DTS (TSE Code: 9682)

Leveraging a sound financial position to make bold growth investments and shareholder returns

Report Summary

A medium-sized SIer with good results

DTS (TSE PRM 9682) is a system integrator (SIer) that provides development, introduction, operations, and maintenance services for business systems and information and communications infrastructure. In the fiscal year ended March 2024, the company had net sales of approximately 115.72 billion yen, placing it around 30th among Japanese domestic SIers. Operating profit for the fiscal year ended March 2024 was 12.5 billion yen or 10.8% of net sales. The company earns around 60% of its net sales from the financial, insurance, and information and communications sectors, which are industries that invest heavily in systems, and it can expect to continue seeing stable growth in earnings in the future.

Achieving the targets of the current medium-term management plan ahead of schedule

DTS is currently driving its business based on a medium-term management plan that ends in the fiscal year ending March 2025. The numerical targets set forth by the plan are net sales of 110 billion yen and EBITDA of 13 billion yen in the plan's final year, but both were achieved ahead of schedule in the fiscal year ended March 2024.

As for management efficiency, whereas the target for the final year of the medium-term management plan being an ROE of 13% or more, the actual result for the fiscal year ended March 2024 was 11.8%. With one year remaining in the medium-term plan, its financial aspects are progressing favorably.

KEY STATISTICS

Key Stock Statistics

Recent Price (09/04/2024)	¥4,100.00
52-week High/Low	¥4,330/¥2,998
Shares Outstanding	46,852,132 shares
Market Cap	¥183,600 million
PER	19.58 times
PSR	1.60 times
Dividend (Dividend Yield)	¥103.00 (2.6%)

Sector

Sector	Information and communication

Financials (FY 03/2025 CE)

Net sales	¥125,000 million
Operating profit margin (%)	10.6%
EBITDA margin (%)	12.0%

Management

President & CEO	Tomoaki Kitamura
URL	https://www.dts.co.jp/en/

Growth strategy with a focus on improving productivity

DTS is working to grow its business from two perspectives: (1) increasing the number of employees providing its services, and (2) improving productivity per person. Regarding (1), the company has not been able to rapidly achieve tremendous increases in its workforce due to a lack of personnel in the IT industry nationwide and because, up through the previous medium-term plan, the company had not been targeting an increase in its workforce (the number of employees increased from 5,604 in March 2022 to 5,703 in March 2023 and 6,157 in March 2024). Therefore, increasing net sales and profits through (2) is essential. The company is boosting its efforts to win orders for high-margin upstream projects and prime contracts through measures such as establishing a dedicated inside sales team. It has committed to investing 7.5 billion yen in human resources development over the three years of its medium-term management plan to improve productivity. The current medium-term plan targets an operating profit of 3.1 million yen per employee in its final year.

Aiming to expand on upselling performance by emphasizing focus businesses

In terms of improving productivity, the expansion of new business areas, which DTS calls "focus businesses," is also expected to make a significant contribution. Focus businesses refer to a group of businesses that target capturing the strong demand for digital transformation (DX), such as the expansion of cloud infrastructure business and cyber security-related services. They have a full range of services that can be used to create higher-priced projects while entering upstream processes, such as consulting to reengineer customer business processes.

The focus businesses also aim to expand stock earnings by building long-term relationships with customers by providing operation and maintenance services after the introduction of systems.

Improving capital efficiency through M&A investment and shareholder returns

Like other companies in the SIer industry, DTS is growing its business through both M&As and organic measures. In the fiscal year ended March 2024, organic growth was expected to contribute 4.8% of the increase in net sales, with the remaining 4.2% coming from M&A growth. The company has a high equity-to-asset ratio of around 73%, which gives it a lot of leeway in terms of investment, but it has also set hurdle rates based on the cost of shareholder's equity. The company has also reinforced its governance by appointing Independent Outside Directors as a majority of the Board of Directors, and it has also put in place a framework to ensure that investment decisions are made reasonably.

In its medium-term management plan, DTS set targets of a dividend payout ratio of at least 50% and a total return ratio of at least 70% for shareholder returns. In the fiscal year ended March 2024, it achieved both targets by a wide margin, with a dividend payout ratio of 61.1% and a total return ratio of 96.5%.

It is worth noting that the cash allocation set out in the long-term vision "Vision2030" aims to reduce the ratio of cash and deposits to total assets to 30%. In the future, we can expect DTS to implement bold return measures alongside growth investments.

Share price rising similarly to other companies in the industry over the past five years

Share prices for SIer companies overall have increased over the five years from July 2019 to June 2024, driven by the strong performance of the information systems market. DTS's share price rose by 76.4%, approximately the same as the average of other SIer companies with high sales. Some of its competitors have seen rises of over 130%, and it is thought that DTS shares also have the potential to perform equally well if conditions are met.

The systems integration industry is generally expected to have high growth potential, and most companies in the industry have a PBR of over 1.0. DTS's PBR is currently at 2.9, which is favorable. However, if the company can achieve a higher level of efficiency, such as a ROE in the 15%–20% range (the target figure in the medium-term management plan is 13% or more in the final year), it is possible to expect a PBR of over 6.0, which would be on par with certain major companies. In addition, the operating profit margin of SIers with high stock price performance, especially those in the consulting sector, is over 10%, and it is thought that DTS reaching a higher profit margin than its current level would also be a positive factor for the stock price.

Attention turns to independent SIer companies in an industry of ongoing restructuring

Traditionally, the SIer industry has continuously inched toward an oligarchy-type structure, where new groups are repeatedly formed through numerous M&As among companies within the industry. At present, there is a certain possibility that some action will be taken toward DTS as an independent SIer that does not have a capital relationship with any particular affiliated company. In any case, it is still important for the company being acquired to deploy high-value services and to remove any factors that could cause dissynergy in management integration. The acquiring company also needs to be careful not to overestimate the premium on the market capitalization and to be creative in the governance of the subsidiary after the merger. It is worth noting that, in the SIer industry in general, there is an increasing trend of switching overseas development work from offshore to nearshore due to factors such as country risk and exchange rates.

Other potential business risks for DTS include cyberattacks on systems for which it was involved in development and operations, the shrinking of system operations and maintenance service markets due to customers' various efficiency measures, such as the automation of operation BPO, uncrewed operations, AI operations/non-operations, etc.

GIR View

Expectations of the Japanese ICT market to exceed 30 trillion yen

The size of the Japanese ICT market (enterprise IT spending) hit 27.2 trillion yen in 2022 and has been growing steadily at an annual rate of approximately 2.1% since 2018. The market continues to expand at an accelerated pace with factors such as the increasing adoption of digital transformation and the expansion of infrastructure investment in cloud security-related areas. In particular, the widespread use of AI and the increase in cyberattacks are leading to a rise in the number of companies increasing their system investment. In turn, this is creating a positive outlook for system integrators (SIers), including DTS. The impacts of the COVID-19 pandemic are also expected to provide a tailwind, with companies moving to the cloud as they relocate or downsize their offices and other companies strengthening their cloud-based ICT infrastructure to promote data-driven business.

DTS achieved record-high net sales of 115.7 billion yen and operating profit of 12.5 billion yen in the fiscal year ended March 2024

DTS's net sales for the fiscal year ended March 2024 were approximately 115.72 billion yen, and the company has continued to grow at an annual rate of 5% over the past 10 years. Operating profit has grown at an annual rate of 7.9%, notably higher than net sales. Additionally, in the fiscal year ended March 2024, operating profit landed at 12.5 billion yen, representing 10.8% of net sales.

Under Vision2030, DTS aims to achieve net sales of at least 180 billion yen and EBITDA of at least 23 billion yen by fiscal 2030. In order to accomplish this, and in light of the company's current performance, it is thought that in addition to organic growth measures, expansion of at least double that amount will be necessary through M&A, and it will be essential to carry out effective deals (Note: In the fiscal year ended March 2024, performance increased by 4.8% with the full-year contribution of Calance, which was acquired in fiscal 2022, and the new consolidation of Anshin Project Japan Inc. and up 4.2% as a result of organic measures).

Reforming the business portfolio over the medium to long term by intensively strengthening focus business areas as pillars of growth

DTS has named the new DX-related business areas "focus businesses," with the potential of being pillars of its next-generation earnings and is promoting them in its medium-term management plan and Vision2030. For example, "ServiceNow," for which a promotion team was established in October 2022, is an offering related to digitalizing workflows and integrating and linking multiple systems. It is a mechanism for DTS to accompany its clients as a onestop service provider, from business consulting to system implementation and subsequent maintenance and operation. In addition, the focus is on solutions that aim to achieve sustainable earnings by linking to the operation phase while proposing these as the prime contractor, such as introducing and operating zero-trust solutions and the "DTS Data Management Solution" that supports data-driven management.

The medium-term management plan aims to first increase the proportion of focus businesses to at least 40% of company-wide net sales, and Vision2030 seeks to reverse the relationship with existing businesses by bringing the proportion up to 60%. In this way, DTS is gradually moving away from the traditional systems development contract business model and is instead planning to transition to a solution sales-based business that builds long-term relationships directly with user companies. At present, the target of 40% of net sales in the medium-term management plan has already been achieved, giving the company a smooth start.

DTS is pursuing both aggressive growth investment and shareholder return measures, making use of its ample capital base

While the equity-to-asset ratio of major Japanese domestic SIers is distributed in the 40% to 50% range, DTS's equity-to-asset ratio is a remarkably high 74% or more. The company's high degree of flexibility in investment, which stems from this balance sheet characteristic, is being allocated to M&A, human resource training, and R&D as part of its growth strategy from a medium- to long-term perspective, and the cumulative investment maximum for the current mid-term management plan's three-year period has been set at 25 billion yen.

The company is committed to achieving an ROE of 13% or more in the fiscal year ending March 2025, the final year of its current medium-term management plan. In addition to the know-how it has accumulated over many years through its human resource development and M&A activities, Global IR, Inc. (GIR) believes that DTS is acquiring a system for efficient management by establishing a framework for making investment decisions with an awareness of the cost of capital.

In addition, the company has announced its intention to actively return any surplus cash that accumulates after making growth investments to its shareholders. Under Vision2030, the company aims to achieve a payout ratio and total return ratio of 50% and 70%, respectively, each fiscal year. In terms of cash allocation, the company plans to reduce the ratio of cash and deposits to total assets to 30%, and the balance sheet with an equity-to-asset ratio in the 70% range will be significantly restructured in the future.

The trend towards group formation in the SIer industry is inevitable

In the SIer industry, there is a trend towards group formation and an oligopoly-type structure by major companies in the long term. In fact, domestic SIers in Japan have expanded their business through repeated M&A within the industry since the 2000s. CTC (formerly ITOCHU Techno-Science) merged with former CRC Solutions in 2006, TIS merged with INTEC Holdings in 2008, and in 2011, the former Sumisho Computer Systems merged with the former CSK to form SCSK. These are just a few of the many major examples. It is also fresh in our memories that in 2023, NTT DATA integrated NTT Group's overseas businesses and achieved over 4 trillion yen in sales.

Even when we look at the US, since the dawn of ERP and CRM in the 1990s, companies such as IBM, Accenture, and EDS have been acquiring many medium- to small-scale SIers, and in recent years, M&As have been accelerating again towards the provision of new technologies such as AI, IoT, and 5G, with the acquisition of Altran by Capgemini and the acquisition of Red Hat by IBM. More recently, in August 2024, it was announced that investment fund Kohlberg Kravis Roberts & Co. L.P. (KKR) would launch a takeover bid for FUJISOFT. Following this, Bain Capital also made a takeover bid approximately 5% higher than that of KKR.

