3. Management Analysis of Financial Position, Operating Results and Cash Flows

(1) Financial Position and Operating Results Situation

The Japanese economy in the fiscal year ended February 28, 2023 showed signs of recovering partly as a result of various policies as we transition to a new stage of living with COVID-19. On the other hand, the outlook remains uncertain due to rising prices and supply side constraints together with a risk that a downturn in overseas economies due to global money tightening may put downward pressure on the economy.
Moreover, with economic activities returning to normal after the COVID-19 pandemic, the rapid increase in recruitment activities has led to significant labor shortages. Together with this, personnel expenses are rising.

Under such an environment, the Group's main customer relationship management (CRM) business is performing well in response to growing outsourcing demand. Furthermore, a further increase in the sophistication of services is being sought in the customer service field. In addition to the diversification of communication methods, with rapid technological innovation, there is a need for automation by introducing artificial intelligence (AI) in dialogue with consumers and capitalization and utilization of dispersed customer support data.

We have been working on "maximizing our workforce of 30,000 employees," the "creation of multifaceted value of voice data" and "growing with partners for credibility and co-creation" in the fiscal year ended February 28, 2023 which served as the final year of our Mid-Term Management Plan.

We started providing the DX Direct Center service which utilizes contact center response logs to increase the sales of clients to achieve the creation of multifaceted value of voice data. The service utilizes the telephone support history in voice data solutions such as voice recognition, text mining and data analysis to achieve optimal customer support. That raises the willingness of customers to make purchases and contributes directly to the business issues of our clients such as improving marketing activities and sales. This service differs to individualized operation which relies on past experiences and intuition. We assign human resources dedicated to data analysis to provide scientific analysis in light of the Group's wide variety of business operation knowledge. Promoting the utilization of voice data such as with issue identification, improvement action plans and operational processes which embody effect measurement allows us to derive the important indicators to solve issues. We then move through the optimal plan, do, check and act (PDCA) cycle. As a result, we are increasing willingness to make purchases and realizing sustainable results through conversations which capture customers' emotions and needs. We will continue to further increase the sophistication of our contact centers as a partner which solves management issues, comes up with improvement proposals and then puts those proposals into practice for our clients in the future.

Moreover, we are working on new challenges (developing business) with highly specialized partners. Specifically, we have established Horizon One Inc. (hereinafter "Horizon One") and made it into a consolidated subsidiary of the Group. This company is a joint venture for the consulting and outsourcing businesses in the personnel and accounting fields with Layers Consulting Co., Ltd. (hereinafter "Layers Consulting"). Horizon One leverages the strengths of both our companies to provide a one-stop service for functions from the upstream to the downstream in the personnel and accounting fields such as strategy formulation, operational reforms, technology utilization, reskilling and operational administration. That will allow it to solve the management issues of companies in an increasingly uncertain environment.

Furthermore, we made an additional investment in Bellsystem24-Hoa Sao Joint Stock Company (hereinafter "Bellsystem24-Hoa Sao"), which runs a contact center business in Vietnam in the Group, in March 2023 as an initiative to strengthen our overseas business. The Group's investment ratio in the company has now reached 80%. Bellsystem24-Hoa Sao is currently responsible for the operations of more than 30 clients including a major telecommunications company in Vietnam. It has 12 contact centers in Ho Chi Minh, Hanoi and Da Nang in Vietnam with approximately 3,400 employees. It has achieved an average sales growth rate of 20% since the Group invested in the company in 2017. Furthermore, since the additional investment, we have been promoting the acquisition of new clients in anticipation of an acceleration in pace of the entry of foreign companies into Vietnam in the future in addition to focusing on telecommunications, finance and e-commerce viewing them as growth industries. We have positioned Bellsystem24-Hoa Sao as the Group's ASEAN strategic base in our offshore business. In addition to supporting digital transformation in domestic contact centers, we are creating synergies with the Group's companies which have strengths in IT helpdesks, clerical BPO, and personnel and accounting BPO to expand our overseas business foundations. We are aiming to create a new market while engaging in advanced contact center operation by supporting the digital transformation of companies in Vietnam with Toppan Inc. (hereinafter "Toppan"), into which we are jointly investing, by leveraging the strengths of both our companies. The Group will position ASEAN as a priority area in our overseas strategy going forward. We will aim to achieve sales of 15 billion yen in our overseas business by fiscal year ending February 28, 2026 in three years by expanding business in Taiwan and Thailand where we have already advanced.

