly recruited staff was more than anticipated owing to the Company's new schemes. Meanwhile, Overseas Business net sales fell short by ¥325 million, dragged by slower economies in Asian nations. As for incomes, stronger incomes in the high-margin Engineering Outsourcing Business offset shortfalls in the Overseas Business.

● 【Table 2】1H FY12/15 Actual vs. 1H FY12/15 Initial Forecasts

(¥ million)	1H FY12/14		1H FY12/15			YoY Changes	
	Actual	Composition Ratio/ Income Margin	Initial Forecasts	Actual	Composition Ratio/ Income Margin	Amount	Ratio
Net sales	**28,070**	100.0%	**35,700**	**36,022**	100.0%	7,952	28.3%
Engineering Outsourcing Business	10,381	37.0%	13,991	14,765	41.0%	4,384	42.2%
Manufacturing Outsourcing Business	12,049	42.9%	14,049	14,031	39.0%	1,981	16.4%
Administrative Outsourcing Business	289	1.0%	282	270	0.8%	(19)	-6.6%
Recruiting and Placing Business	370	1.3%	375	341	0.9%	(28)	-7.7%
Overseas Business	4,879	17.4%	6,860	6,535	18.1%	1,655	33.9%
Other Business	99	0.4%	143	78	0.2%	(21)	-21.8%
Operating income	**713**	2.5%	**830**	**937**	2.6%	224	+0.1pp
Engineering Outsourcing Business	494	4.8%	678	949	6.4%	455	+1.7pp
Manufacturing Outsourcing Business	195	1.6%	107	189	1.3%	(6)	-0.3pp
Administrative Outsourcing Business	41	14.4%	18	30	11.5%	(10)	-3.0pp
Recruiting and Placing Business	167	45.3%	115	142	41.6%	(25)	-3.7pp
Overseas Business	34	0.7%	95	(19)	-0.3%	(54)	-1.0pp
Other Business	4	4.8%	8	7	9.8%	2	+5.0pp
Adjustment	(225)	-	(191)	(362)	-	(136)	-

Note: From Q2 FY12/15, the Company has modified the English term of the operating segment formerly titled "Recruitment and Placement Business" to "Recruiting and Placing Business". The contents and Japanese title of the operating segment remain the same.
Source: Compiled by Trias Corporation from the Company IR materials

Total assets at the end of 1H FY12/15 stood at ¥27.4 billion, up ¥3.2 billion from the end of FY12/14 as shown in Table 3. For assets, notes and accounts receivable - trade increased by ¥1.2 billion owing to business expansion, and intangible assets by ¥700 million partially due to increased goodwill associated with acquisition of subsidiaries' shares. For liabilities and net assets, short-term and long-term loans payable decreased a total of ¥1.7 billion as the Company paid back its loans on the back of financing through a third-party allotment of subscription rights to shares.

●【Table 3】1H-End FY12/15 Consolidated Balance Sheet Summary

(¥ million)	FY12/14-End		1H-End FY12/15		YoY Changes	
	Actual	Composition Ratio	Actual	Composition Ratio	Amount	Major Factors
Current assets	**17,065**	**70.7%**	**19,565**	**71.4%**	**2,500**	
Cash and deposits	6,671	27.6%	7,411	27.0%	739	
Notes and accounts receivable - trade	8,257	34.2%	9,544	34.8%	1,286	Acquisitions of subsidiaries' share and business expansion
Non-current assets	**7,067**	**29.3%**	**7,852**	**28.6%**	**785**	
Goodwill	1,791	7.4%	2,592	9.5%	800	Acquisitions of subsidiaries' share
Total assets	**24,132**	**100.0%**	**27,418**	**100.0%**	**3,285**	
Current liabilities	**12,967**	**53.7%**	**11,755**	**42.9%**	**(1,211)**	
Short-term loans payable (incl. current portion of long-term loans payable)	4,666	19.3%	2,316	8.4%	(2,349)	Repayment from fund-raising associated with the exercise of subscription rights to shares
Accounts payable - other	3,800	15.7%	5,380	19.6%	1,580	Acquisitions of subsidiaries' share and business expansion
Non-current liabilities	**3,596**	**14.9%**	**4,168**	**15.2%**	**571**	
Long-term loans payable	1,763	7.3%	2,347	8.6%	584	
Shareholders' equity	6,219	25.8%	10,244	37.4%	4,024	Increased from the exercise of subscription rights to shares
Total net assets	**7,569**	**31.4%**	**11,495**	**41.9%**	**3,925**	
Total liabilities and net assets	**24,132**	**100.0%**	**27,418**	**100.0%**	**3,285**	

Source: Compiled by Trias Corporation from the Company IR materials

FY12/15 Consolidated Financial Forecasts

While Q1 and Q2 results exceeded initial forecasts, the Company left FY12/15 full-year forecasts unchanged. Domestic businesses should continue to fare well as in the previous term as demand has been buoyant particularly for Engineering Outsourcing Business, and staff recruiting has been in line with plans. Potential downside risks of Overseas Business falling short should be absorbed by stronger domestic operations to result in an upswing in overall consolidated performance.