In light of this trend, for small to semi-major SIers that could be acquired, in addition to aiming for synergy effects with the buy-side by developing high-value-added services for a deal on favorable terms, it is also important to improve the management structure, such as by controlling debt. It is essential to remove any factors that could cause dissynergies by improving the management structure, such as controlling debt. DTS is no exception, and while the company is independent and has no capital relationship with any particular affiliated company, there is a possibility that it will be involved in the restructuring of other major groups in the future.

Implement a growth strategy will also require adapting to changes in the technological environment, such as with low-code/no-code tools

The recent spread of low-code and no-code tools is an important development for SIers that undertake contract development. These tools existed as concepts in the early 2000s, but their use spread rapidly from the mid-2010s with the launch of Microsoft Power Apps and Google App Maker. Recently, there has been an increase in cases where complex business systems and custom solutions are developed using platforms such as OutSystems and Mendix, and this is a trend that cannot be ignored even for DTS, which is mainly involved in business systems for large companies.

Low-code/no-code tools are compatible with agile development methods, as they have the advantage of enabling rapid prototyping and iterative development, making it possible to release products quickly, and their visual development environment facilitates communication between the development team and user departments. Although they are often promoted on the premise that "even non-technical people can participate in development," these tools are still "development environments," and system engineering skills and experience are still required. Therefore, it is unlikely that the market for outsourced development will shrink significantly simply due to low-code/no-code tools. Instead, for SIers moving forward, it is thought that there will be an increase in expectations for BPO and PMO businesses, such as providing advice and support on how to use tools and taking responsibility for the overall promotion of development projects while assuming the existence of citizen developers and development staff in user departments. DTS is also working to strengthen its ability to propose agile development as part of its focus businesses, as well as providing the low-code application development environment "Creator Workflow" as part of the aforementioned ServiceNow.

Figure 1: Consolidated Results

Fiscal Year	Net sales (mn)	YoY (%)	Operating profit (mn)	YoY (%)	Ordinary profit (mn)	YoY (%)	Profit (mn)	YoY (%)	EPS (Yen)	PER (times)
FY 03/2015	74,609	116.3	6,432	135.7	6,518	135.5	3,692	139.1	156.7	10.5
FY 03/2016	82,537	110.6	7,599	118.2	7,707	118.2	4,341	117.6	186.6	11.5
FY 03/2017	79,858	96.8	7,986	105.1	8,093	105	5,121	118	222.4	12.4
FY 03/2018	83,163	104.1	8,523	106.7	8,574	105.9	5,765	112.6	247.9	14.8
FY 03/2019	86,716	104.3	9,789	114.8	9,929	115.8	6,817	118.2	292.2	14
FY 03/2020	94,618	109.1	10,674	109	10,849	109.3	7,317	107.3	158	11.9
FY 03/2021	90,493	95.6	10,817	101.3	11,131	101.3	7,593	103.8	165.4	15.2
FY 03/2022	94,452	104.4	11,196	103.5	11,403	102.4	7,853	103.4	172.7	15.5
FY 03/2023	106,132	112.4	11,694	104.4	11,932	104.6	8,001	101.9	181.4	17.7
FY 03/2024	115,727	109	12,508	107	12,831	107.5	7,293	91.1	168.5	23.8

Source: Prepared by Global IR, Inc. based on company securities reports and company IR materials.

Note: Rounded to the nearest million yen, rounded to one decimal place *Calculated by Global IR, Inc.

FAQs from Meetings with Investors

Regarding the improper payment incident at an overseas subsidiary

Q1. What is the general outline of the improper payment incident at an overseas subsidiary that was investigated starting in April 2024?

The management of DTS's overseas subsidiary made payments for work that did not exist, then collected the cash and delivered it to the customer to win the business. The improper payments were made systematically starting from 2011, before DTS made the overseas company into a subsidiary, which continued until March 2024, even after becoming a subsidiary in 2019. During the most recent month, the improper activities were discovered through an internal tip-off. The total amount of improper payments identified by the special investigation committee for the period under investigation, from the fiscal year ended March 2020 to the fiscal year ended March 2024, was 107 million yen. The name of the subsidiary in question has not been disclosed.

Q2. What impact did this incident have on DTS's business performance?

The earnings report for the fiscal year ended March 2024 has been corrected and announced on August 15. Consolidated profit attributable to owners of parent (profit) was revised downward by 1.5 billion yen, and the corrected profit was 7.2 billion yen, a 9% decrease compared to the previous year (before the correction, it was 8.8 billion yen, an 11% increase). The direct impact of the incident was a loss of around 500 million yen due to additional tax provisions, etc. However, in addition to this, a new goodwill impairment loss of 1 billion yen was recorded as a subsequent event due to a conservative review of business plans at group companies other than the group company in question. The securities report for the fiscal year ended March 2024 has been submitted to the Kanto Local Finance Bureau.

In the fiscal year ending March 2025, several hundred million yen in investigation costs will be recorded, and there is also a possibility that the authorities will impose a fine after the investigation is completed.

Q3. What measures are being taken to prevent a recurrence?

Measures to prevent a recurrence were formulated and announced on August 15, 2024. As a group, DTS will prioritize compliance in developing its global strategy and implement a new auditing process to prevent inappropriate transactions. In addition, the relevant overseas group companies will rebuild their auditing committee system with independent outside members and appoint external experts as auditing committee members.

Regarding the recent strong performance

Q4. In the first quarter of the fiscal year ending March 2025, net sales increased by 8% year-on-year, and operating profit increased by more than 5%, making for a strong start. What are the factors behind the strong performance?

A large-scale system development project from Mizuho Bank has contributed to solid sales and profits. Orders from Mizuho Bank have been increasing since around 2022, sometime after the bank's system failure scandal ended. Orders from other megabanks and major insurance companies, including expected orders, are also continuing. Many of these projects involve migrating core banking systems to the cloud, making it easier to secure profits.

Q5. How do you acquire the pipeline of projects?

Many of the projects we work on are repeat business from existing clients. We work with consulting firms for new projects and are often called to work on system development projects arising from business reengineering consulting or IT strategy consulting projects. In addition, in recent years, we have often been introduced as a partner by package vendors such as SAP.

Regarding the development services and solutions that DTS sells

Q6. Does DTS often develop systems from scratch, or do you often customize and introduce existing packages?

Traditionally, DTS has specialized in from-scratch development, and sales generated by from-scratch development are still large, such as in the integration of systems for banks, for example. At the same time, in recent years, the company has gradually increased the proportion of solutions sales that combine packaged software and DTS's technology. This is the essence of Technology and Solutions, and the medium-term management plan focuses on next-generation products that will lead to high productivity and profitability.

Q7. What kind of packages do you handle?

SAP, mcframe, ServiceNow, and intra-mart are some of the major sales items on a sales basis. SAP, in particular, may have a strong image in the accounting and production management fields, but DTS specializes in introducing Success Factors, a package in the human resources field. While SAP projects related to human resources are often out of the target for larger SIers, such as SCSK, in terms of size, they cannot be delivered by smaller SIers, either. Therefore, this is a promising area for DTS, which is positioned in between, to be unlikely to encounter competition.

Shareholder Return Measures

Q8. How will you strike a balance between growth investment and shareholder return?

We have set aside a budget of 25 billion yen for growth investment in our medium-term management plan, and we will steadily implement this. While our priority remains growth, we will actively use surplus funds for shareholder return. While maintaining a policy of a dividend payout ratio of 50% or more and a total return ratio of 70% or more, we are also working on a cash allocation plan to reduce the current cash ratio of 70% of total assets to 30% by 2030.

Regarding Strengthening the Management Base

Q9. What is the progress of strengthening the management base, including ESG management?

Over the past five years, DTS has strengthened its dialogue with shareholders and, in addition to measures for returning profits, has been considering governance, environmental measures, and the promotion of women. Concerning the ratio of female managers, we have set a target of achieving a ratio of at least 6% during our medium-term management plan, and as of the personnel changes on April 1, 2024, we have reached a level of 5.1%. In addition, we have already achieved some items ahead of schedule, such as the ratio of outside directors and female directors, and we are on track.

Q10. How are you responding to the IT industry's overall shortage of human resources?

In FY2023, the company managed to keep the employee turnover rate for the parent company down to around 5%. In terms of recruitment, the company hired 221 new graduates against a target of 200 and 33 mid-career hires against a target of 40. The fact that the company was able to hire so many new graduates was partly because it has MIRUCA, a company within the group that specializes in human resources training. On the other hand, the company has not achieved its target for mid-career hires, so it is working actively with recruitment agencies.

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Company Profile

Business Activities

DTS is an independent SIer that handles system integration, software development, and hardware sales. Currently, the company has adopted a three-segment system as the premise of its business strategy, adding a cross-section of technology and services to the industry and regional classifications.

Figure 2: Overview of Business Segments

Segment	Details	Net sales/ Composition ratio (FY 03/2024)
Operation and Solutions	A group of solutions specialized for individual industries that make use of project management skills and industry knowledge	436.6 million/37.7%
Technology and Solutions	Responding to diverse needs regardless of industry or sector through digital technology and solutions	422.1 million/36.5%
Platform and Service	IT equipment installation, IT platform construction, operation monitoring services, etc.	298.4 million/25.8%

Philosophy

Technology is the power to make people happy and create greater enrichment in society

At DTS Group, we use:

technology to build the trust and confidence of our customers,

technology to increase our corporate value,

technology to improve the lives of our employees,

technology to contribute to society.

Vision

Vision2030: "Become a company that continuously takes on challenges in order to provide value that exceeds expectations"

The DTS Group will provide value that exceeds the expectations of our customers, shareholders, business partners, employees and their families, and the society surrounding all of them.

Japan's domestic systems integrator market and the characteristics of DTS

In this section, we will look at what kind of business a systems integrator (SIer) operates and how the companies that compete in this field are managed in order to understand the competitive environment surrounding DTS. As the services offered by each SIer are similar, it is difficult to clearly distinguish between companies from the outside, except for their sales and staff numbers. In light of this, we will spend this section highlighting the characteristics of DTS through comparisons with its competitors.

A continually growing IT market

In FY2023, the size of the IT market (IT investment by Japanese domestic companies, including hardware, software, and services) was 14.93 trillion yen, a 5.4% increase over the previous year. The market is performing well due to factors such as the increased digital transformation activity and the expansion of infrastructure investment related to cloud security. In addition, digital investment in all industries in FY2023 was 762.9 billion yen, a 23% increase compared to the previous year's results and the highest since FY2005. With the spread of AI, telecommunications companies are rushing to improve their data centers, and there is also a trend toward increasing investment in measures against cyberattacks in response to a series of major incidents. For these reasons, SIers can be said to be in a promising market overall.

Figure 3: Enterprise IT spending by industry in Japan (billions of yen)

	2022 expenditure	2022 growth rate (%)	2023 expenditure	2023 growth rate (%)	2024 expenditure	2024 growth rate (%)
Banking/Investment Services	4,401	7.9	4,699	6.8	5,011	6.6
Communications/Media/Services	4,925	6.2	5,130	4.2	5,365	4.5
Education	414	-11.5	418	1.1	429	2.5
Government/Local Government	4,641	7.7	4,886	5.3	5,097	4.3
Healthcare/Life Sciences	1,137	4.1	1,181	3.9	1,226	3.8
Insurance	1,657	5.2	1,740	5.0	1,826	4.9
Manufacturing/Natural Resources	5,955	3.4	6,178	3.7	6,456	4.5
Oil/Natural Gas	138	1.8	141	2.6	145	2.9
Power/Gas/Water	727	2.5	750	3.1	789	5.2
Retail	1,275	4.9	1,350	6.0	1,439	6.6
Transportation	1,089	3.8	1,143	5.0	1,195	4.5
Wholesale	887	3.5	917	3.5	952	3.8
Total IT Spending	**27,246**	**5.2**	**28,534**	**4.7**	**29,931**	**4.9**

Source: Prepared by Global IR, Inc. based on the 2023 Information and Communications White Paper (Ministry of Internal Affairs and Communications)

If we look at the IT market by sector, the ratios for finance, information and communications, and public services are high. In particular, the scale of core banking systems is large, and the level of difficulty in their development is high, so both development and maintenance costs are enormous. Reorganization is progressing in the financial industry, centering on regional banks, and competition between Japanese domestic SIer companies over system integration projects is expected to intensify.

