



Medical System Network / 4350

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How to read a Shared Research report: This report begins with the trends and outlook section, which discusses the company's most recent earnings. First-time readers should start at the business section later in the report.

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Executive summary

Business overview

- Medical System Network operates the Nanohana Pharmacy chain. It also provides a wide range of pharmacy management support services (from pharmaceuticals procurement to pharmacist training) to dispensing pharmacies and medical institutions including directly operated pharmacies and non-group affiliates that register to become members of the company's network. The core of these services is the one-stop supply chain management service that comprises price negotiations with drug wholesalers, drug ordering, and settlement of bills. Medical System Network receives commissions from its network members based on the amount of drug orders they place. As of end-FY03/21, there were 6,116 network members (+871 from end-FY03/19) comprising 416 directly operated pharmacies and 5,700 affiliates. The company has reorganized its business segments in FY03/20, moving the Pharmaceuticals Network and Dispensing Pharmacy businesses, as well as the manufacture and market pharmaceuticals business previously included in the Other business, under the Community Pharmacy Network segment. The Leasing and Facility-related business and the Food Service business are unchanged. In the Other business, since the manufacture and market pharmaceuticals business is transferred out, the main business comprises home-visit nursing care.
- Nanohana Pharmacies, the company's directly operated pharmacies, are generally located near large medical institutions or in medical malls or complexes that integrate multiple clinics and hospitals. According to the Ministry of Health, Labour and Welfare, there were 60,171 dispensing pharmacies in Japan at end-March 2019, but the market is highly fragmented; the top 10 pharmacies with nationwide chains, including Medical System Network with 0.7% share of pharmacies, have a combined market share of less than 10%. Because mid-tier regional chains with roots in local communities and small, family-owned pharmacies account for 90% of the domestic market, the primary growth strategy of major pharmacy chains is opening new pharmacies and expanding through M&A. Through this increase in affiliates to the Pharmaceuticals Network, the number of network members as of end-March 2021 had exceeded 10% of the market share.
- In FY03/21, Community Pharmacy Network accounted for 95.2% of sales, Leasing and Facility-related 2.2%, Food Service 2.4%, and Other 0.2%. The Community Pharmacy Network segment is a new segment following a segment change in FY03/20 that initially combined the former Pharmaceuticals Network and Dispensing Pharmacy segments with manufacture and market pharmaceuticals business (previously part of Other segment), but the digital shift business was added from FY03/21. The Community Pharmacy Network segment comprises the Pharmaceuticals Network, Dispensing Pharmacy, and manufacture and market pharmaceuticals, and digital shift businesses. The company discloses operating status of each business under the Community Pharmacy Network segment, but does not provide a sales and profit breakdown by business.

Trends and outlook

- FY03/21 results: For FY03/21, the company reported full-year consolidated sales of JPY104.3bn (-0.9% YoY), operating profit of JPY3.4bn (+112.3% YoY), recurring profit of JPY3.5bn (+123.0% YoY), and net income attributable to owners of the parent of JPY2.2bn (versus loss of JPY895mn in FY03/20). Performance was strong at the mainstay Community Pharmacy Network segment's Pharmaceuticals Network business, and while the Dispensing Pharmacy business filled fewer prescriptions because of the COVID-19 pandemic, it benefited from efficiency gains. As a consequence, operating profit was 2.1x the prior-year figure. The company also turned into the black at the net income level, thanks in part to JPY907mn in proceeds from the sale of shares in a non-equity-method affiliate, booked as an extraordinary gain.
- Full-year FY03/22 forecast: The company forecast calls for full-year consolidated sales of JPY105.7bn (+1.4% YoY), EBITDA of JPY6.5bn (+1.2% YoY), operating profit of JPY3.5bn (+2.1% YoY), recurring profit of JPY4.0bn (+15.0% YoY), and net income attributable to owners of the parent of JPY1.8bn (-18.1% YoY). In the dispensing pharmacy industry, earnings traditionally have been at the mercy of biennial NHI drug price revisions. The first-ever "off-year" revision took place in April 2021, with revisions applied to some 70% of all pharmaceuticals on the NHI drug price list. Going forward, drug price revisions will take place annually (incorporating the off-year revisions), and Medical System Network foresees further deterioration in the business climate for dispensing pharmacies, heightening the need for operational stability. The company sees this change in the business climate as an opportunity for the Community Pharmacy Network segment's Pharmaceuticals Network business to

expand via growth in the number of network members. In the Dispensing Pharmacy business, the company will focus on filling more prescriptions by strengthening family pharmacy functions and utilizing its LINE official account to enhance communication with customers. At the Leasing and Facility-related business, the company seeks to stabilize earnings by targeting 90% occupancy for all serviced residences for the elderly. From FY03/22, Medical System Network also has adopted EBITDA as one of its profitability yardsticks.