Full-year forecasts, as shown in Table 4, look for net sales at ¥74 billion (+24.5% YoY), operating income ¥3.1 billion (+54.2% YoY), ordinary income ¥3.0 billion (+36.5% YoY) and net income ¥1.62 billion (+23.1% YoY). Operating income margin is to rise markedly to 4.2% from 3.4% in FY12/14.

【Table 4】1H FY12/15 Financial Results and FY12/15 Financial Forecasts

(¥ million)	FY12/14		FY12/15		Full-Year YoY	
	1H Actual	Full-Year Actual	1H Actual	Full-Year Initial Forecasts	Amout	Ratio
Net sales	28,070	59,421	36,022	74,000	14,578	24.5%
Cost of sales	22,549	47,457	28,947	-	-	-
Gross profit	5,521	11,963	7,074	-	-	-
Gross profit margin	*19.7%*	*20.1%*	*19.6%*	-	-	-
SG&A expenses	4,807	9,953	6,136	-	-	-
SG&A expenses ratio	*17.1%*	*16.8%*	*17.0%*	-	-	-
Operating income	713	2,010	937	3,100	1,089	54.2%
Operating income margin	*2.5%*	*3.4%*	*2.6%*	*4.2%*	-	*+0.8pp*
Ordinary income	759	2,197	1,003	3,000	802	36.5%
Ordinary income margin	*2.7%*	*3.7%*	*2.8%*	*4.1%*	-	*+0.4pp*
Net income	375	1,316	488	1,620	303	23.1%
Net income margin	*1.3%*	*2.2%*	*1.4%*	*2.2%*	-	*-0.0pp*

Source: Compiled by Trias Corporation from the Company IR materials

By operating segment, Manufacturing Outsourcing Business should maintain double-digit growth, while Engineering Outsourcing and Overseas Business are expected to accelerate net sales growths. Consolidated operating income margin is to rise 0.8pp YoY to 4.2%. All the three main operating segments expect operating income margin to rise, with that of Overseas Business in particular jumping to 3.3% from 0.8% in FY12/14 to top that of Manufacturing Outsourcing Business. Although results fell slightly short of forecasts in 1H, net sales and incomes in overseas operations are expected to recover significantly in 2H as negative impacts from last year's coups and civil demonstrations fade out and local operations are sufficiently set up in each area.

The operating income margin in the Company's mainstay Engineering Outsourcing Business is to rise 0.4pp YoY to 6.9% as is shown Table 5 on the next page. Performance of Manufacturing Outsourcing Business is likely to strengthen further as the Revised Worker Dispatching Act enforced on September 30, 2015, which is not factored into the forecasts, will apparently serve as a tailwind.

Trend of Main Operating Segments

1H saw significantly stronger results in the Engineering Outsourcing Business

Domestic demand was strong in 1H as in FY12/14. Robust worker demand can be attributed to increased production at export manufacturers benefiting from the weaker yen, return of auto and electronics component production to Japan, and also clients' needs for dispatched employees ahead of the anticipated enactment of the Revised Worker Dispatching Act. Meanwhile, costs increased as the Group's recruiting expenses soared, reflecting very tight overall labor markets. Under such circumstances, the OS Group launched a new initiative to facilitate training and education of worksite employees, thereby adding value to respective personnel, and this resulted in stronger financial results in the 1H.

In the high-margin Engineering Outsourcing Business, 4,285 worksite employees were working at clients' sites at the end of 1H, sharply increasing by 1,392 and 1,014 compared to 1H-end FY12/14 and FY12/14-end, respectively. The number of worksite employees at 1H-end counts 138 more than the Company's plan presented on May 7, the day it released Q1 FY12/15 financial results presentation. Economies of scale from this increase helped absorb increases in costs, leading the operating segment's operating income margin to rise to 6.4% from 4.8% in 1H FY12/14.