By solution, cloud services are still robust. According to the "2023 Information and Communications White Paper" data compiled by Japan's Ministry of Internal Affairs and Communications, the Japanese domestic public cloud market size was 2.1594 trillion yen (29.8% increase year-on-year) in 2022. The market is expected to continue to grow due to factors such as the migration to cloud services in line with office relocations and downsizing in response to the COVID-19 pandemic, and the strengthening of ICT infrastructure that utilizes cloud services to promote data-driven business.

However, as in other industries, there is a shortage of human resources, and it is thought that industry restructuring through major M&As will also advance at the same time to make up for this.

History of consolidation within the industry

SIers in Japan have a variety of origins, including companies that were initially the service departments of computer manufacturers, spin-offs of the information systems departments of manufacturers and financial institutions, trading companies, and foreign-affiliated companies. NTT DATA, which originates in the Data Communications Division of Nippon Telegraph and Telephone Public Corporation, and the hardware manufacturers Fujitsu, Hitachi, NEC and the foreign-affiliated IBM Japan are five of the major players. Semi-major players include the trading company-affiliated ITOCHU Techno-Solutions Corporation (CTC), BIPROGY (formerly Nihon Unisys), SCSK, the user-originated TIS, NS Solutions (NSSOL), the logistics company Otsuka Corporation, and the think tank company Nomura Research Institute. The manufacturers among these companies have also been involved in businesses other than system construction, and because of their large scale, they have been distinguished from companies that specialize in system integration.

Among the SIers that do not own hardware, NTT DATA is by far the largest company. The company's sales exceeded 1 trillion yen in the fiscal year ended March 2007 due to domestic and overseas acquisitions. Most recently, it integrated NTT Group's overseas business and achieved 4.1 trillion yen in sales in the fiscal year ended March 2024. It has surpassed Fujitsu, which is expected to reach 3.86 trillion yen, and has become the top SIer in Japan. The next largest companies after NTT DATA are Nomura Research Institute, ITOCHU Techno-Solutions (CTC), TIS, and

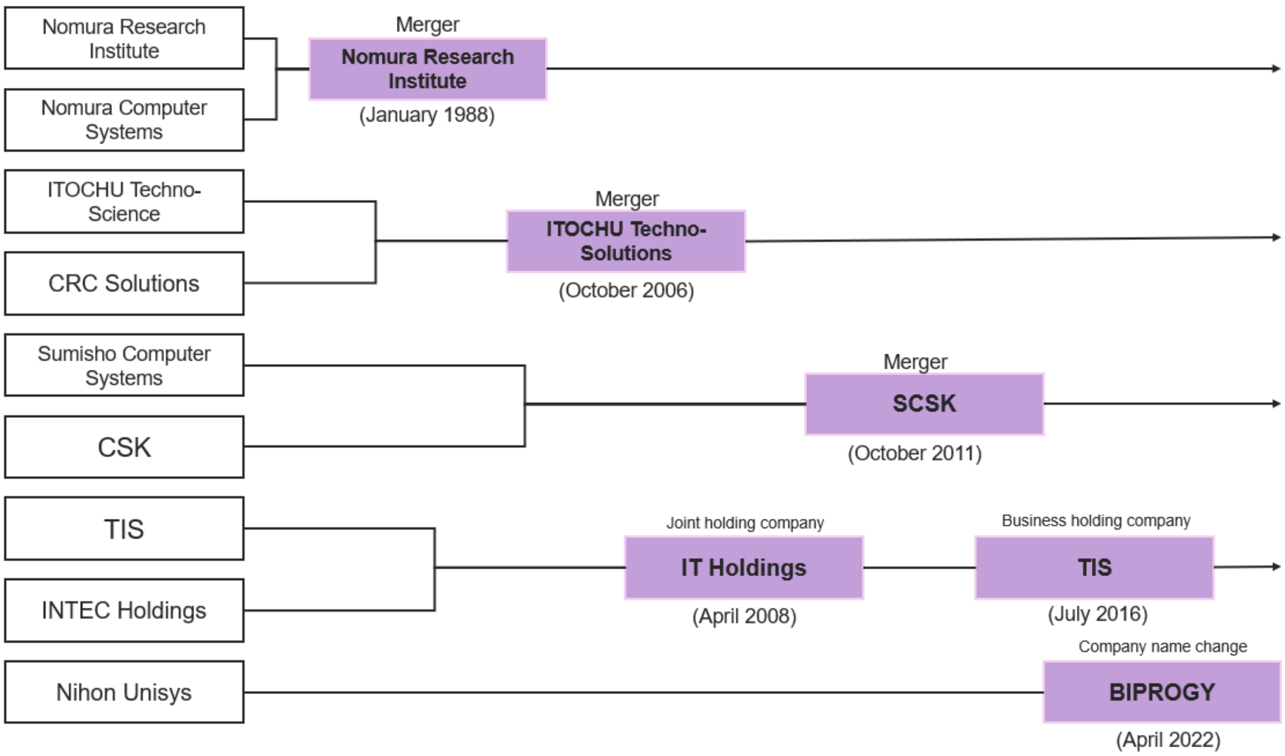
SCSK.

These semi-major system integrators have a history of expanding their business through repeated mergers and acquisitions since the second half of the 2000s. CTC (then known as ITOCHU Techno-Science) merged with former CRC Solutions in October 2006, and TIS merged with INTEC Holdings in April 2008. In October 2011, the former Sumisho Computer Systems merged with the former CSK to form SCSK.

Even in the United States, since the 1990s, which was the dawn of ERP and CRM, companies such as IBM, Accenture, and EDS have been acquiring many medium- to small-sized SIers. In recent years, M&As have again been accelerating, with companies such as Capgemini acquiring Altran and IBM acquiring Red Hat in order to provide new technologies such as AI, IoT, and 5G.

As you can see, non-organic tactics have traditionally played an important role in business growth and market share acquisition in the IT services market.

Figure 4: History of the business integration of major Japanese domestic SIers



Source: Prepared by Global IR, Inc.

Major M&As in recent years

Even after entering the 2020s, the trend continues for M&As in Japan's domestic SIer industry to strengthen high-value-added areas such as consulting and cloud services and expand business in response to the growing demand for DX.

For example, in May 2024, NTT DATA made a tender offer for the shares of JASTEC Co., Ltd. The purchase price was up to 34.246 billion yen, with a 34.26% premium added. NTT DATA had a long-standing partnership with JASTEC, and the acquisition was intended to strengthen its competitiveness in the IT services market, which is in a strong demand environment amid intensifying competition to acquire engineering talent.

In April 2024, Fujitsu made Ridgelinez Limited, a company with strengths in cloud services, a wholly-owned subsidiary. As it was already a consolidated subsidiary, the impact on valuation was limited, but it is thought that the purpose was to consolidate cloud services businesses within the group and improve the efficiency of management resources.

These acquisitions are sometimes carried out to acquire new technologies or use facilities owned by overseas companies as R&D bases. However, in many cases, they are simply a way of solving the labor shortage problem. Because the skills required to work at an SIer, such as project management, coding, and system testing, are to a certain extent modularized and standardized, the acquisition of an established SIer is a logical choice for securing a large number of ready-to-work human resources. As the trend towards industry consolidation by major companies and investment funds is set to continue, it is strategically important for medium- to small-sized companies to aim for synergy effects by developing high-value-added services and removing factors that could lead to dissynergy, such as improving their management structure, so that acquisitions can be carried out on more favorable terms.

The announcement of a TOB by KKR, an investment fund, for FUJISOFT in August 2024 was also a move that attracted attention in the industry in recent years. The purchase price was 8,800 yen per ordinary share, and this price included a 31% premium on the closing price on June 14 of the same year when FUJISOFT received the proposal, with the total amount reaching approximately 560 billion yen. It is said that the reason for this is that activists have been confronting FUJISOFT, and the aim is to stabilize the shareholder structure. However, some integration with another SIer will likely take place in the future with the aim of an exit. Following this, there was also a TOB proposal from Bain Capital for a higher amount than KKR, so the situation surrounding M&As for SIers in Japan continues to be something to keep an eye on.

Investment in human resources to achieve a high-profit structure

The semi-major system integrators mentioned above often play the role of first-tier subcontractors, but they also act as prime contractors for certain customers. DTS does not currently fit in the net sales range of the semi-major system integrators, but in terms of the percentage of prime contracts, which is over 70%, it can be said that the two companies are similar in terms of their position. As we will discuss later, the key issue for companies in this layer is how to increase the proportion of prime projects that can charge high unit prices as part of their growth strategy.

In addition, securing personnel who can steadily carry out projects is essential to expand business. However, the IT industry currently has one of the most significant labor shortages. Therefore, each company needs to secure a human resources pool through recruitment and business integration and train personnel with experience to deliver high-unit-price projects reliably.

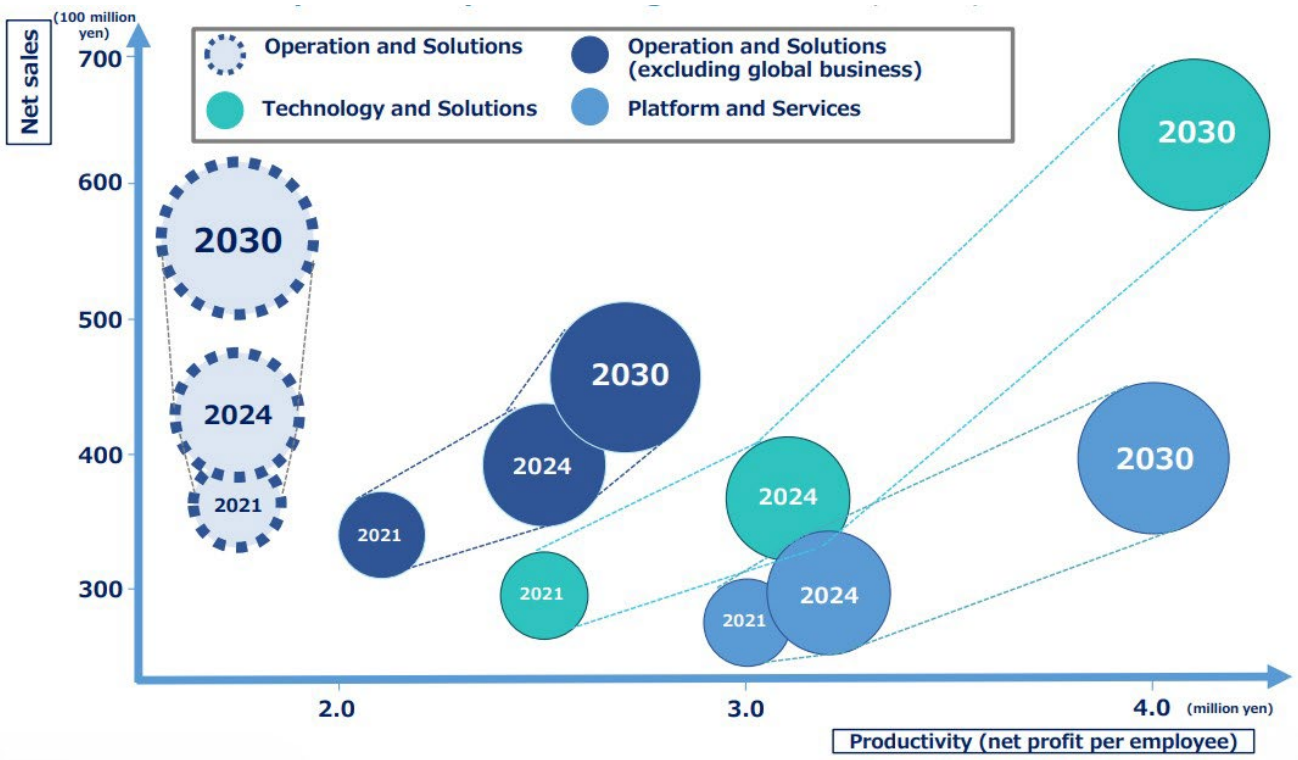
Figure 5: Number of employees and profit per person at major SIers in Japan

Source: Prepared by Global IR, Inc. based on materials from each company

Looking at the above chart, which shows the increase in staff numbers at each of the semi-major companies and the trend in operating profit per person, we can see that, except for Nomura Research Institute, which has a strong strategy consulting division with high unit prices, the profit per person for all the other companies is in the range of 2-3.5 million yen, and that each of the semi-major companies is steadily increasing its productivity per person year on year. This shows that the market is becoming one where companies can pass on the cost of training staff members who can provide high value to their customers.

