

Summary of Consolidated Financial Results
for the Second Quarter of the Fiscal Year Ending March 31, 2021
(Six Months Ended September 30, 2020)

[Japanese GAAP]

Company name: MKSystem Corporation

Listing: Tokyo Stock Exchange (JASDAQ)

Stock code: 3910

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Scheduled date of filing of Quarterly Report:

November 6, 2020

Scheduled date of payment of dividend:

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Preparation of supplementary materials for quarterly financial results: Yes

Holding of quarterly financial results meeting:

Yes (A video will be uploaded as a substitute)

(All amounts are rounded down to the nearest million yen)

1. Consolidated Financial Results for the Second Quarter Ended September 30, 2020

(April 1, 2020 – September 30, 2020)

(1) Consolidated operating results

(Percentages represent year-on-year changes)

	Net sales		Operating profit		Ordinary profit		Profit attributable to owners of parent	
	Million yen	%	Million yen	%	Million yen	%	Million yen	%
Six months ended Sep. 30, 2020	1,128	(4.7)	75	(52.6)	83	(47.8)	40	(59.6)
Six months ended Sep. 30, 2019	1,183	25.0	160	103.5	159	106.2	101	-

Note: Comprehensive income (million yen)

Six months ended Sep. 30, 2020: 38 (down 60.4%)

Six months ended Sep. 30, 2019: 97 (-%)

	Basic earnings per share	Diluted earnings per share
	Yen	Yen
Six months ended Sep. 30, 2020	7.55	-
Six months ended Sep. 30, 2019	18.70	-

(2) Consolidated financial position

	Total assets	Net assets	Equity ratio
	Million yen	Million yen	%
As of Sep. 30, 2020	2,214	1,299	57.3
As of Mar. 31, 2020	2,234	1,304	56.8

Reference: Shareholders' equity (million yen)

As of Sep. 30, 2020: 1,267

As of Mar. 31, 2020:

1,270

2. Dividends

	Dividend per share				
	1Q-end	2Q-end	3Q-end	Year-end	Total
	Yen	Yen	Yen	Yen	Yen
Fiscal year ended Mar. 31, 2020	-	0.00	-	8.00	8.00
Fiscal year ending Mar. 31, 2021	-	0.00			
Fiscal year ending Mar. 31, 2021 (forecast)			0.00	8.00	8.00

Note: Revisions to the most recently announced dividend forecast: None

3. Consolidated Earnings Forecasts for the Fiscal Year Ending March 31, 2021 (April 1, 2020 – March 31, 2021)

(Percentages represent year-on-year changes)

	Net sales		Operating profit		Ordinary profit		Profit attributable to owners of parent		Basic earnings per share
	Million yen	%	Million yen	%	Million yen	%	Million yen	%	Yen
Full year	2,749	15.5	324	3.2	322	3.1	201	2.1	37.08

Note: Revisions to the most recently announced earnings forecasts: None

*** Notes**

(1) Changes in significant subsidiaries during the period (changes in scope of consolidation): None

(2) Application of special accounting methods for presenting quarterly consolidated financial statements: None

(3) Changes in accounting policies and accounting-based estimates, and restatements

1) Changes in accounting policies due to revisions in accounting standards, others: None

2) Changes in accounting policies other than 1) above: None

3) Changes in accounting-based estimates: None

4) Restatements: None

(4) Number of issued shares (common stock)

1) Number of shares issued at the end of period (including treasury shares)

As of Sep. 30, 2020:	5,428,000 shares	As of Mar. 31, 2020:	5,428,000 shares
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2) Number of treasury shares at the end of period

As of Sep. 30, 2020:	506 shares	As of Mar. 31, 2020:	474 shares
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3) Average number of shares during the period

Six months ended Sep. 30, 2020:	5,427,516 shares	Six months ended Sep. 30, 2019:	5,427,642 shares
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* This quarterly financial report is not subject to quarterly review by certified public accountants or auditing firms.