●【Table 5】Trend of Operating Segment: 1H FY12/15 Actual and FY12/15 Forecasts

(¥ million)	FY12/14		FY12/15		Full-Year YoY	
	1H Actual	Full-Year Actual	1H Actual	Full-Year Initial Forecasts	Amout	Ratio
Net sales	**28,070**	**59,421**	**36,022**	**74,000**	**14,578**	**24.5%**
Engineering Outsourcing Business	10,381	22,036	14,765	28,568	6,531	29.6%
Manufacturing Outsourcing Business	12,049	25,478	14,031	28,399	2,920	11.5%
Administrative Outsourcing Business	289	601	270	620	18	3.0%
Recruiting and Placing Business	370	779	341	783	3	0.4%
Overseas Business	4,879	10,346	6,535	15,256	4,909	47.4%
Other Business	99	178	78	374	195	109.7%
Operating income	**713**	**2,010**	**937**	**3,100**	**1,089**	**54.2%**
Engineering Outsourcing Business	494	1,423	949	1,965	541	38.1%
Manufacturing Outsourcing Business	195	584	189	713	128	21.9%
Administrative Outsourcing Business	41	92	30	59	(33)	-35.9%
Recruiting and Placing Business	167	354	142	237	(117)	-33.1%
Overseas Business	34	87	(19)	497	409	468.9%
Other Business	4	6	7	9	2	48.7%
Adjustment	(225)	(537)	(362)	(380)	157	-
Operating income margin	**2.5%**	**3.4%**	**2.6%**	**4.2%**	**-**	*+0.8pp*
Engineering Outsourcing Business	4.8%	6.5%	6.4%	6.9%	-	*+0.4pp*
Manufacturing Outsourcing Business	1.6%	2.3%	1.3%	2.5%	-	*+0.2pp*
Administrative Outsourcing Business	14.4%	15.3%	11.5%	9.5%	-	*-5.8pp*
Recruiting and Placing Business	45.3%	45.5%	41.6%	30.3%	-	*-15.2pp*
Overseas Business	0.7%	0.8%	-0.3%	3.3%	-	*+2.4pp*
Other Business	4.8%	3.4%	9.8%	2.4%	-	*-1.0pp*
No. of Worksite Employees at Year-end						
Engineering Outsourcing Business	2,893	3,271	4,285	4,367	1,096	33.5%
(Utilization Rate for Engineering Outsourcing Business)	*(96.8%)*	*(97.3%)*	*(97.5%)*	-	-	-
Manufacturing Outsourcing Business	6,213	6,732	6,935	7,891	1,159	17.2%

Source: Compiled by Trias Corporation from the Company IR materials

By industry, net sales to Electrical & Electronics and Transportation Equipment makers rose 20-60% YoY while those to IT-related clients, the OS Group's focus, jumped 25.3% YoY. Civil Engineering and Construction-related net sales soared by 7.4 times YoY to ¥2.0 billion as acquired operations through M&As contributed. Workers were almost fully dispatched to client sites despite the sharply increased headcount, with the utilization rate up 0.7pp YoY to 97.5%, which also contributed to better profitability.

In Manufacturing Outsourcing Business, the number of worksite employees was 6,935 at the end of 1H, increasing from 6,213 employees at 1H-end FY12/14, but nonetheless, markedly below the target of 7,601 planned in May. This is partly because of the overall tight labor situation but mostly due to the Group's strategy to enhance added-value by converting workers from manufacturing to engineering tasks. The segment income was mostly flat YoY, with sharp rises in recruiting expenses mostly offset by a nearly 10% rise in net sales per employee. By industry, net sales to the Group's mainstay Electrical & Electronics and Transport Equipment led by autos were robust, rising 27.3% and 37.3% YoY respectively.

In the PEO scheme—the Group's new and unique recruiting system where subsidiary PEO Co., Ltd. recruits fixed-term contract employees employed directly by client makers as regular employees prior to employment period expiration, and then lease them to clients participating in the scheme—employees increased from 1,025 at the end of FY12/14, to 1,442 at Q1-end (March), and 1,861 at Q2-end (June). The participating makers of the PEO scheme also rose from 87 to 102 and 104 respectively. It is most likely these numbers will top the initial plans of 2,700 employees and 150 participating makers at the end of FY12/15. This scheme is also contributing to control sharp rises in recruiting expenses.

On the other hand, Overseas Business, deemed as a pillar for future growth, fell short of the initial plan by 5.0%. Recoveries have been somewhat lagging due to sluggish economies in Thailand, Vietnam and Hong Kong where the Group was hoping employment adjustment triggered by last year's coup or civil demonstrations would fade away. Net sales increased 33.9% YoY to ¥6.5 billion, marking a slowdown from the approximately 50% pace through Q3 FY12/14 and resulting in a ¥300 million shortfall to initial forecasts. Q2 saw the operating income level turning positive, but not enough to cover the Q1 loss. Over the last several years, establishing new bases in succession in Southeast Asia has resulted in upfront investment expenses.

Full-year forecasts were left unchanged, however, there is large potential for an overshoot

The OS Group left full-year consolidated forecasts unchanged, also leaving segment estimates unchanged, however, considering 1H results, overall earnings are likely to overshoot forecasts. While there is still potential for a slight shortfall in Overseas Business, favorable domestic business is running well ahead of that.