In relation to this, as will be explained later, DTS has committed to investing 7.5 billion yen of the 25 billion yen growth investment target in its current medium-term management plan in human resource development and is expanding its workforce, increasing base salaries and allowances, and implementing educational training for the development of highly skilled personnel. The company aims to achieve a profit of 4 million yen or more per person under its Vision2030, and it is clearly placing importance on increasing productivity and its workforce.

Figure 6: Net sales and productivity of each segment in 2021, 2024, and 2030



Source: Excerpt from the DTS Medium-Term Management Plan

Comparison of valuations of SIer companies

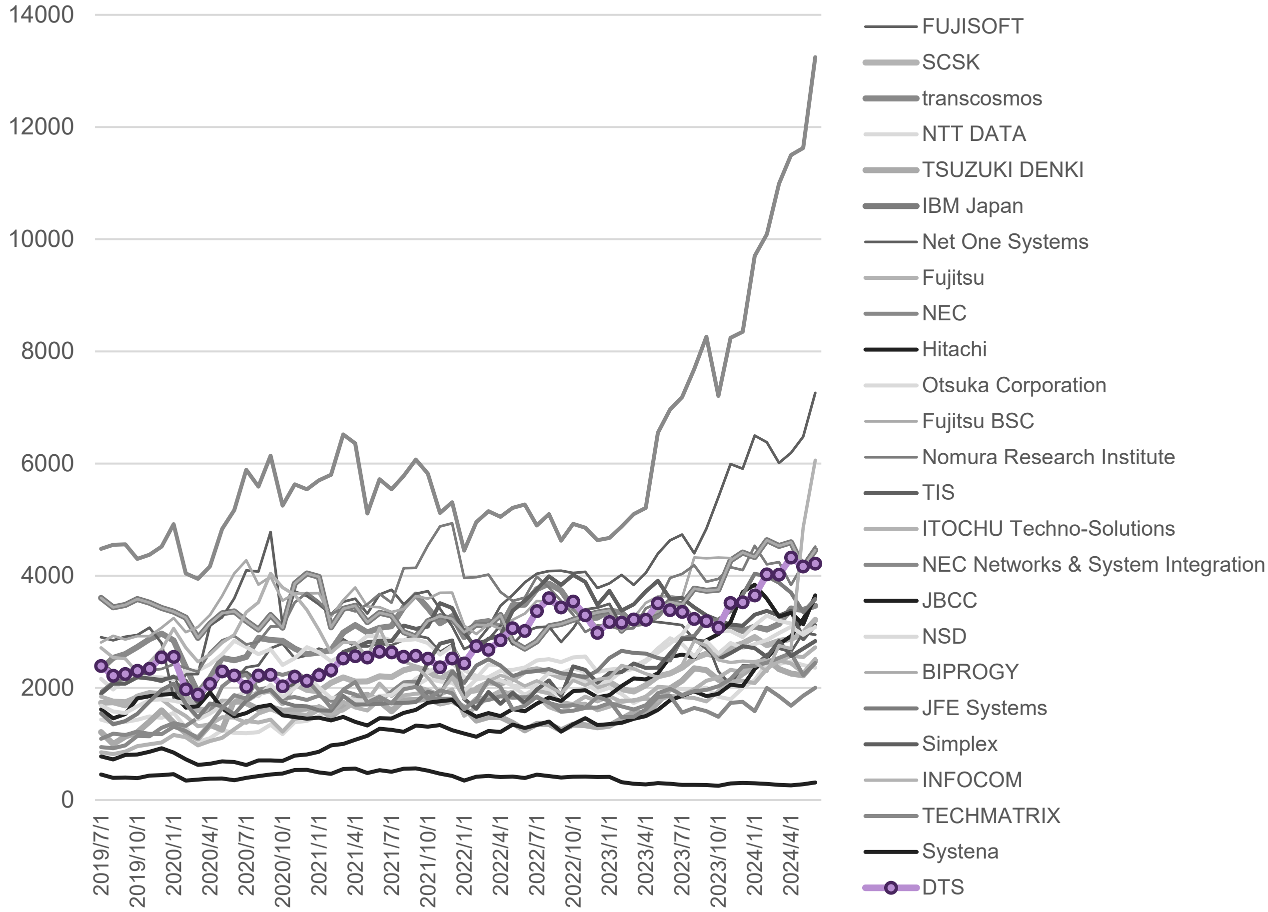
Let's look at the companies among Japanese domestic SIer companies that have seen their share prices rise significantly over the past five years and compare their valuation characteristics.

In the graph on the next page, we have selected the top 25 listed SIers in Japan with a high turnover, excluding companies with large turnover from other businesses, such as Fujitsu and Hitachi, and plotted the monthly share price trends from July 2019, which is five years back from June 2024 (we have used the closing price at the end of each month).

Many companies saw their share prices rise, reflecting the strong performance of the information systems services market. The average growth rate over the five years was 175%, and DTS's share price also grew by a similar amount (from 2,390 yen per share at the end of July 2019 to 4,215 yen per share at the end of June 2024).

If we extract the companies that have seen their share prices increase by 220% or more over the past five years, we get a list that includes FUJISOFT (295%), Nomura Research Institute (233%), NEC Networks & System Integration (259%), JBCC (226%), JFE Systems (232%), and INFOCOM (223%).

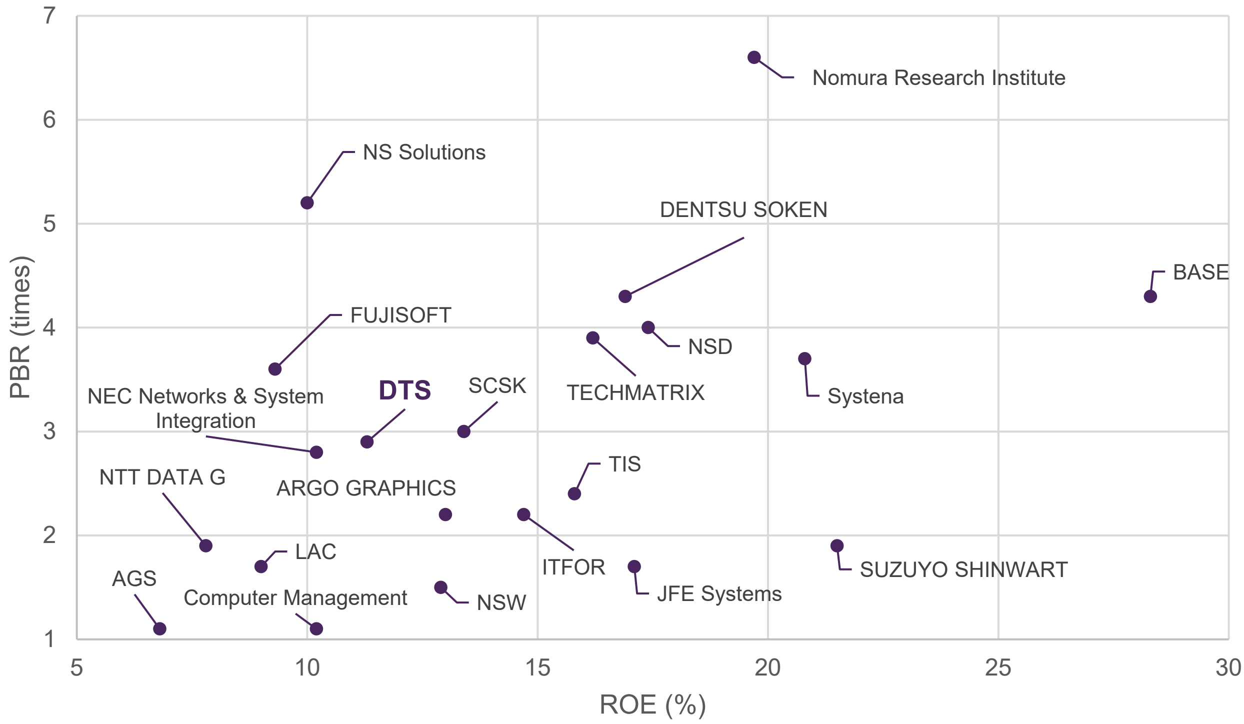
Figure 7: Trends in share prices of major Japanese domestic SIers over the past 5 years (Unit: yen)



Source: Prepared by Global IR, Inc. based on materials from each company

The business scale and profit margins vary for these SIers, which have excellent stock price performance. However, their ROEs are generally distributed in the 10%-19% range, which is high compared to other industries. The figure of 13% or more in ROE that DTS targets in its medium-term management plan also falls within this range. IT service companies, including system integrators, tend to be characterized by business models that make it easy to accumulate cash, such as subscription models and prepayment of fees, and the tendency for them to have high ROE reflects the fact that the market demands high capital efficiency that makes use of cash.

Figure 8: Comparison of ROE and PBR for major SIers in Japan



Source: Prepared by Global IR, Inc. based on materials from each company

Next, if we compare the relationship between ROE and PBR, we can see a fairly loose correlation (see above). Compared to other companies with solid stock prices, DTS has room to grow in terms of ROE. It is thought that increasing this will positively impact valuations, including PBR. One of the key points in increasing ROE is the equity-to-asset ratio.

Figure 9: Comparison of PBR and financial indicators for major SIers in Japan (based on FY 03/2024 financial results)

Code	Company name	PBR (times)	EV/EBITDA (times)	ROE (%)	Equity-to-asset ratio (%)
4348	INFOCOM	6.8	23.9	13.6	72.4
4307	Nomura Research Institute	6.7	15.6	19.9	43.3
9749	FUJISOFT	3.6	18.1	9.3	49.2
9682	DTS	2.8	10.1	11.8	74.2
9889	JBCCHD	2.7	8.7	15.0	56.9
1973	NEC Networks & System Integration	2.5	9.5	10.0	53.5
4832	JFE Systems	1.9	5.6	17.1	61.9

Source: Prepared by Global IR, Inc. based on materials from each company

As you can see from the table above, compared with the other system integrators whose share prices have risen significantly, DTS stands out for its high equity-to-asset ratio. If the company can make use of this characteristic in the future and direct its abundant capital towards flexible and effective growth investment and shareholder returns, there is room for significant growth in profitability. In terms of shareholder returns, the company has set a target of achieving a dividend payout ratio of 50% or more and a total return ratio of 70% or more in the fiscal year ending March 2025, the final year of its current medium-term management plan, and is putting forward strategies that are in line with this direction. Furthermore, the cash allocation target in Vision2030 is an aggressive one, aiming to reduce the ratio of cash and deposits to total assets to 30% or less. If this is achieved, it will certainly be a positive factor for valuations. Already, the board of directors has decided to acquire up to 6 billion yen in treasury shares by the end of 2024, and progress is also being made with measures to improve ROE.