* Explanation of appropriate use of earnings forecasts, and other special items

Forecasts of future performance in this report are based on assumptions judged to be valid and information available to the MKSystem's management at the time the materials were prepared but are not promises by MKSystem regarding future performance. Actual results may differ significantly from these forecasts for a number of reasons. Please refer to "1. Qualitative Information on Quarterly Consolidated Financial Performance, (3) Explanation of Consolidated Earnings Forecasts and Other Forward-looking Statements" on page 5 for forecast assumptions and notes of caution for usage.

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1. Qualitative Information on Quarterly Consolidated Financial Performance

(1) Explanation of Results of Operations

During the first half of the fiscal year ending March 31, 2021 (hereinafter “the period under review”), the Japanese economy continued to face a severe situation under the influence of the spread of the novel coronavirus disease (COVID-19) infection. While economic activity slowly picked up and economic indicators showed trends towards improvement after the lifting of the state of emergency in May, there was no sign of the end of the pandemic. Under such environment, it is concerned that economic activity is expected to remain restrained for an extended period of time.

The information service industries in Japan have been seeing an accelerated transition to DX (Digital Transformation) that flexibly transforms the way of business and life by adopting digital technology, whereas some conservative stance is viewed recently such as postponing or restraining IT investments due to the economic downturn. In the field of the personnel and labor management, which MKSystem Corporation (hereinafter the “Company”) and its group companies (hereinafter collectively the “Group”) are involved, some corporations and local governments readjust or postpone their investment plans despite a rapid transition to teleworking due to the work-style reform promoted by the central government as well as the spread of the COVID-19 infection.

Under these circumstances, the Group worked to help our customers to improve operational efficiency and increase added value, as well as to further enhance our customers’ satisfaction. The “Shalom” series, our mainstay service, are the systems that support the business processes associated primarily with social insurance and labor insurance, and have been introduced broadly by more than 2,500 labor and social security attorney offices. In addition, the Group strengthened marketing activities to expand sales for “Company Edition” series designed for general corporation customers, “eNEN (renamed from Nenmatsu-chosei CuBe Cloud),” a year-end tax adjustment tool, as well as “Cloud Pocket,” which was newly released in July 2020. In the CuBe Business, we worked to expand our business by enhancing the service functions of “GooooN” and strengthening marketing activities to expand sales channels.

During the period under review, the Company relocated its Tokyo office. The new office site has not only the Company’s Tokyo office but also the offices of our consolidated subsidiary, partner companies and other affiliated organizations, which relocated at the same time, in order to work more closely and aim for streamlining the operations. As a result of the relocation, the Company reported rental income of 7 million yen from the partner companies and other affiliated organizations as non-operating income.

As a result, the Group reported net sales for the period under review of 1,128 million yen (down 4.7% year on year), cost of sales of 566 million yen (down 3.1%), the ratio of cost of sales to net sales of 50.2% (up 0.8 percentage points), gross profit of 561 million yen (down 6.3%), operating profit of 75 million yen (down 52.6%), the ratio of operating profit to net sales of 6.7% (down 6.8 percentage points), ordinary profit of 83 million yen (down 47.8%), and profit attributable to owners of parent of 40 million yen (down 59.6%). In addition, the return on equity (ROE), one of the KPIs for the Group, was 5.4% (compared with 10.8% for the same period of the previous fiscal year) on a non-consolidated basis and 3.2% (compared with 8.9% for the same period of the previous fiscal year) on a consolidated basis.

Results by business segment were as follows.

The Shalom Business

A growing number of companies as well as labor and social security attorney offices, our main customers, are motivated to introduce relevant systems from an increasing need for operational efficiency for the work-style reforms including teleworking. At the same time, we expect an intensified competition and pricing pressure as we witness an active entries in the market.

For the period under review, labor and social security attorneys were busy providing advice on the utilization of the treatments for their corporate clients that comply with the government’s requests to suspend operations, such as compensation for absence from work and subsidies for employment adjustment. In the general corporate market, we experienced delays in negotiations and installations because our customers in personnel divisions and in decision-making positions were on a tight schedule. Furthermore, our in-person sales activities were mostly

restricted. This is mainly because Human Capital 2020—a professional event on HR-related solutions at which we have exhibited every year and received many inquiries—was cancelled due to the spread of the COVID-19 infections and also because we were forced to call off the Company-sponsored seminars that were to be held at physical venues.