- Medical System Network announced its fifth medium-term plan spanning a four-year period ending FY03/22 (previous plans covered three-year periods). The latest plan sets out five basic policies: (1) expansion of the Pharmaceuticals Network business with a view to offering greater support for community-based medical care and streamlining drug distribution; (2) raising the caliber of group pharmacies; (3) expanding manufacture and sales of quality generic drugs; (4) strengthening collaboration among group businesses in order to better provide community care functions considered essential to a community-based integrated care system; and (5) improving cash flows as a means of fortifying the financial base.

Strengths and weaknesses

Strengths: a management support network service available to small and mid-tier pharmacies; certified pharmacist training support system that appeals to pharmacies struggling with the pharmacist shortage; and regional dispensing pharmacy strategy in line with administrative guidance. Weaknesses: potential conflict of interest between M&A-driven pharmacy chain expansion and support services for small pharmacies; low profit margins for dispensing pharmacies without drugstore function; and relatively small assets being a disadvantage in acquisitions. (See the Strengths and weaknesses section for details.)

Key financial data

Income statement (JPYmn)	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.	FY03/21 Cons.	FY03/22 Est.
Sales	54,827	66,182	75,548	87,715	88,865	93,977	98,232	105,241	104,257	105,700
YoY	-	20.7%	14.2%	16.1%	1.3%	5.8%	4.5%	7.1%	-0.9%	1.4%
Gross profit	19,412	22,737	28,476	32,801	34,164	36,607	37,271	40,214	42,412	
YoY	-	17.1%	25.2%	15.2%	4.2%	7.2%	1.8%	7.9%	5.5%	
Gross profit margin	35.4%	34.4%	37.7%	37.4%	38.4%	39.0%	37.9%	38.2%	40.7%	
Operating profit	2,047	2,091	2,641	3,783	2,113	3,163	1,428	1,615	3,429	3,500
YoY	-	2.2%	26.3%	43.2%	-44.1%	49.7%	-54.9%	13.1%	112.3%	2.1%
Operating profit margin	3.7%	3.2%	3.5%	4.3%	2.4%	3.4%	1.5%	1.5%	3.3%	3.3%
Recurring profit	1,912	2,020	2,540	3,860	2,109	3,250	1,501	1,560	3,479	4,000
YoY	-	5.6%	25.8%	52.0%	-45.4%	54.1%	-53.8%	3.9%	123.0%	15.0%
Recurring profit margin	3.5%	3.1%	3.4%	4.4%	2.4%	3.5%	1.5%	1.5%	3.3%	3.8%
Net income	756	668	885	1,720	571	1,022	462	-895	2,198	1,800
YoY	-	-11.6%	32.4%	94.4%	-66.8%	79.0%	-54.8%	-	-	-18.1%
Net margin	1.4%	1.0%	1.2%	2.0%	0.6%	1.1%	0.5%	-	2.1%	1.7%
Per-share data (JPY)										
Shares issued (year-end; '000)	25,970	25,970	25,970	29,890	29,890	30,523	30,643	30,643	30,643	-
EPS	29.1	27.7	37.1	60.1	19.3	34.5	15.3	-29.5	72.5	59.7
EPS (fully diluted)	-	-	-	-	-	34.3	15.0	-	-	-
Dividend per share	8.0	8.0	8.0	9.5	10.0	10.0	10.0	10.0	10.0	10.0
Book value per share	222.9	214.7	243.3	334.9	345.3	351.4	354.8	310.4	-	-
Balance sheet (JPYmn)										
Cash and cash equivalents	2,092	3,106	2,499	2,081	2,252	10,201	11,703	11,722	10,118	
Total current assets	8,271	10,941	11,023	10,783	11,098	18,736	21,055	20,578	19,313	
Tangible fixed assets	11,472	15,976	17,249	20,253	21,246	24,129	25,721	25,126	24,634	
Investments and other assets	2,783	3,798	3,759	4,329	4,559	4,847	5,922	6,143	6,926	
Intangible assets	8,263	12,399	13,554	13,481	13,833	15,045	16,235	14,615	13,572	
Total assets	30,789	43,114	45,587	48,847	50,737	62,759	68,935	66,464	64,448	
Accounts payable	5,616	7,798	8,598	9,525	9,144	9,416	10,198	10,021	9,258	
Short-term debt	5,119	12,922	9,214	6,910	3,863	7,463	9,158	8,905	10,210	
Total current liabilities	14,375	24,880	21,626	21,061	16,920	21,769	23,844	23,296	25,418	
Long-term debt	8,758	10,948	15,391	14,859	20,186	26,329	29,739	28,653	22,348	
Total fixed liabilities	10,178	12,882	17,826	17,520	23,172	30,404	34,329	33,749	27,841	
Total liabilities	24,553	37,762	39,452	38,581	40,092	52,174	58,173	57,045	53,260	
Total net assets	6,236	5,352	6,136	10,265	10,644	10,584	10,761	9,418	11,187	
To Total interest-bearing debt	13,877	23,870	24,605	21,769	24,049	33,792	38,897	37,558	32,558	
Cash flow statement (JPYmn)										
Cash flows from operating activities	3,790	3,706	3,838	6,409	3,084	6,699	2,840	4,232	5,205	
Cash flows from investing activities	-5,425	-7,559	-3,958	-5,040	-3,909	-6,848	-5,921	-2,383	-1,485	
Cash flows from financing activities	1,654	4,864	-483	-1,792	998	8,050	4,338	-1,687	-5,312	
Financial ratios										
ROA (RP-based)	6.7%	5.5%	5.7%	8.2%	4.2%	5.7%	2.3%	2.3%	5.3%	
ROE	13.7%	12.2%	16.2%	21.9%	5.7%	9.8%	4.3%	-8.9%	19.7%	
Equity ratio	18.8%	11.9%	12.7%	20.3%	20.1%	16.9%	15.6%	14.2%	17.3%	