Engineering Outsourcing Business to which the Company is currently devoting efforts, is looking for net sales to increase 29.6% and operating income 38.1% YoY through recruiting more worksite employees. Actual results would be even higher as was the case in 1H, because strong net sales growth should absorb temporary hikes in expenses for recruiting more worksite employees, or regular use-type dispatched employees, which should lead operating income margin to rise 0.4pp YoY to 6.9%. Engineers are increasing more than planned as existing OS Group companies, namely OUTSOURCING TECHNOLOGY Inc., have been performing well, newly acquired subsidiaries are now fully contributing to financial results, and the Company's new measures to shift employees' tasks from manufacturing to engineering are proceeding more effectively than initially planned.

Manufacturing Outsourcing Business expects operating income to jump 21.9% YoY and operating income margin to improve 0.2pp to 2.5% as net sales maintain double-digit growth, though slightly smaller than that of FY12/14. This may somewhat involve a shortfall risk, however, because the number of worksite employees may not reach the target of 7,891 at the end of FY12/15, as the Company has been strategically reducing traditional outsourcing to manufacturers only for short-term adjustment purposes, and is instead encouraging manufacturing workers to take on engineering tasks. At the same time, the PEO scheme is more likely to roll out in full scale as the Revised Worker Dispatching Act was enforced on September 30.

For Overseas Business, the key is whether it can take back the 1H shortfall to achieve much better profitability as was initially planned. Net sales are expected to soar 47.4% and operating income 5.7 times YoY as upfront investments would gradually bear fruit. Operating income margin is expected to rise significantly from 0.8% in FY12/14 to 3.3%, topping that of Manufacturing Outsourcing Business. Even with potential shortfall risks taken into account, however, net sales should expand to around 20% of consolidated net sales, significantly up from 10.6% three years ago (FY12/12). Structural changes in the OS Group in preparation for contraction in domestic productions, are expected to progress steadily, targeting the FY2017 goal set in the Medium-term Management Plan.

TOPICS: Won order for dispatching of facilities operations personnel for US military base, made acquisitions of overseas IT-related outsourcing business firms, and the Revised Worker Dispatching Act was enacted

Forays into new businesses are progressing steadily. Recent announcements include: winning an order for outsourcing facilities operations personnel at the US military Kadena Air Base in Okinawa Prefecture, and making acquisitions of IT-related outsourcing business firms in Australia and the UK/Europe.

Won order for facilities operations personnel outsourcing business at a US military base

The Company announced on August 3 that it won an order for facilities operations personnel outsourcing business at the US military Kadena Air Base in Okinawa Prefecture. In preparation for this new business, the Company established consolidated subsidiary IOD Inc. ("IOD") in March as the management vehicle, which will conduct dispatching on a scale of 300 personnel to start.

Going forward, the Company plans to develop this business for facilities operations personnel within US military bases in Iwakuni, Yokota, Yokosuka and Zama. According to the Company, the outsourcing market for facilities operations personnel within US military bases in Japan is approximately 40,000 personnel, however, only a small portion of dispatching is handled by regional private firms, and the majority is handled by the Labor Management Organization for USFJ Employees, Incorporated Administrative Agency (LMO/IAA), and lack of competition became a real issue. If the Company's outsourcing business proves to be successful at Kadena, similar expansion to other bases is expected, offering a large potential market to be newly developed by the OS Group.

IOD is targeting net sales of ¥15.0 billion by FY2018. On par with other domestic dispatching business, gross profit margin is estimated at roughly 20%, however the operating income margin has not been decided. This is due to potential to adopt a strategy of initially sacrificing income margin in order to raise the quality of service, with a view toward winning expanded orders at other bases.

Starting up HR services for US military base facilities is not limited to mere expansion of sales, but also has major significance from a management perspective. In the past, the Company has targeted "smoothing earnings through industry diversification," however, since manufacturers and IT-related service providers account for the majority of clients, the Company has been unable to completely eliminate the risks from a Lehman-type global event. However, since facilities operations personnel outsourcing business for US military bases is not susceptible to impact from the business cycle, this new business will provide an extremely stable source of income for the Company.

Based on 1H average monthly net sales per employee for Manufacturing Outsourcing Business of just under ¥350,000, annualized net sales for Kadena facilities operations personnel outsourcing business can be estimated at roughly ¥1.2-1.3 billion. The OS Group apparently has a view toward providing outsourcing personnel for US military bases throughout the Trans-Pacific region (including California, Alaska, Hawaii, Guam etc.), and if this is realized, in addition to domestic business, overseas business will reinforce this stable source of income.