Of course, if the company can generate high profits through growth investments, this will also positively impact efficiency. In the next section, we will examine the specific details of DTS's growth strategy.

DTS's Growth Strategy

In this section, we will look at the kind of business DTS has been developing and how it plans to achieve future growth using its cultivated capabilities and business excellence. In light of the competitive environment and the factors necessary for success in the SIer business outlined in the previous section, as well as DTS's strengths and challenges, it can be understood that the company is developing its management to achieve steady growth.

History

The history of DTS Corporation can be traced back to Data Communication System Co., Ltd. which was established in 1972. Data Communication System Co., Ltd. grew by taking advantage of the wave of account system integration that was taking place in the financial industry at the time and by receiving many large-scale bank-related projects. In the 1980s, the company grew steadily in response to strong demand for systems, including the spread of PCs, eased regulations in the financial industry, and the change of the era in Japan to Heisei. In the 1990s, the company expanded its business in its original areas of strength, finance and telecommunications, in response to the spread of the Internet, Japan's financial Big Bang, and the shift to multimedia in the telecommunications industry.

Regarding capital policy, the company was listed on the Second Section of the Tokyo Stock Exchange in 1997 and then on the First Section in 1999. In 2002, it became a loan stock on the First Section of the Tokyo Stock Exchange.

Around the time the company changed its name to DTS Corporation in 2003, the IT industry as a whole was going through significant changes, such as downsizing and a move towards open systems, and there was a wave of industry restructuring and the emergence of large SIers. DTS responded by promoting the grouping of companies, including making medium-sized SIers like JAPAN SYSTEMS ENGINEERING CORPORATION and SOUGOU SYSTEM SERVICE CORPORATION into subsidiaries. Several new companies were also established in line with the implementation of various measures, such as the development of new businesses and overseas expansion.

In response to the rise of Big Tech and the spread of new technologies such as cloud technologies, AI, and big data that occurred in the 2010s and beyond, the company is working to improve its PM capabilities and is focusing on acquiring prime projects. Furthermore, DTS has been actively pursuing M&As both in Japan and overseas, including the absorption of DATALINKS CORPORATION and the acquisition of Nelito Systems Limited and Partners Information Technology, Inc. as subsidiaries.

In this way, DTS has steadily expanded its business while responding to dynamic environmental changes. In 2022, the year the current medium-term management plan began, it was transferred to TSE Prime.

1972	Data Communication System Co., Ltd. established.
1991	Registered with the Japan Securities Dealers Association as a storefront sales brand.
1997	Listed on the Second Section of the Tokyo Stock Exchange.
1999	Listed on the First Section of the Tokyo Stock Exchange.
2000	KYUSHU DTS CORPORATION established.
2001	DATALINKS CORPORATION becomes a subsidiary.
2002	Becomes a loan stock on the First Section of the Tokyo Stock Exchange.
2003	Company name changes to DTS Corporation.
2006	Japan Systems Engineering Corporation becomes a subsidiary.
2007	SOUGOU SYSTEM SERVICE CORPORATION becomes a subsidiary. Established MIRUCA CORPORATION. Established DTS (Shanghai) CORPORATION.
2009	Established Digital Technologies Corporation.
2011	Established DTS palette Inc. as a special subsidiary. Established DTS America Corporation.
2014	Established DTS WEST Corporation. ART System Co., Ltd. becomes a subsidiary. YOKOGAWA DIGITAL COMPUTER CORPORATION becomes a subsidiary. Established DTS SOFTWARE VIETNAM CO., LTD.
2015	Merged DTS WEST Corporation and SOUGOU SYSTEM SERVICE CORPORATION (Company name changes to DTS WEST CORPORATION).
2017	Capital alliance formed with Nelito Systems Limited of India. Merged YOKOGAWA DIGITAL COMPUTER CORPORATION and ART System Co., Ltd. to establish DTS INSIGHT CORPORATION. DATALINKS CORPORATION becomes a wholly owned subsidiary through a share exchange.
2018	Merged DATALINKS CORPORATION through an absorption-type merger.
2019	DTS (Shanghai) CORPORATION signs an agreement with Dalian SuperElectronics Co., Ltd. to increase its stake. Nelito Systems Limited becomes a subsidiary.
2021	I NET Rely Corporation becomes a subsidiary.
2022	Moved to the Tokyo Stock Exchange Prime Market. Partners Information Technology, Inc. becomes a subsidiary.

2023	Anshin Project Japan Inc. becomes a subsidiary.

DTS's Strengths

DTS's strengths as an SIer lie in three areas: (1) its customer base, (2) its capabilities as an SIer, and (3) its sound financial position.

First, regarding (1) its customer base, it has long-term relationships with large corporate clients, mainly in the banking, insurance, manufacturing, and government sectors. The number of clients the group has is over 1,700, and the percentage of prime projects it receives as the prime contractor is about 70% and is on the rise. In other words, contrary to the image of being a company that undertakes commissioned development generally held by SIers of a similar scale, DTS has established long-term relationships directly with its prime clients. In terms of project leads, in addition to direct inquiries from client companies, there are also many cases where projects are formed via consulting companies or through direct introductions from package vendors such as SAP.

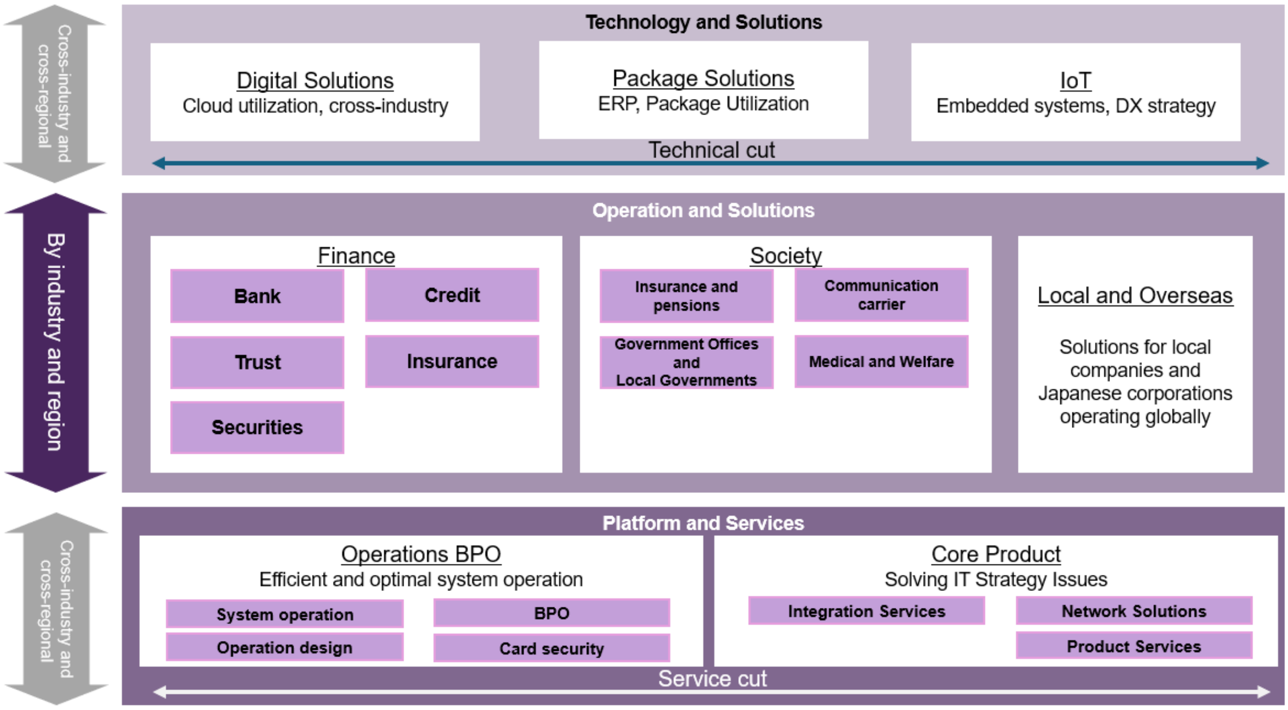
The reason why DTS is continuously receiving orders for projects centered around prime contracts is, of course, because of its capabilities as an SIer. The company has a wide range of proposals based on a high level of understanding of client companies' businesses, and it is particular about and strong in developing systems with few errors. In addition, the company steadily implements each project using project management (PM) capabilities cultivated through more than 50 years of experience in systems development and integration. As of 2022, the number of people capable of performing PM will account for 12.8% of the total, and this is also a prerequisite for the composition of projects centered on prime contracts.

DTS's sound financial position (3), as described below, has created the leeway to enable proactive investment in growth. The equity-to-asset ratio for the fiscal year ended March 2024 was 73.4%, and the net cash ratio was 39.1% (both on a consolidated basis), which are both incredibly high.

Business Overview

DTS's business was reorganized into three segments in the long-term growth strategy Vision2030 announced in 2022 at the same time as the medium-term management plan: the Operation and Solutions segment, which constructs and introduces systems specialized by industry; the Technology and Solutions segment, which provides technologies and solutions that cut across industries; and the Platform and Services segment, which consists of hardware sales and operation and maintenance services. The organization was also reorganized into a business management system based on these segments.

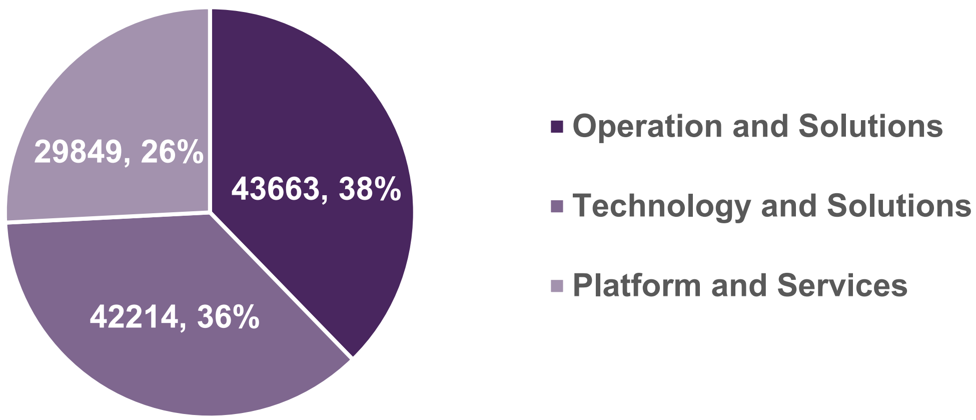
Figure 10: Overview of segment structure



Source: Prepared by Global IR, Inc. based on company materials

The first segment, Operation and Solutions, provides system development services, mostly in the financial sector, that leverage the industry-specific business knowledge the company has cultivated over many years. At present, the company continues to receive large orders, mainly for projects to migrate the core systems of major banks and insurance companies from on-premise to cloud-based systems. As of the fiscal year ended March 2024, the Operation and Solutions segment accounts for 38% of net sales, the largest among the segments. The Operation and Solutions segment is positioned as a "cash cow" since it leverages operational knowledge and PM capabilities cultivated over many years to provide value.