Under such circumstances, we have strengthened web-based promotional activities by holding follow-up meetings for the Shalom brand products and various seminars online. In addition, we have enhanced the service functions of “DirectHR,” which we released in the previous fiscal year as a new solution for small- and medium-sized companies, as well as “eNEN (renamed from Nenmatsu-chosei CuBe Cloud),” which was acquired by the Company from Business Net Corporation Co., Ltd. (hereinafter “BNC”), a consolidated subsidiary, through the business transfer.

As a result, sales of the cloud services, which consist of ASP services and system construction services, were 871 million yen (up 6.6% year on year). Specifically, sales of ASP services amounted to 799 million yen (up 12.9%) due to increased use by general corporations as well as accumulated monthly usage fees in line with an increase in the number of customers who use our main services of Shalom brand products. However, sales of system construction services decreased to 72 million yen (down 34.0%) due to the slower-than-expected progress of orders received for Shalom House Plan and new installation by general corporations, which was impacted by curtailed sales activities. In addition, sales of system products also decreased to 46 million yen (down 18.1%), affected by a trend of customers transitioning to telework.

Cost of sales increased year on year due mainly to increases in labor cost and software amortization expenses. This is primarily as a result of the following two transactions entered into in the previous fiscal year between the Company and BNC: succession of BNC’s system development business at Matsuyama Development Center through a company split and acquisition of BNC’s “eNEN (renamed from Nenmatsu-chosei CuBe Cloud)” business.

Consequently, the segment recorded net sales of 934 million yen (up 6.9% year on year), gross profit of 503 million yen (down 2.6%) and operating profit of 104 million yen (down 46.9%). The ratio of operating profit to net sales, one of the KPIs for the Group, was 11.2% (down 11.3 percentage points).

The CuBe Business

We have been engaged in the contracted development of front-end systems, customized to needs of an individual company, for the personnel and general affairs divisions of large companies to improve their business processes. The CuBe Business also provides cloud services that bring the convenience to small- and medium-sized companies by leveraging our know-how gained through the contracted development of systems for large companies.

In the previous fiscal year, the “eNEN (renamed from Nenmatsu-chosei CuBe Cloud)” business was transferred by BNC to its parent company, MKSystem Corporation.

Particularly in the contracted development of front-end systems, the influence of the spread of the COVID-19 infections resulted in delays in negotiations and installations because our customers in corporations and local governments, who are in charge of the installation and in decision-making positions, were making the transition to working from home and on a tight schedule. In the cloud service business, on the other hand, we have developed new sales channels for and enhanced the service functions of “GooooN.”

As a result, the segment recorded net sales of 215 million yen (down 31.1% year on year), gross profit of 57 million yen (down 31.5%), and operating loss of 37 million yen (compared with operating loss of 35 million yen for the same quarter of the previous fiscal year). Operating loss of the CuBe Business reflects amortization of goodwill of 19 million yen.

(2) Explanation of Financial Position

Cash Flows

The balance of cash and cash equivalents (hereinafter “net cash”) at the end of the period under review decreased 137 million yen from the end of the previous fiscal year to 585 million yen. The details of cash flows for the period under review from each activity and the major components of changes are as follows.

Cash flows from operating activities

Net cash provided by operating activities was 77 million yen (compared with net cash provided of 345 million yen for the same period of the previous fiscal year). Major positive factors include depreciation of 154 million yen and profit before income taxes of 82 million yen, while major negative factors include a 91 million yen decrease in accrued consumption taxes and income taxes paid of 71 million yen.

Cash flows from investing activities

Net cash used in investing activities was 276 million yen (compared with net cash used of 78 million yen for the same period of the previous fiscal year). Major negative factors include purchase of property, plant and equipment of 181 million yen and purchase of intangible assets of 95 million yen.

Cash flows from financing activities

Net cash provided by financing activities was 62 million yen (compared with net cash used of 67 million yen for the same period of the previous fiscal year). Major positive factors include proceeds from long-term borrowings of 200 million yen, while major negative factors include repayments of long-term borrowings of 94 million yen and dividends paid of 43 million yen.