Globalization of IT-related outsourcing business through M&A

Along with announcing 1H FY12/15 financial results on August 6, the Company announced acquisition of 100% of the shares of BLUEFIN RESOURCES GROUP PTY LIMITED ("BLUEFIN GROUP"), the holding company for BLUEFIN RESOURCES PTY LIMITED ("BLUEFIN"), an outsourcing business specialized in providing financial system specialists in Australia, making it a wholly-owned subsidiary.

BLUEFIN was established in 2003, currently holding a large number of professionals in the fields of IT-engineering, accounting, finance, risk management etc., providing staffing services to major banks, government institutions etc. across major cities in Australia. Currently it provides roughly 230 professionals to 40-50 clients, planning to raise this to 300 staff to 60 clients by the end of the current term for FY6/16, according to the Company.

According to the Company, FY6/14 net sales rose +34% YoY to over AUD 40.0 million (roughly ¥3.46 billion on current exchange rates), and net income rose 2.4 times YoY to AUD 1.59 million (similarly

¥137 million). Favorable growth continued in FY6/15, with net sales apparently increasing over +30% YoY, guiding for net sales growth of +20% in FY6/16.

The provisional acquisition value is ¥1,728 million. A portion is scheduled to be paid each year in 2016, 2017 and 2018, depending on financial results. This method called “Earn-out” gives incentive to existing management to raise profitability, helping to prevent staff outflow common after acquisitions.

While the Company says it is too early to estimate the impact on financial results, the Company expressed confidence that it will “be able to recoup the investment within 4 years.”

Then in quick succession, the Company announced a second acquisition on August 25. The Company announced that it acquired 65% of the shares of 4 group companies held by NTRINSIC HOLDINGS LIMITED (“NHL”) based in Europe for ¥1,196 million.

The NHL Group is a specialist provider of independent, freelance consultants for Oracle products in Europe, and from bases established in the UK and Belgium, is engaged in operations in 18 countries across Europe. As an Oracle Gold Partner, NHL has a strong reputation locally, serving mainly large multi-national enterprises as clients.

For the OS Group which has placed priority on strengthening IT-related business, starting with these 2 M&A transactions, the Company is aiming at accelerating globalization efforts, while generating synergies in each region, with a view toward early achievement of its Medium-term Management Plan target in the final year for Overseas Business net sales of ¥41.6 billion.

Enactment of the Revised Worker Dispatching Act is a Tailwind…

The Revised Worker Dispatching Act, which had been delayed several times due to opposition from the opposition parties, was passed and enacted by regular session of the House of Councilors (upper house of the Diet) on September 18, and went into effect on September 30. This likely gives rise to two major benefits for the OS Group: survivor advantage after industry consolidation, and growth in dispatching business.

Basic principles with respect to the Revised Worker Dispatching Act include the following:

I. To promote healthy business development of the dispatching industry as a whole
II. To advance employment security and improved terms for dispatched workers through targeting career advancement and direct employment
III. To create an easy-to-understand system for dispatched workers, company to supply dispatched workers and company to be supplied with dispatched workers

Based on these basic principles, major changes under the Revised Act include the following:

① Coexistence of the "Notification System" with a "Licensing System" until now for dispatching business in all cases becomes a "Licensing System"