Figure 11: Net sales by segment for the fiscal year ended March 2024 (millions of yen)



Source: Prepared by Global IR, Inc. based on financial statements

On the other hand, the Technology and Solutions segment can be described as the current "star." This business specializes in digital technology and solutions, with cloud business at its core, and uses the latest technology to meet the DX needs of a wide range of customers across all industries. DTS has positioned this segment as its main engine for medium- to long-term growth, and has achieved the most significant growth, with net sales in the fiscal year ended March 2024 increased by 22.7% compared to the same period in the previous year. Organizational expansion and growth investment for this purpose are also most active in this segment, and the company is hiring and training full-stack engineers with diverse skills, as well as DX consultants and business producers.

The Platform and Services segment includes the construction of IT infrastructure, including hardware installation, and subsequent operational BPO, such as monitoring services. While operation and maintenance services are positioned as a recurring-revenue base, the hardware sales segment has high volatility in net sales between fiscal periods due to the large amount of money involved in each sale. For this reason, there are some fiscal periods when net sales decline, but this does not mean that the business is in a state of decline, and it should be considered as a recurring revenue base that supports the continued growth of the company's overall business.

Recent business performance and future outlook

For the fiscal year ended March 2024, net sales were up 9.0% year-on-year to 115.72 billion yen, operating profit was up 7.0% year-on-year to 12.5 billion yen, and EBITDA was up 9.3% year-on-year to 13.58 billion yen. The company achieved its medium-term management plan targets for operating profit and EBITDA one year ahead of schedule.

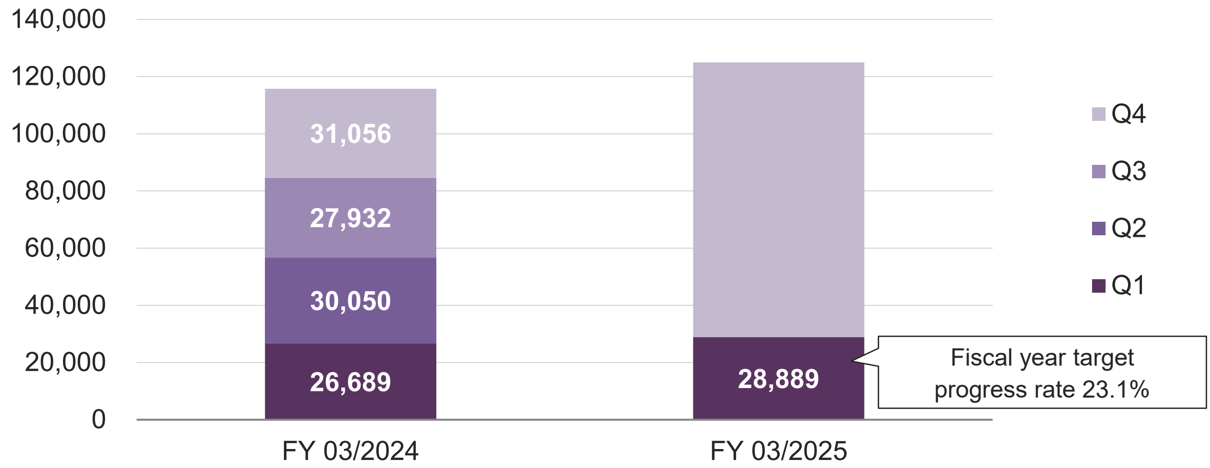
With regard to net sales, the main factors behind the increase were projects related to the modernization of the banking industry and public sector projects in the Operation and Solutions segment, as well as solutions for the manufacturing industry and new consolidations in the Technology and Solutions segment. In line with this, operating profit also increased in the Operation and Solutions and Technology and Solutions segments. The Platform and Services segment saw a 280 million yen decrease in profit, equivalent to 8.8% year-on-year, but this was due to a decline in hardware sales, and we believe it to be a temporary phenomenon. In fact, the company received a large order for hardware in the first quarter of the fiscal year ending March 2025 and is firmly securing profits.

For the full year of the fiscal year ending March 2025, the company plans to achieve net sales of 125 billion yen, 113.6% of the medium-term plan target, operating profit of 13.3 billion yen, 110.8% of the medium-term plan target, and EBITDA of 14.95 billion yen, 115.0% of the medium-term plan target. Compared to the previous year, net sales are targeted at an increase of 8.0%, operating profit at an increase of 6.3%, and EBITDA at an increase of 10.0%. Given the trends in these performance indicators to date, these are solid targets at a reasonable level. The first quarter got off to an excellent start, and there is no sign of a downturn in the future performance outlook.

In the second quarter, there is expected to be a few hundred million yen impact on profits in the Operation and Solutions segment due to investigation costs related to the misconduct at an overseas group company that came to light in May 2024, but the impact on the company's overall performance targets will be minimal.

DTS has continued to grow without a decline in profits, even amid the global investment restraint caused by the COVID-19 pandemic. In the banking industry, which is the company's primary customer, interest rate hikes are expected in line with the rise in policy interest rates, and a significant increase in revenue is expected. In addition, it is thought that banks will become more active in system investment, which can be said to be a significant business opportunity for DTS. As we will touch upon later, DTS's strategy toward focus businesses, which aims to capture the strong demand for DX across all industries, will also drive earnings growth. With the market conditions as a tailwind, the company will continue to achieve steady growth in its traditional areas of strength, such as from-scratch system development and solution sales, and the probability of achieving its medium-term plan targets is exceptionally high.

Figure 12: Breakdown of quarterly net sales (millions of yen)



Source: Prepared by Global IR, Inc. based on company materials

Focus Businesses

DTS is emphasizing its focus businesses, combining digital-, solution-, and service-related businesses in the DX domain common to each segment. It has positioned this as a growth area in its medium-term management plan. It is fair to say that the focus businesses have driven the strong performance described above. The medium-term management plan targets increasing the ratio of net sales in focus businesses to total net sales to 40% by the fiscal year ending March 2025. This target was achieved in the first year, and the company is now working towards the target of 60% in Vision2030. DTS has traditionally specialized in from-scratch system development in the legacy domain but is gradually shifting to providing service solutions that combine existing packages and digital technology. The focus businesses are symbolic of this.

Figure 13: Overview of Focus Business Areas by Segment

Segment	Focus Business Area	Details
Operation and Solutions	Strengthen AP development capabilities based on cloud architecture	Containers, DevOps, microservices, CI/CD, etc.
	Strengthen responsiveness to agile/low-code development	Scrum/ServiceNow, OutSystems, GeneXus, etc.
	Expand and create more industry-specific solutions and services	AMLion, DAVinCI LABS, etc.
Technology and Solutions	Operational reform DX	Transition from from-scratch to SaaS-based system development methods
	Cloud infrastructure	Provision of cloud integration services that combine multi-cloud, cloud security, etc.
	Strengthening cloud business technology and transforming business models	AWS, Azure, ServiceNow, Snowflake, Okta, etc.
	Data utilization	BI tools, data utilization and operational improvement specific to the manufacturing industry, GalleriaSolo, etc.
	Expanding and strengthening ERP business	SAP, others
	IoT	Strengthening data utilization and edge data linkage, creation of new businesses
	Housing	Walk in home, HOUSING CORE
	Zero trust	Support for security risks associated with workstyle reform
	Establishing edge AI and cyber security technology	AI, LSI design (RISC-V, Am), etc.
Platform and Services	Expansion of operation service offerings centered on ReSM and ReSM plus	AWS, Azure, ServiceNow, zero trust
	Strengthening and expanding sales of HybridCloud, Data Management, etc.	AWS, Azure, Vmware, cloud, telework, HCI, various backup solutions
	Promotion of network integration business	SDN, 5G, VPN, WAN, LAN, Internet Security, etc.

Source: Prepared by Global IR, Inc. based on company materials

■ Operation and Solutions segment

The main focus businesses of the Operation and Solutions segment include "enhancing cloud architecture-based application development methods," including technologies for containers, DevOps, microservices, and CI/CD (an approach that automates and continuously performs build, test, delivery, and deployment processes in software development); "strengthening of responsiveness to agile/low-code development," such as with Scrum, OutSystems, and GeneXus; and the "expansion and creation of industry-specific solutions and services," such as AMLion and DAVinCI LABS. Of these, the cloud-related solutions are by far the most profitable, followed by RPA (robotic process automation) and low-code/no-code development. In terms of expanding industry-specific solutions services, the company has enhanced the functionality of its anti-money laundering system AMLion. The system complies with international standards and has been introduced by major securities companies for use in their money laundering and terrorist financing countermeasures operations, including checking against economic sanctions lists and negative news.

■ Technology and Solutions segment

The Technology and Solutions segment has the highest proportion of net sales from focus businesses of any segment, and a wide range of service offerings are being developed and deployed.

For example, in the operational reform DX area, DTS combines its own services and technologies with the workflow package ServiceNow to provide solutions that optimize customers' business operations. Rather than the traditional approach of creating solutions in response to customer requests, the aim is to propose solutions in areas that customers are not yet aware of and to drive business forward with these services. This can be said to be a service development that considers the trend in system development, which is shifting from development from scratch to the use of SaaS.

In the cloud infrastructure area, rather than sticking to integration with Amazon's AWS, which has a high market share, they are focusing on and evolving cloud integration that always provides the optimal environment for customers, such as by combining it with Microsoft's Azure and other application layer cloud services and adding security.

In data utilization and ERP, DTS has launched and is promoting its own BI (business intelligence) solutions, Geminiot and Pasteriot.mi, which analyze and visualize various data to make it useful for management and business. Pasteriot.mi is a solution specializing in the manufacturing industry and combines the world of digital twins and AI. It collects and analyzes data and can link to operations by advancing data utilization suited to the manufacturing industry. DTS specializes in industries where the company has operational expertise, such as the manufacturing industry, and makes DX proposals to bring innovation to customers' operations. This is because the company first intends to accumulate specialized know-how and then expand by combining new technologies. DTS is also reviewing its ERP packages. The company plans to identify which areas of the various packages are growing and where there is potential for success, then focus on initiatives to maximize the company's strengths.

In the IoT field, the company is working to create new businesses by strengthening data utilization and edge data collaboration, using the technologies of group companies that are strong in device control systems and focusing on IoT as a starting point.