The Group’s demand for working capital includes consideration and funds needed to pay tax obligations that are accounted for as cost of sales and selling, general and administrative expenses whereas its capital expenditures represent major investments in equipment for purposes such as increasing the capacity of servers. In addition, the Group pays dividends and other distributions to shareholders based on our dividend policy while maintaining a sound financial position.

The Group’s working capital, funds for capital investments, and dividends and other distributions to shareholders are primarily covered by internally generated funds derived from operating cash flows as well as by loans from financial institutions.

We believe the Group is capable of procuring funds to increase liquidity on hand as well as funds for specific investments for the future business growth with its sound financial position and capability of consistently generating operating cash flows.

The balance of interest-bearing debt at the end of the period under review was 612 million yen. The balance of cash and cash equivalents at the end of the period under review was 585 million yen.

Assets, Liabilities and Net Assets

Assets

The balance of current assets at the end of the period under review was 1,073 million yen (down 10.3% from the end of the previous fiscal year), consisting primarily of 612 million yen in cash and deposits, and 406 million yen in accounts receivable-trade.

The balance of non-current assets was 1,141 million yen (up 9.9% from the end of the previous fiscal year), consisting primarily of 428 million yen in software, 233 million yen in goodwill, 180 million yen in guarantee deposits, and 141 million yen in buildings.

As a result, the balance of total assets was 2,214 million yen (down 0.9% from the end of the previous fiscal year).

Liabilities

The balance of current liabilities at the end of the period under review was 545 million yen (down 9.1% from the end of the previous fiscal year), consisting primarily of 233 million yen in current portion of long-term borrowings, 80 million yen in accounts payable-other, and 60 million yen in provision for bonuses.

The balance of non-current liabilities was 369 million yen (up 11.8% from the end of the previous fiscal year), consisting solely of 369 million yen in long-term borrowings.

As a result, the balance of total liabilities was 914 million yen (down 1.7% from the end of the previous fiscal year).

Net assets

The balance of shareholders' equity at the end of the period under review was 1,267 million yen (down 0.2% from the end of the previous fiscal year), consisting primarily of 219 million yen in share capital, 197 million yen in capital surplus, and 851 million yen in retained earnings.

As a result, the balance of net assets was 1,299 million yen (down 0.4% from the end of the previous fiscal year).

(3) Explanation of Consolidated Earnings Forecasts and Other Forward-looking Statements

There are no revisions to the consolidated earnings forecast for the fiscal year ending March 31, 2021, which was announced in the "Summary of Consolidated Financial Results for the Fiscal Year Ended March 31, 2020 (Japanese GAAP)" on May 11, 2020.

2. Quarterly Consolidated Financial Statements and Notes**(1) Quarterly Consolidated Balance Sheet**

	(Thousands of yen)	
	FY3/20 (As of Mar. 31, 2020)	Second quarter of FY3/21 (As of Sep. 30, 2020)
Assets		
Current assets		
Cash and deposits	749,960	612,677
Accounts receivable-trade	420,149	406,787
Merchandise	5,904	7,207
Work in process	1,451	15,042
Supplies	173	108
Prepaid expenses	17,623	27,940
Consumption taxes receivable	-	123
Other	1,004	3,258
Total current assets	1,196,267	1,073,146
Non-current assets		
Property, plant and equipment		
Buildings, net	18,455	141,152
Vehicles, net	2,608	2,173
Tools, furniture and fixtures, net	41,623	86,490
Total property, plant and equipment	62,688	229,816
Intangible assets		
Software	476,781	428,600
Software in progress	29,507	33,918
Trademark right	1,535	1,432
Telephone subscription right	1,218	1,218
Goodwill	252,602	233,171
Total intangible assets	761,646	698,341
Investments and other assets		
Investments in capital	70	60
Guarantee deposits	180,890	180,855
Deferred tax assets	33,078	32,051
Other	98	98
Total investments and other assets	214,137	213,065
Total non-current assets	1,038,471	1,141,223
Total assets	2,234,739	2,214,369

(Thousands of yen)