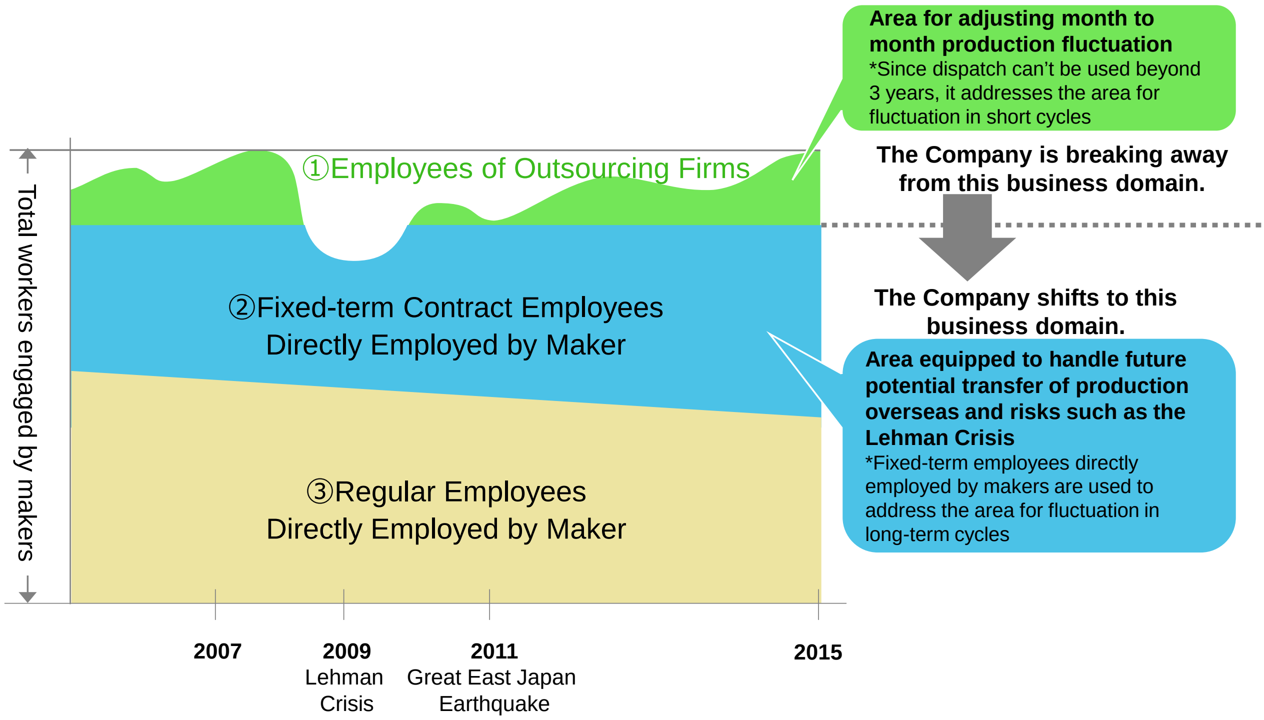
② Previous classifications for 26 specialized occupations and deregulated occupations are abolished, now classified as either indefinite-term employment or fixed-term employment

③ Use of fixed-term employment dispatched workers is subject to a restriction of 3 years maximum, while use of indefinite-term employment dispatched workers is exempt from term restriction

Regarding point ①, since dispatching firms must meet all of the requirements for approval by the Ministry of Health, Labor and Welfare (MHLW), there is high potential that small- and medium-sized firms with poor management resources will be forced to withdraw. This implies a growing market for surviving firms. Regarding points ② and ③, by dispatching firms making dispatched workers indefinite-term employment, companies supplied with dispatched workers can use the same dispatched workers without term restriction.

Here, we look at the composition of production personnel for major domestic automobile makers which have a large number of workers on fixed-term contracts.

●[Graph 1] Composition of Production Personnel for Major Automobile Makers (general image)



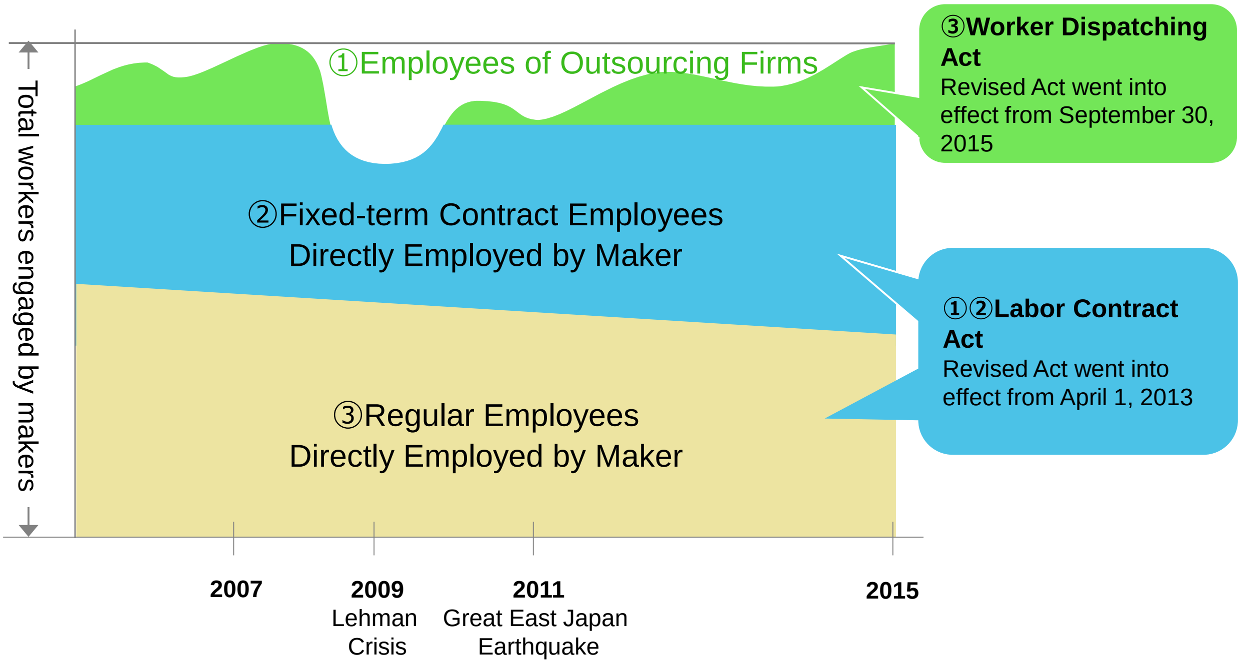
Source: Compiled by Trias Corporation from the Company IR materials