We are proactively promoting at-home contact centers in terms of maximizing our workforce of 30,000 employees. We also received the highest rank of gold for four years in a row in the PRIDE Index 2022. This is an index which evaluates initiatives for LGBTQs and other sexual minorities (hereinafter “LGBTQs”) in the workplace of companies and organizations. It was formulated by the work with Pride voluntary association which supports the promotion and entrenchment of LGBTQ-related diversity management.

Furthermore, in terms of promoting the success of women in the workplace, our company-wide diversity & inclusion (D&I) structure and our initiatives to accelerate the pace at which we develop female leaders have been praised. We received the Grand Prize in the highest-class Advanced Category at the 2023 J-Win Diversity Award. This is a scheme organized by NPO J-Win and backed by the Cabinet Office and the Ministry of Health, Labour and Welfare.

The Group will continue to work to improve the environment inside and outside our company so that employees with diverse backgrounds can work in peace of mind over a long period of time.
In addition, we formulated the Climate Change Policy. Our aim is to realize carbon neutrality by 2040 by promoting aggressive measures mainly with carbon neutralization while evaluating the impact climate change will have on our business and society as an environment, social and governance (ESG)-related initiative. We announce various initiatives and targets and results in each fiscal year on our official website based on that policy. As a result, we have been selected as a constituent of the FTSE Blossom Japan Sector Relative Index. This is a stock index which evaluates Japanese companies that have satisfied global ESG standards. We have also had our MSCI ESG Rating raised from BBB to A.

We will continue to position initiatives for ESG as an important element of the Group’s growth strategy in the future. That will lead to both social contribution and the Group’s growth through the implementation of that.

We give below our performance by segment.

We merged two consolidated subsidiaries on March 1, 2022 with BELLSYSTEM24, Inc. (hereinafter “BELLSYSTEM24”) the surviving company and Pocke Inc. (hereinafter “Pocke”) the absorbed company. Our aim with this merger is to reallocate digital human resources, optimally allocate management resources and build an efficient group operation structure.

As a result, we have included and disclosed in “CRM Business” our system development business for the CRM business of Pocke which was previously included in “Other” from this the fiscal year ended February 28, 2023. Moreover, we have revised and re-stated the segment information for the same period of the fiscal year ended February 28, 2022.

<u>CRM Business</u>

The economic outlook remained uncertain. Nevertheless, spot demand for social infrastructure and sales of existing ongoing projects we started in the fiscal year ended February 28, 2022 increased. In addition, revenue increased year-on-year because synergy projects progressed favorably due to the strengthening of collaboration with ITOCHU Corporation (hereinafter “ITOCHU”) and Toppan. Income before income taxes increased year-on-year partly as a result of the effect from activities to improve earnings in addition to extending income with an increase in revenue.

As a result, revenue in the CRM business was 155,158 million yen (up 6.7% year-on-year) and income before income taxes was 13,900 million yen (up 2.0% year-on-year).

<u>Other</u>

Revenue in our other segment was 896 million yen (down 11.6% year-on-year) because content revenue declined. Income before income taxes increased by 420 million yen year-on-year to 257 million yen. That was mainly because we recorded an impairment loss of 496 million yen in regards to the goodwill attributable to Pocke in the fiscal year ended February 28, 2022.

As a result of the above, revenue was 156,054 million yen (up 6.5% year-on-year), income before income taxes was 14,157 million yen (up 5.1% year-on-year) and net income attributable to owners of the parent was 9,330 million yen (up 4.3% year-on-year) in the fiscal year ended February 28, 2023.

(2) Cash Flows Situation

Cash and cash equivalents as of the end of the fiscal year ended February 28, 2023 increased by 802 million yen compared to the end of the fiscal year ended February 28, 2022 to 6,998 million yen. We give below the respective cash flows situation in the fiscal year ended February 28, 2023 and the factors for them.