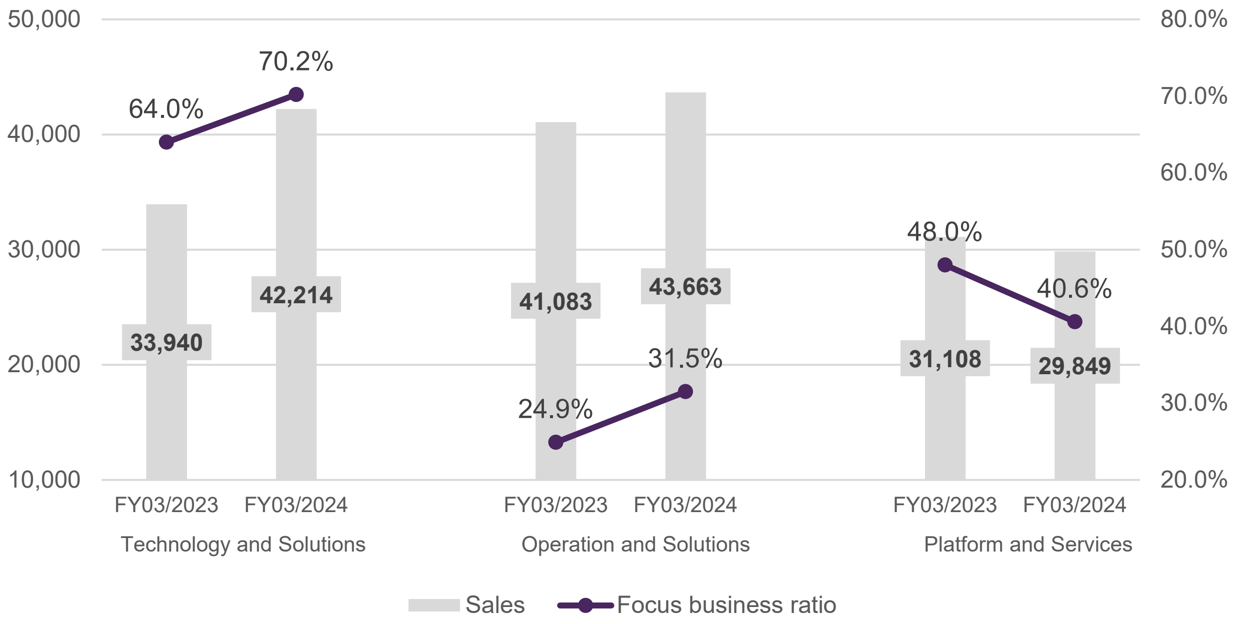
DTS has a strong solution for the housing industry called "Walk in Home," which is used by house manufacturers and is one of the top three solutions in terms of market share. The solution is seeing active applications in the housing domain. The plan is to upgrade the current package further to take it to the top position and eventually advance it into a model provided as SaaS.

DTS has been working on security in the zero-trust domain that spans the application and infrastructure layers. As the situation regarding the protection of personal information and responses to cyberattacks, etc., becomes an indicator of a company's reliability, DTS has been actively developing zero-trust solutions since 2022, seeing the security risks that are increasing due to changes in the way we work, including the widespread adoption of telework, as an opportunity.

■ Platform and Services segment

The Platform and Services segment defines its focus business area as one where they provide and expand the IT outsourcing services ReSM and ReSM plus. These services are related to AWS, Azure and ServiceNow, and they involve taking over operations centered on system design and construction, operation and maintenance, and business process design. In addition, strengthening and expanding sales of hybrid cloud, data management, etc., and promoting network integration businesses are also positioned as focus businesses to be promoted.

Figure 14: Net sales of focus businesses as a percentage of total net sales by segment (millions of yen)



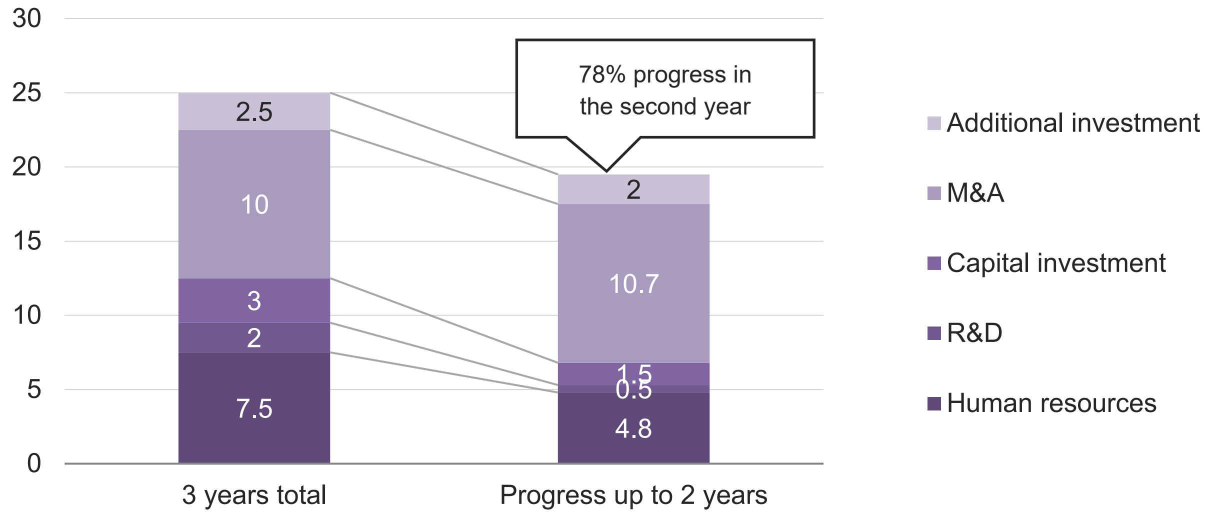
Source: Prepared by Global IR, Inc. based on company materials

The medium-term management plan set the focus businesses ratio targets for the Operation and Solutions, Technology and Solutions, and Platform and Services segments at 26%, 63%, and 32%, respectively. Each segment has achieved its targets ahead of schedule.

Growth investment

DTS is actively investing its ample cash reserves in growth investments, aiming to double its EBITDA margin and improve its ROE. The company has set aside 25 billion yen for growth investments over the three years of its medium-term management plan. The investment areas are classified as follows: human resources investment, which aims to strengthen the development and recruitment of highly skilled personnel; R&D investment, which invests in R&D in areas such as packaging, IoT, and AI, as well as in the development of security-related services; capital investment, which aims to achieve DX at BPO bases and internal back offices; M&A, which is related to the development of new businesses and overseas business areas; and additional investment, which is a reserve fund for further investment in each area.

Figure 15: Breakdown of growth investments in the medium-term management plan and progress in the fiscal year ended March 2024 (billion yen)



Source: Prepared by Global IR, Inc. based on company materials

As of the end of the second year of the medium-term management plan, which corresponds to the end of the fiscal year ended March 2024, the overall progress of investment was a strong 78%. In particular, in the area of human resources, where 4.8 billion yen was actually invested (a progress rate of 64%) compared to the planned 7.5 billion yen, the number of employees in Japan has risen, base pay and allowances were increased, and education and training was provided for the development of highly skilled personnel. It will likely take a certain amount of time following investment in human resources until its effects on management indicators can be observed. However, this is also directly linked to the productivity that DTS values. It is clear that the company is proceeding with its investment with resolve.

In addition, the company is also actively pursuing M&A, having already acquired shares in four companies, and has already achieved its target of 10.7 billion yen ahead of schedule. As discussed later, DTS recognizes that non-organic measures are essential for growth, proving that it is taking the initiative in critical areas.

Figure 16: Trends in investment in growth

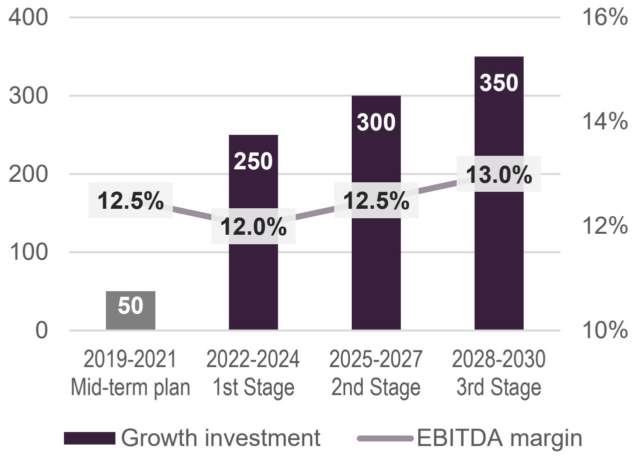
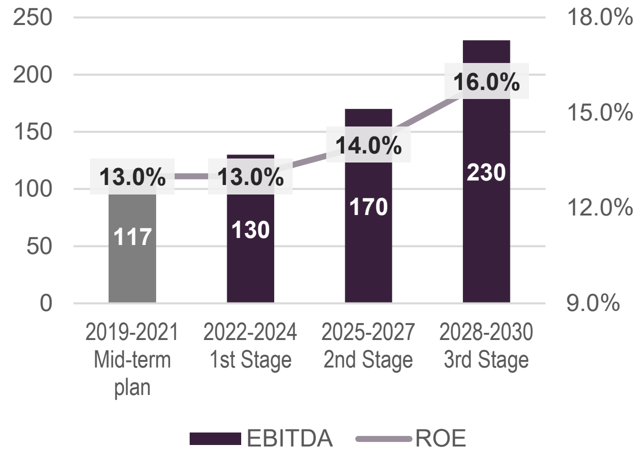


Figure 17: Trends in profits and ROE



Source: Prepared by Global IR, Inc. based on company materials

As a long-term outlook that goes beyond the medium-term management plan, DTS has divided the period up to fiscal 2030 into three stages of three years each. In the final three years, it plans to gradually expand the investment budget to reach 35 billion yen. In line with the significant increase in the investment budget, EBITDA margins will temporarily decline in the first stage, corresponding to the current medium-term management plan period. However, they are expected to exceed the level of the previous medium-term plan due to growth in human resources and expanded sales of solutions. In terms of EBITDA growth, the company aims to double the EBITDA of the previous medium-term plan period to 23 billion yen by 2030. In conjunction with this, the company targets a rise in ROE to 16%.

As can be seen, DTS is actively investing with a focus on capital efficiency indicators such as ROE and equity spread and is aggressively seeking the next pillar of growth without resting on the strength of its financial position.

M&A strategy

M&A is a major part of DTS's investment in growth. Like most SIers, DTS has expanded its business by forming groups both in Japan and overseas. However, the reality is that this is not just about increasing the number of staff but is also closely related to organic business development and building a customer base in each region.

Figure 18: Subsidiaries and affiliates

Trade name	Head office location	Established	Became group company	Investment ratio	Business segment
KYUSHU DTS CORPORATION	Fukuoka	Oct. 2000		100%	Operation and Solutions
JAPAN SYSTEMS ENGINEERING CORPORATION	Tokyo	Feb. 2005	Nov. 2006	100%	Operation and Solutions
DTS WEST CORPORATION	Osaka	Feb. 1979	Feb. 2007	100%	Operation and Solutions
MIRUCA CORPORATION	Tokyo	Apr. 2007		100%	Operation and Solutions
DTS (Shanghai) CORPORATION	Shanghai (China)	Oct. 2007		100%	Operation and Solutions
Dalian SuperElectronics Co., Ltd.	Dalian (China)	May 2004	Mar. 2019	51%	Operation and Solutions
Nelito Systems Private Limited	Navi Mumbai (India)	May 1995	Mar. 2017	98.8%	Operation and Solutions
DTS INSIGHT CORPORATION	Tokyo	Jun. 2001	Apr. 2014	100%	Technology and Solutions
Anshin Project Japan Inc.	Fukuoka	Mar. 1988	May 2023	100%	Technology and Solutions
DTS America Corporation	New York (USA)	Nov. 2011		100%	Technology and Solutions
Partners Information Technology, Inc.	Anaheim (USA)	Oct. 2011	Nov. 2022	51%	Technology and Solutions
DTS SOFTWARE VIETNAM CO., LTD.	Hanoi (Vietnam)	Apr. 2014		100%	Technology and Solutions
Digital Technologies Corporation	Tokyo	Oct. 2009	Oct. 2009	100%	Platform and Services
DTS palette Inc.	Tokyo	Oct. 2011		100%	Special subsidiary

Source: Prepared by Global IR, Inc. based on company materials

In the US, DTS America Corporation (DTS America) is developing business for Japanese financial institutions through its network of offices (on the West Coast, East Coast, and in the Mid-South). In order to continue its business in North America and expand its customer base to include manufacturers and other industries beyond financial institutions, DTS acquired Calance through an MA in 2023. Calance has a base in Anaheim on the West Coast, and has a dedicated team for solution implementation and maintenance. Its strengths include IT staffing and IT services with highly specialized skills in each field, and it can quickly search for and select personnel within the United States. There is a strong demand for bilingual SIers from Japanese companies, and half of Calance's clients are Japanese companies.