In the case of many domestic automobile makers which have relatively long production cycle work sites, as can be seen in Graph 1, there are 3 types of employment formats. ①regular employees with indefinite-term contract employees directly employed by makers, forming the base of the production worksite. Above this are ②fixed-term employees with fixed-term contracts employed by makers, which become an adjustment valve in the event of production cuts for potential economic risks that can occur over the medium-term or after natural disasters. In the case of ②fixed-term employees, contract terms are relatively long at several years, and they are assigned to operations that require skills/expertise.

In addition, ③employees of outsourcing firms are fixed-term contract employees recruited by dispatching firms on short terms (generally 3-6 months), and since they are used for the purpose of adjusting month-to-month production fluctuations, a high degree of skills/expertise is basically not required.

Next, we look at laws related to each type of employment format. As can be seen in Graph 2, since ① and ② are contract formats for employees directly employed by makers, they fall under the Labor Contract Act, and ③employees of outsourcing firms fall under the Revised Worker Dispatching Act.

●[Graph 2] Labor Contract Formats for Domestic Production Sites and Related Laws



Source: Compiled by Trias Corporation from the Company IR materials

In the case of fixed-term contract employees directly employed by makers themselves, at the time the labor contract expires at a maximum 5 years, if the worker makes a request, the fixed-term contract until then must be converted to an indefinite-term contract.* In other words, makers are faced with the option of either hiring that worker as a regular employee, or letting him/her go. Makers are faced with the decision of whether or not to take on the fixed costs burden from personnel expenses.

*In the past, repeated renewal of fixed-term labor contracts was used to hire the same worker without term restriction, however, with enactment of the Revised Labor Contract Act in 2013, a new rule was introduced whereby, after a consecutive total of 5 years is exceeded, at the request of the employee, the labor contract must be converted to an indefinite-term labor contract (= becoming a regular employee).

However, at production sites of domestic manufacturing firms, due to market changes and whether or not products have competitiveness, there are also many cases of large fluctuations in the level of production. Therefore, the real intention of makers switching from fixed-term contract employees to dispatched employees is likely to avoid taking on fixed costs any more than is necessary. The Revised Worker Dispatching Act has given rise to the possibility of changing personnel expenses for maker directly employed fixed-term employees to variable expense. In particular, this likely has a major impact for the automobile makers which have a large number of fixed-term employees with a high degree of skills/expertise.

The OS Group's PEO scheme business is a promising management vehicle for changing maker personnel expenses into variable expense. This business takes fixed-term employees of client maker firms participating in the PEO scheme, and with the agreement of said workers, makes them into regular employees of PEO Co., Ltd., offering them to PEO participating client maker firms. Through this process, in addition to changing maker personnel expenses into variable expense, this also makes possible securing workers with a high degree of skills/expertise required for ② in Graph 1.

The noteworthy point for the PEO scheme is makers participating in the scheme and the OS Group working together, aiming at employment security and improved terms for workers. As an effort to quickly realize the basic principles of the Revised Worker Dispatching Act, and as an effort committed to the OS Group leading the revitalization of the dispatching industry, there are high expectations for future developments.

The Company's estimate for PEO scheme employees at the end of FY12/15 is 2,700, however, this doesn't incorporate the impact from enactment of the Revised Worker Dispatching Act. Currently almost all participating makers are Electrical & Electronics-related, however, contract terms are short for fixed-term employees in this industry, and compared with the Transport Equipment industry, dependence on fixed-term employees is low. At the same time, Transport Equipment makers, which have the largest number of directly employed fixed-term employees, have been waiting for the Revised Act to go into effect. The target market for the OS Group is the roughly 200,000 fixed-term employees in the Transport Equipment industry, a massive latent market. Also, production cycles for this industry are long over several years, and for the OS Group which has made ③ in Graph 1 as it main battleground, this will facilitate building a more secure business base.

The Revised Worker Dispatching Act was passed, and after going through a preparation period over the next several months, Transport Equipment client makers which have been watching developments are expected to accelerate moves to entrust fixed-term employees to PEO Co., Ltd. In the not-too-distant future after the Revised Act goes into effect, the Company would not be surprised to see the number of PEO employees reach 10,000-20,000.