Cash Flows from Operating Activities

Net cash provided by operating activities was 18,172 million yen (income of 16,278 million yen in the same period in the fiscal year ended February 28, 2022). This was mainly because income before income taxes was 14,157 million yen, depreciation and amortization were 8,450 million yen, increase in trade and other payables was 721 million yen, financial costs were 557 million yen, interest and dividends received were 399 million yen, income taxes paid were 4,419 million yen, interest paid was 475 million yen and decrease in payable for consumption tax was 448 million yen.

Cash Flows from Investing Activities

Net cash used in investing activities was 1,803 million yen (expenditure of 2,431 million yen in the same period in the fiscal year ended February 28, 2022). This was mainly because proceeds from sale of investment securities were 1,440 million yen, purchase of property, plant and equipment was 1,408 million yen, transfer to escrow account was 717 million yen, purchase of securities was 531 million yen and purchase of intangible assets was 363 million yen.

Cash Flows from Financial Activities

Net cash used in financial activities was 15,583 million yen (expenditure of 13,181 million yen in the same period in the fiscal year ended February 28, 2022). This was mainly because proceeds from long-term borrowings were 24,000 million yen, Increase in short-term borrowings was 5,100 million yen, repayments of long-term borrowings were 33,781 million yen, repayments of lease liability were 6,421 million yen and dividends paid were 4,584 million yen.

Production, Orders Received and Sales

(1) Production Results

The Group does not engage in production activities. Therefore, this item does not apply.

(2) Orders Received Results

The contracts the Group enters into with clients use unit prices which form the basis for fee calculations. The contact center capacity and hours required to calculate the order amount fluctuate frequently depending on the call forecast. Accordingly, it is extremely difficult to specify the order amount. Therefore, we have omitted giving these figures.

(3) Sales Results

We give below our sales results for each segment in the fiscal year ended February 28, 2023.

Segment	Sales (millions of yen)	Year-on-year Comparison (%)
CRM business	155,158	6.7
Other	896	(11.6)
Total	156,054	6.5

Notes:
1. We have offset transactions between segments.
2. We have not included consumption tax in the above amounts.

We give below our sales results by major client and the ratio of those sales with respect to our total sales results.

Client	Fiscal Year Ended February 28, 2022		Fiscal Year Ended February 28, 2023	
	Sales (millions of yen)	Ratio (%)	Sales (millions of yen)	Ratio (%)
Softbank Corp.	15,564	10.6	14,363	9.2

Note:
We have not included consumption tax in the above amounts.

Analysis and Consideration of the Operating Results Situation from the Perspective of Executive Managers

The matters relating to the future in this text are based on judgments made by the Group as of the date on which we submitted this document.

(1) Significant Accounting Policies and Estimates

The Group's consolidated financial statements have been prepared based on international accounting standards. We need the estimates and forecasts of executive managers which may affect the financial position, operating results and cash flows situation on the closing date when preparing these consolidated financial statements. We make those estimates and forecasts based on assumptions we judge to be reasonable in light of past results and the situation. However, actual results may differ from these estimates if there is a change in the preconditions or the subsequent environment.

We give the significant accounting policies, the significant accounting estimates and the assumptions used in making those estimates we adopted when preparing the consolidated financial statements in "5: Accounting Situation, 1. Consolidated Financial Statements, Notes to the Consolidated Financial Statements, 2.3 Summary of the Significant Accounting Policies and 3. Significant accounting Judgment, Estimates and Assumption."

(2) Analysis of Operating Results

(i) Revenue

The economic outlook remained uncertain in our main CRM business. Nevertheless, spot demand for social infrastructure and sales of existing ongoing projects we started in the fiscal year ended February 28, 2022 increased. In addition, synergy projects progressed favorably due to the strengthening of collaboration with ITOCHU and Toppan. That meant revenue in the fiscal year ended February 28, 2023 increased by 9,575 million yen compared to the fiscal year ended February 28, 2022 (up 6.5% year-on-year) to 156,054 million yen.

(ii) Gross Profit

Gross profit in the fiscal year ended February 28, 2023 increased by 1,705 million yen compared to the fiscal year ended February 28, 2022 (up 5.6% year-on-year) to 31,962 million yen. That was partly as a result of the effect from activities to improve earnings in addition to extending income with an increase in revenue.

(iii) Selling, General and Administrative Expenses

Selling, general and administrative expenses in the fiscal year ended February 28, 2023 increased by 660 million yen compared to the fiscal year ended February 28, 2022 (up 4.0% year-on-year) to 17,231 million yen due to an increase in advertising expenses.