DTS America has been working in alliance with Calance as a strategic partner since 2017. In addition to responding to customer system construction, they have been working together on ERP and SAP implementation. One of Calance's distinctive service offerings is 24-hour operational support, which they provide as part of their BPO operations. During the daytime on weekdays, the team in Anaheim takes over, and when it is nighttime in the US, the team in Delhi, India, takes over. There is always a base in Japan for Japanese companies, so the aim is to demonstrate synergy effects, including collaboration with that base.

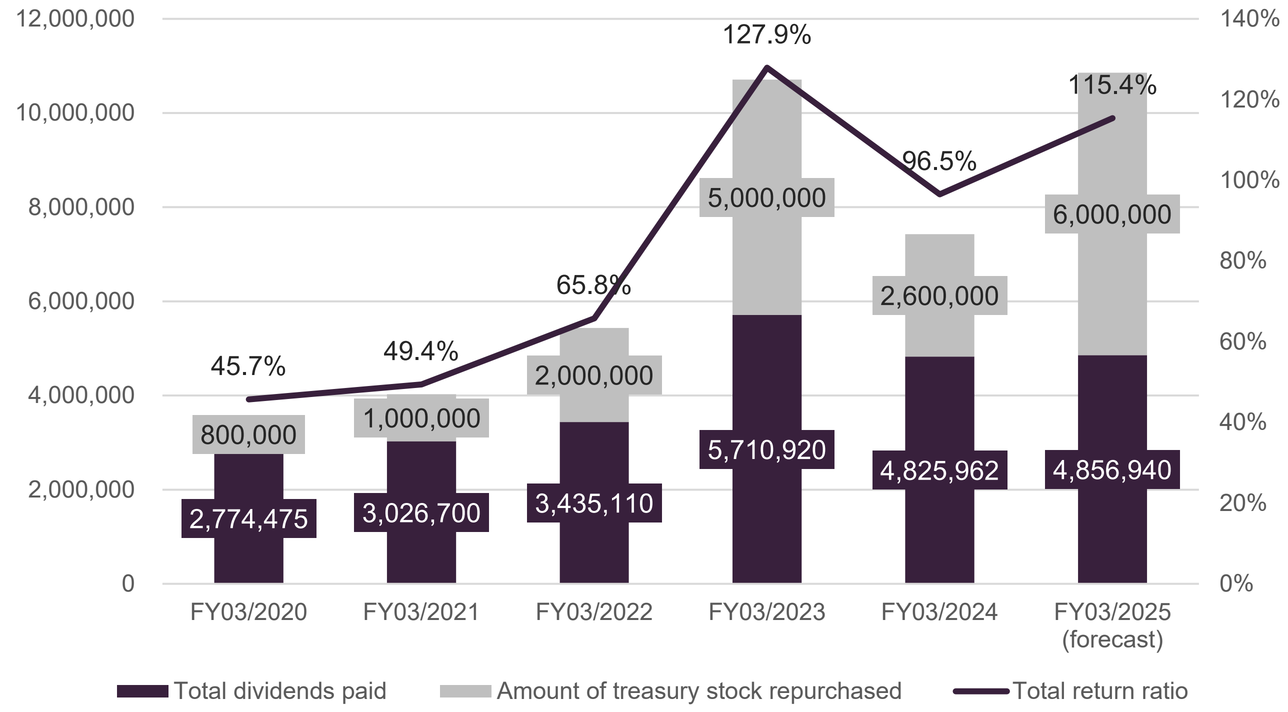
In this way, the DTS Group is actively pursuing M&A and other methods to supplement areas where it lacks in-house expertise. There is a fast-growing need for nearshore development, where large-scale projects are outsourced to and developed in regional areas, and it appears that the company is considering M&A to supplement this area. In addition, to become a resilient company during economic downturns with stable business performance, the company is promoting the incorporation of public sector businesses into its business portfolio through M&A. In terms of becoming a company resistant to economic downturns, the company aims to stabilize its overall business by strengthening its financial, public, and other corporate sectors in a well-balanced manner.

In Japan, the company made Anshin Project Japan Inc. a subsidiary in 2023. Anshin Project Japan Inc. distributes 3D CAD software for the construction and housing industries. This has enabled the group to promote solutions specialized for the housing construction industry, from development to provision to first users, and is a strength that can be more easily showcased to external parties. DTS also has a wide range of versatile services, such as cloud-related services and security. It has the potential to build a distinctive position for itself in the SIer industry, where it is often difficult to distinguish one company from another, by independently refining its service offerings to give it an edge in specific industries.

Shareholder Returns

In its medium-term management plan, DTS has formulated a cash allocation plan that indicates how it will allocate capital to generate cash from its business, invest in growth, and return profits to shareholders. Over the three years, the company expects to generate 35 billion yen in cash from its business and have 45 billion yen cash on hand. It plans to invest 25 billion yen in growth and return 20 billion yen to shareholders. As a result, the company aims to reduce its cash on hand to 35 billion yen, or 40% of its total assets. It is making steady progress towards this goal, with the figure at the end of March 2024 standing at 44%. Under Vision2030, the company aims to further reduce its cash on hand to 30% of its total assets.

Figure 19: Shareholder returns



Source: Prepared by Global IR, Inc. based on company materials

In addition to returning profits to shareholders, the company has also set targets for ROE, maximum investments, dividend payout ratios, and total return ratios, which shows that the company is also mindful of capital efficiency in its management.

ESG and other initiatives to strengthen the management base

Lastly, let's touch on the ESG management being promoted by DTS. As a group, DTS is strengthening its ESG initiatives to realize carbon neutrality and contribute to achieving a sustainable society. DTS's ESG initiatives are being promoted under three pillars: "promote efforts for the environment," "promote employee engagement and diversity," and "enhance governance and information disclosures." KPIs have been set for each pillar. In addition, in order to promote employee challenges and accelerate management decisions, the company is promoting reform of its management foundation through the renewal of business processes and the use of cutting-edge technology.

Figure 20: ESG management initiatives and progress

ESG management

Scope of Activities	KPIs and Key Points in the Medium-Term Plan	Status of achievement for the fiscal year ended March 2024
Environment **Promoting environmental initiatives**	• Promotion of decarbonization management, including procurement of renewable energy • Expansion and promotion of projects that are conscious of the SDGs • Establishment of a Sustainability Committee to accelerate discussion and response - CO_2 emissions reduction: 50% or more compared to FY2013 - SDGs-related sales: 40% or more	• CO_2 emissions reduction: **49.6%** • SDGs-related sales: **41.7% (Achieved)**
Society **Employee Engagement and Diversity Improvement**	• Creating a comfortable working environment where a diverse range of people can thrive • Strategic development of management talent • Regular implementation, analysis and response to employee engagement surveys - Ratio of female managers: 6% or more	• Ratio of women in managerial positions: **5.1%**
Governance **Strengthening governance and information disclosure**	• Transition to a company with an audit and supervisory committee • Improvement of the independence and diversity of the Board of Directors • Enhancement of non-financial information and continuous improvement of business performance disclosure - Ratio of female directors: 10% or more - Ratio of independent outside directors: majority	• Ratio of female directors: **18.2% (Achieved)** • Ratio of outside directors: **54.5% (Achieved)**

Source: Prepared by Global IR, Inc. based on company materials

In April 2022, the DTS Group established a new Sustainability Committee to further strengthen its environmental and social initiatives. The committee is responsible for promoting group-wide initiatives related to sustainability issues, such as the SDGs and climate change. It is also responsible for identifying climate-related risks and opportunities, planning initiatives, and reporting on evaluations to the Board of Directors.

As part of its measures to strengthen its management base, the company has also established and is implementing policies regarding the development of systems and initiatives to promote dialogue with shareholders (shareholder relations: SR). These policies include holding quarterly financial results briefings for analysts and institutional investors; attending briefings for individual investors; regularly reporting the opinions and requests of shareholders to the board of directors to help with management decisions; formulation of the Rules Relating to the Management of Insider Trading; conducting surveys of substantial shareholders; and the creation and provision of documents in English as appropriate in order to improve dialogue with non-Japanese shareholders.

In this way, by actively promoting SR in addition to IR during the current medium-term plan, DTS has established highly transparent management, has continued to improve corporate value, and has built relationships of trust with stakeholders.

Management Indicators

Financial Data (consolidated: quarterly) (millions of yen)

Accounting period	FY 03/2021 Q1-Q4	FY 03/2022 Q1-Q4	FY 03/2023 Q1-Q4	FY 03/2024 Q1	Q2	H1	Q3	Q4	Q1-Q4
Operating revenue	90,493	94,452	106,132	26,689	30,050	56,739	27,932	31,056	115,727
YoY (%)	95.6	103.3	110.0	108.4	118.7	113.6	109.1	101.5	109.0
Profit before tax	11,100	11,384	11,637	2,710	3,410	6,120	3,664	1807	11,592
YoY(%)	103.0	102.6	102.2	130.9	119.6	124.4	117.6	50.2	99.6
Profit before tax margin (%)	12.3	12.1	11.0	10.2	113.5	10.7	13.1	9.5	10.0
Profit attributable to owners of parent	7,630	7,837	8,005	1,873	2,315	4,188	2,482	689	7,293
YoY (%)	104.3	102.7	102.1	134.2	122.0	127.1	117.7	26.8	91.2
Profit margin (%)	8.4	8.3	7.5	7.0	7.7	7.4	8.9	2.2	6.3

Source: Prepared by Global IR, Inc. based on company securities reports and company IR materials.

Per Share Data (Consolidated)

Accounting period	FY 03/2018	FY 03/2019	FY 03/2020	FY 03/2021	FY 03/2022	FY 03/2023	FY 03/2024
Total number of shares issued and outstanding (thousand shares)	25,222	25,222	50,445	50,445	49,073	47,591	46,854
EPS	247.90	292.21	158.01	165.49	172.78	181.41	168.51
EPS Adjusted	-	-	-	-	-	-	-
BPS	2003.23	2203.22	1190.71	1293.61	1376.05	1408.81	1451.61
DPS	80.00	95.00	55.00	60.00	70.00	120.00	103.00

Source: Prepared by Global IR, Inc. based on company securities reports and company IR materials.

Cash Flows (millions of yen)

Accounting period	FY 03/2018	FY 03/2019	FY 03/2020	FY 03/2021	FY 03/2022	FY 03/2023	FY 03/2024
Depreciation and amortization	421	474	473	535	532	608	628
Cash flows from operating activities	6,761	6,947	7,551	9,459	7,589	7,642	10,410
Cash flows from investing activities	-1,806	-1,770	-1,360	-787	-139	-931	-8,516
Cash flows from financing activities	-2,967	-2,477	-3,047	-3,848	-5,025	-9,095	-7,817

Source: Prepared by Global IR, Inc. based on company securities reports and company IR materials.

Financial Data (%)

Accounting period	FY 03/2018	FY 03/2019	FY 03/2020	FY 03/2021	FY 03/2022	FY 03/2023	FY 03/2024
Return on Assets (ROA)	10.4	11.7	10.4	10.1	9.9	9.9	8.8
Return on Equity (ROE)	12.9	13.9	13.8	13.3	13.0	13.0	11.8
Equity-to-asset ratio	76.5	76.7	78.0	78.8	78.4	76.1	73.4

Source: Prepared by Global IR, Inc. based on company securities reports and company IR materials.

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