References

Consolidated Key Financial Data

No. of Shares Issued	Jun-15	17,394,000
No. of Treasury Shares	Jun-15	-
Market Value (￥mn)	1-Oct-15	43,641
BPS (￥)	Jun-15	619.35
ROE (%)	Dec-14	21.6
ROA (%)	Dec-14	5.9
PER (times)	FY12/15 fcst.	23.0
PCFR (times)	Jun-15	63.5
PBR (times)	Jun-15	3.4
Share Price (￥)	1-Oct-15	2,509
Unit Share (shares)	1-Oct-15	100
Average Daily Volume (shs)	1-Oct-15	233,778

Total Assets (￥mn)	Jun-15	27,418
Shareholders' Equity (￥mn)	Jun-15	10,773
Interest-Bearing Debt (￥mn)	Jun-15	(*) 4,893
Equity Ratio (%)	Jun-15	39.3
Ratio of Interest-Bearing Debt (%)	Jun-15	45.4
Free Cash Flows (￥mn)	Jun-15	(729)

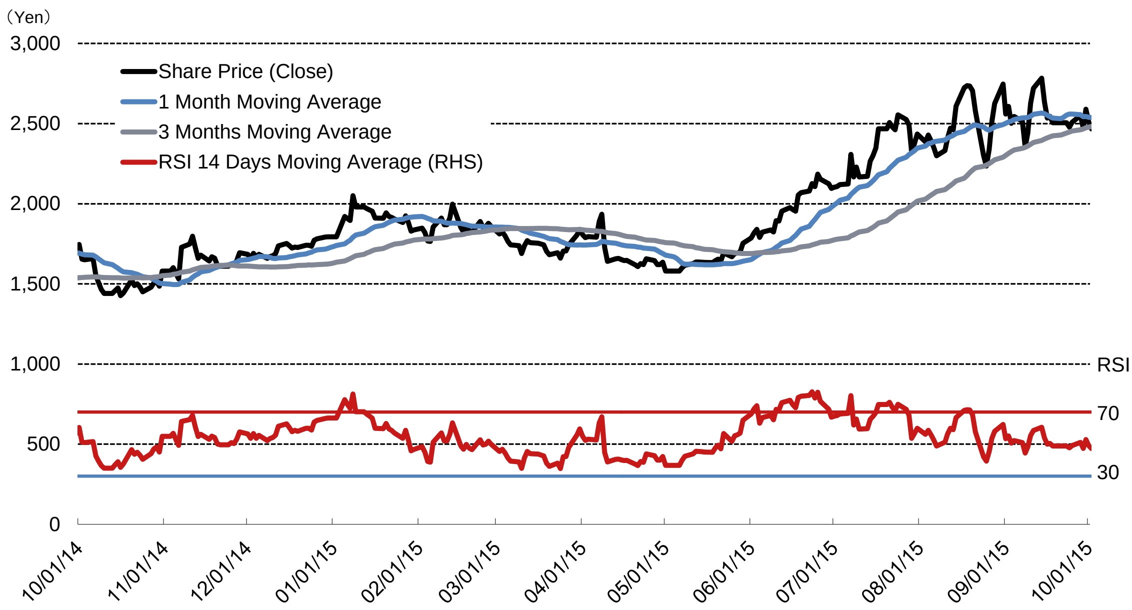
ROE = Net Income ÷ Averaged Shareholders' Equity
ROA = Net Income ÷ Averaged Total Assets
PCFR = Market Value ÷ (Net Income + Depreciation)
Ave. Daily Vol. = Ave. Daily Vol. for the last 12 months
Interest-Bearing Debts* Ratio = I.B.D. ÷ Shareholders' Equity
*Incl. current portion of accounts payable-installment purchase
Free Cash Flows = Operating CF + Investment CF

Consolidated Financial Results

Consolidated (￥million)	Net Sales	Operating Income	Ordinary Income	Net Income	EPS (￥)	DPS (￥)
FY12/11	32,397	563	702	194	13.48	8.00
FY12/12	42,090	1,000	1,153	641	44.46	8.00
FY12/13	47,384	1,202	1,357	1,122	77.54	13.00
FY12/14	59,421	2,010	2,197	1,316	89.81	35.00
1H FY12/15	36,022	937	1,003	488	31.64	0.00
FY12/15 full-year fcst.	74,000	3,100	3,000	1,620	109.12	35.00

Note: FY12/15 forecasts announced on Feb. 12, 2015

Share Prices and RSI (October 1, 2014～October 1, 2015)



Source: Prepared by Trias Corp. with Bloomberg data.
Note: RSI, Relative Strength Index, is the index representing the ratio of overbought or oversold share prices. In general, over 70 in RSI shows overbought share price range, while below 30 shows oversold share price range.
RSI=averaged share price appreciation for N days÷(averaged share price appreciation for N days +averaged share price decline for N days) x100