(iv) Other Income and Expenses

Other income and expenses in the fiscal year ended February 28, 2023 came to a total of 186 million yen (income).

(v) Operating Income

Operating income in the fiscal year ended February 28, 2023 increased by 1,683 million yen compared to the fiscal year ended February 28, 2022 (up 12.7% year-on-year) to 14,917 million yen because gross profit increased.

(vi) Financial Income, Financial Costs and Share of Profit (Loss) of Investments Accounted for Using the Equity Method

Financial income, financial costs and share of profit (loss) of investments accounted for using the equity method in the fiscal year ended February 28, 2023 were 760 million yen (expenses) (fiscal year ended February 28, 2022: 229 million yen (income)) due to a decrease in the share of profit (loss) of investments accounted for using the equity method.

(vii) Income before Income Taxes

Income before income taxes in the fiscal year ended February 28, 2023 increased by 694 million yen compared to the fiscal year ended February 28, 2022 (up 5.1% year-on-year) to 14,157 million yen because operating income increased.

(viii) Net Income Attributable to Owners of the Parent

Although income taxes increased, income before income taxes increased. That meant net income attributable to owners of the parent in the fiscal year ended February 28, 2023 increased by 387 million yen compared to the fiscal year ended February 28, 2022 (up 4.3% year-on-year) to 9,330 million yen.

(3) Analysis of the Financial Position

(i) Analysis of Assets

Current assets increased by 1,864 million yen compared to the end of the fiscal year ended February 28, 2022 to 30,673 million yen. That was mainly because cash and cash equivalents increased by 802 million yen, other financial assets increased by 655 million yen and other current assets increased by 356 million yen.

Non-current assets decreased by 3,926 million yen compared to the end of the fiscal year ended February 28, 2022 to 145,577 million yen. That was mainly because, although other non-current assets increased by 242 million yen and deferred tax assets increased by 179 million yen, property, plant and equipment decreased by 3,060 million yen, investments accounted for using the equity method decreased by 460 million yen, other financial assets decreased by 431 million yen and intangible assets decreased by 396 million yen.

As a result, total assets decreased by 2,062 million yen compared to the end of the fiscal year ended February 28, 2022 to 176,250 million yen.

(ii) Analysis of Liabilities

Current liabilities decreased by 21,165 million yen compared to the end of the fiscal year ended February 28, 2022 to 46,238 million yen. That was mainly because, although trade and other payables increased by 943 million yen and income taxes payable increased by 553 million yen, borrowings decreased by 20,881 million yen, other financial liabilities decreased by 720 million yen, liabilities for employee benefits decreased by 532 million yen and other current liabilities decreased by 528 million yen.

Non-current liabilities increased by 13,681 million yen compared to the end of the fiscal year ended February 28, 2022 to 65,101 million yen. That was mainly because, although other financial liabilities decreased by 2,945 million yen, borrowings increased by 16,250 million yen and provisions increased by 309 million yen.

As a result, total liabilities decreased by 7,484 million yen compared to the end of the fiscal year ended February 28, 2022 to 111,339 million yen.

(iii) Analysis of Equity

Equity increased by 5,422 million yen compared to the end of the fiscal year ended February 28, 2022 to 64,911 million yen. That was mainly because, although capital surplus decreased by 2,210 million yen, retained earnings increased by 7,054 million yen and other components of equity increased by 382 million yen.

(4) Information on Equity Resources and Capital Liquidity

The Group is continuing to build new contact centers and to update equipment in line with business operation in terms of equity requirements and fundraising. In principle, we will cover these equity requirements with cash on hand. We raise funds as necessary.

Please refer to “2: Business Situation, 3. Management Analysis of Financial Position, Operating results and Cash Flows, (2) Cash Flows Situation” for the cash flow situation.

(5) Factors with a Significant Impact on Operating Results

We recognize that service provision price fluctuations, securing operators and personnel expense fluctuations are major factors with a significant impact on operating results in the Group’s main CRM business. The business environment surrounding the Group is extremely competitive. If the trend for clients to cut costs due to recent economic conditions becomes stronger, it may affect the Group’s operating results. Moreover, most of the costs in this business are personnel expenses for operators. Therefore, the increase in operator costs due to recruiting difficulties and wage increases caused by a lack of human resources will affect the Group’s operating results.