	FY3/20 (As of Mar. 31, 2020)	Second quarter of FY3/21 (As of Sep. 30, 2020)
Liabilities		
Current liabilities		
Accounts payable-trade	27,019	16,551
Short-term borrowings	10,000	10,000
Current portion of long-term borrowings	166,644	233,304
Accounts payable-other	91,235	80,881
Accrued expenses	32,347	37,982
Income taxes payable	81,720	46,747
Accrued consumption taxes	94,545	3,644
Advances received	33,341	48,240
Provision for bonuses	55,634	60,049
Other	7,099	7,638
Total current liabilities	599,588	545,039
Non-current liabilities		
Long-term borrowings	330,595	369,503
Total non-current liabilities	330,595	369,503
Total liabilities	930,183	914,542
Net assets		
Shareholders' equity		
Share capital	219,110	219,110
Capital surplus	197,457	197,457
Retained earnings	854,151	851,842
Treasury shares	(466)	(499)
Total shareholders' equity	1,270,251	1,267,909
Non-controlling interests	34,303	31,917
Total net assets	1,304,555	1,299,827
Total liabilities and net assets	2,234,739	2,214,369

(2) Quarterly Consolidated Statements of Income and Comprehensive Income**Quarterly Consolidated Statement of Income
(For the Six-month Period)**

	(Thousands of yen)	
	First six months of FY3/20 (Apr. 1, 2019 – Sep. 30, 2019)	First six months of FY3/21 (Apr. 1, 2020 – Sep. 30, 2020)
Net sales	1,183,640	1,128,029
Cost of sales	583,947	566,043
Gross profit	599,692	561,985
Selling, general and administrative expenses	439,433	486,041
Operating profit	160,259	75,944
Non-operating income		
Interest income	2	3
Dividend income	1	1
Royalty income	-	300
Rental income	-	7,035
Subsidy income	-	1,056
Surrender value of insurance policies	21	25
Purchase discounts	5	190
Interest on tax refund	358	-
Other	49	69
Total non-operating income	439	8,681
Non-operating expenses		
Interest expenses	1,267	1,333
Other	1	0
Total non-operating expenses	1,269	1,334
Ordinary profit	159,429	83,291
Extraordinary losses		
Loss on retirement of property, plant and equipment	-	700
Total extraordinary losses	-	700
Profit before income taxes	159,429	82,591
Income taxes-current	33,716	42,842
Income taxes-deferred	27,984	1,026
Total income taxes	61,700	43,868
Profit	97,728	38,723
Loss attributable to non-controlling interests	(3,756)	(2,253)
Profit attributable to owners of parent	101,485	40,976

Quarterly Consolidated Statement of Comprehensive Income
(For the Six-month Period)

	(Thousands of yen)	
	First six months of FY3/20 (Apr. 1, 2019 – Sep. 30, 2019)	First six months of FY3/21 (Apr. 1, 2020 – Sep. 30, 2020)
Profit	97,728	38,723
Comprehensive income	97,728	38,723
Comprehensive income attributable to		
Comprehensive income attributable to owners of parent	101,485	40,976
Comprehensive income attributable to non-controlling interests	(3,756)	(2,253)

(3) Quarterly Consolidated Statement of Cash Flows

(Thousands of yen)