As countermeasures, we will look to differentiate ourselves from other companies by utilizing the results and experience the Group has built up over 40 years and work to improve quality and to provide new solutions. Through those efforts, we will strive to improve operational efficiency and to expand the size of our sales. Together with that, we will strive to set appropriate prices in response to securing operators and the increase in personnel expenses by improving the value of the Group’s brand. In addition, we will continue to develop strategic CRM business and to provide new solutions with the aim of evolving into a partner which can grow together with our clients in the future.

(6) Current Situation and Outlook of Management Strategies

The total size of the contact center outsourcing market, including dispatch sales, to which the Group belongs is 1 trillion yen. It is expected to expand with an annual average growth rate of about 5% from FY2019 to FY2025. Moreover, the oligopoly in the market will continue with the top three to five major companies by sales including the Group (source: Deloitte Tohmatsu MIC Research Institute Co., Ltd.'s "Current Situation and Outlook of the Total BPO Market for FY2022: Contact Center and Fulfillment Service Edition (16th Edition)." With such circumstances, it is believed that, although our top competitors are securing a certain share of this contact center outsourcing market, they are looking to find new means of growth by shifting their focus to peripheral markets. Nevertheless, the Group's policy is to chart a path to growth by continuing to focus on this contact center outsourcing market.

As we mention above, with a few top companies account for the majority share of this market, it is said to be important to expand customer contact focused on voice platforms, improve operational efficiency and utilize data such as by making use of VOC to differentiate ourselves from our competitors. At the same time, it is also said to be essential employees have literacy and skills with respect to voice recognition, emotion analysis and AI. We are advancing the sophistication of such data utilization and striving to improve operational quality and added value. There is a possibility that these efforts will lead to the solutions model with its anticipated high profit margins becoming a new pillar of our business.

The Group's strengths are our scale based on the most extensive network of in-house contact centers in Japan, dialogue skills built up over 40 years, data utilization with new technologies such as AI and teamwork as we work together to tackle difficult issues. In addition to these strengths we have built up, we create synergies in the sales, business development and technology fields with partners such as the ITOCHU Group and the Toppan Group. Through that, we want to achieve further growth in the future as a partner which tackles management issues from the same perspective as our clients and puts into practice improvement proposals.

(7) Executive Managers' Awareness of Issues and Future Policy

The Group's executive management team strives to formulate the best management policies based on the current business environment and available information. The Group will aggressively roll out measures to expand our earnings base with a focus on our main CRM business. We will increase sales by expanding transactions with existing clients and acquiring even more new clients utilizing the diverse corporate networks of the ITOCHU Group and the Toppan Group. We will also implement appropriate pricing in response to the increase in personnel expenses, improve efficiency of operations and utilize synergistic effects with improved profitability through thorough cost control.

We recognize that returning profits to shareholders is one of our most important issues. Accordingly, we pay stable and ongoing dividends of surplus. Our basic policy is to pay a dividend of surplus twice a year with an interim dividend and year-end dividend. Our aim is for a consolidated dividend payout ratio of 50% based on net income attributable to owners of the parent in the medium-term upon comprehensively considering the dividend payout ratio and enhancement of the necessary internal reserves according to the progress of business performance.

Moreover, we will continue our initiatives to improve the environment to realize even more diverse work styles for our employees. We are gradually introducing a new personnel system and human resource development measures to become a company where professionals come together and where work is rewarding. We will also provide development programs to promote the success of women in the workplace, establish in-house nurseries and open educational training facilities. In addition to those initiatives, we will encourage the success in the workplace of diverse human resources by striving to encourage D&I and health management.

Furthermore, we will create new business value for our clients by providing them with optimal solutions. That is in addition to realizing a customer experience which impresses our clients through initiatives for automation utilizing new technologies such as AI and hybrid operation through value provision brimming with hospitality characteristic of humans.

We will not limit ourselves to simply being an outsourcer focused on cost reduction as before; rather, we will continue to strengthen our business foundations to ensure the key measures we have set forth in our Mid-Term Management Plan 2025 contribute to our profit as a partner which tackles management issues from the same perspective as our clients and then puts into practice and implements improvement proposals.