	First six months of FY3/20 (Apr. 1, 2019 – Sep. 30, 2019)	First six months of FY3/21 (Apr. 1, 2020 – Sep. 30, 2020)
Cash flows from operating activities		
Profit before income taxes	159,429	82,591
Depreciation	127,873	154,392
Amortization of goodwill	19,430	19,430
Increase (decrease) in provision for loss on order received	(10,367)	-
Increase (decrease) in provision for bonuses	4,278	4,415
Interest and dividend income	(3)	(4)
Interest expenses	1,267	1,333
Decrease (increase) in trade receivables	(72,261)	13,362
Decrease (increase) in inventories	32,986	(14,828)
Increase (decrease) in trade payables	(277)	(10,467)
Increase (decrease) in accrued consumption taxes	84,739	(91,025)
Increase (decrease) in accounts payable-other	(20,764)	(11,145)
Other, net	18,930	2,674
Subtotal	345,262	150,728
Interest and dividends received	2	3
Interest paid	(1,267)	(1,333)
Income taxes (paid) refund	1,762	(71,987)
Net cash provided by (used in) operating activities	345,758	77,411
Cash flows from investing activities		
Purchase of property, plant and equipment	(2,838)	(181,068)
Purchase of intangible assets	(85,354)	(95,786)
Proceeds from divestments	-	10
Payments of leasehold and guarantee deposits	(1,431)	-
Proceeds from refund of leasehold and guarantee deposits	10,981	35
Net cash provided by (used in) investing activities	(78,643)	(276,810)
Cash flows from financing activities		
Net increase (decrease) in short-term borrowings	(10,000)	-
Proceeds from long-term borrowings	100,000	200,000
Repayments of long-term borrowings	(102,906)	(94,432)
Payments from changes in ownership interests in subsidiaries that do not result in change in scope of consolidation	(10,839)	-
Purchase of treasury shares	(109)	(32)
Dividends paid	(43,421)	(43,420)
Net cash provided by (used in) financing activities	(67,276)	62,115
Net increase (decrease) in cash and cash equivalents	199,839	(137,283)
Cash and cash equivalents at beginning of period	299,755	722,818
Cash and cash equivalents at end of period	499,595	585,534

(4) Notes to Quarterly Consolidated Financial Statements**Going Concern Assumption**

Not applicable.

Significant Changes in Shareholders' Equity

Not applicable.

Segment Information

First six months of FY3/20 (Apr. 1, 2019 – Sep. 30, 2019)

Information related to net sales and profit/loss for each reportable segment

	Shalom Business	CuBe Business	Total	Adjustment (Note)	(Thousands of yen) Amounts recorded in quarterly consolidated statement of income
Net sales					
External sales	874,318	309,322	1,183,640	-	1,183,640
Inter-segment sales and transfers	276	3,852	4,128	(4,128)	-
Total	874,594	313,174	1,187,768	(4,128)	1,183,640
Segment profit (loss)	196,384	(35,908)	160,476	(216)	160,259

Notes: 1. The adjustment to segment profit (loss) is the elimination of inter-segment transactions.

2. Segment profit (loss) is adjusted to be consistent with operating profit presented on the quarterly consolidated statement of income.

First six months of FY3/21 (Apr. 1, 2020 – Sep. 30, 2020)

Information related to net sales and profit/loss for each reportable segment

	Shalom Business	CuBe Business	Total	Adjustment (Note)	(Thousands of yen) Amounts recorded in quarterly consolidated statement of income
Net sales					
External sales	917,304	210,725	1,128,029	-	1,128,029
Inter-segment sales and transfers	17,466	5,062	22,528	(22,528)	-
Total	934,770	215,788	1,150,558	(22,528)	1,128,029
Segment profit (loss)	104,356	(37,685)	66,670	9,274	75,944

Notes: 1. The adjustment to segment profit (loss) is the elimination of inter-segment transactions.

2. Segment profit (loss) is adjusted to be consistent with operating profit presented on the quarterly consolidated statement of income.

Additional Information

The impact of the spread of the COVID-19 infections

As impacted by the spread of the COVID-19 infections, the economic outlook has become increasingly uncertain. The Group has seen the apparent impact of the pandemic, including delays in negotiations and cancellations of seminars at physical venues. However, the majority of the Group's sales is comprised of the monthly license fee for the "Shalom" series, our mainstay service, which continues to provide a highly stable revenue stream. Therefore, we have decided that currently there have been no events that significantly affect the accounting-based estimates, including recoverability of deferred tax assets.

The estimates are based mainly on the information currently available to the Group and subject to significant uncertainty. In case the impact changes according to how long the COVID-19 pandemic lingers and how the situation develops, there may be effects on the estimates, which may affect the financial position and results of operations for the following fiscal years.

This financial report is solely a translation of MKSystem's Kessan Tanshin (including attachments) in Japanese, which has been prepared in accordance with accounting principles and practices generally accepted in Japan, for the convenience of readers who prefer an English translation.