Source: Shared Research based on company data

Note: Figures may differ from company materials due to differences in rounding methods.

Segment sales and profit (JPYmn)	FY03/15 Act.	FY03/16 Act.	FY03/17 Act.	FY03/18 Act.	FY03/19 Act.
Sales	75,548	87,715	88,865	93,977	98,232
YoY	14.2%	16.1%	1.3%	5.8%	4.5%
Pharmaceuticals Network	2,814	3,235	3,237	3,639	3,951
YoY	-1.0%	15.0%	0.1%	12.4%	8.6%
% of total	3.6%	3.6%	3.5%	3.8%	4.0%
Dispensing Pharmacy	71,743	82,002	81,650	87,172	90,706
YoY	13.9%	14.3%	-0.4%	6.8%	4.1%
% of total	91.8%	90.5%	89.0%	89.8%	91.7%
Leasing and Facility-related	1,517	2,430	2,046	2,031	3,320
YoY	15.1%	60.2%	-15.8%	-0.7%	63.5%
% of total	1.9%	2.7%	2.2%	2.1%	3.4%
Food Service	1,932	2,830	4,667	4,103	3,161
YoY	218.3%	46.5%	64.9%	-12.1%	-23.0%
% of total	2.5%	3.1%	5.1%	4.2%	3.2%
Other	182	143	163	92	261
YoY	-55.3%	-21.4%	14.0%	-43.6%	183.7%
% of total	0.2%	0.2%	0.2%	0.1%	0.3%
Segment sales adjustments	-2,641	-2,926	-2,900	-3,063	-674
Operating profit	2,641	3,783	2,113	3,163	1,428
YoY	26.3%	43.2%	-44.1%	49.7%	-54.9%
Operating profit margin	3.5%	4.3%	2.4%	3.4%	1.5%
Pharmaceuticals Network	1,549	1,776	1,718	1,949	2,331
YoY	5.0%	14.7%	-3.3%	13.4%	19.6%
Operating profit margin	55.0%	54.9%	53.1%	53.6%	59.0%
Dispensing Pharmacy	2,377	3,412	2,314	3,060	1,068
YoY	29.2%	43.5%	-32.2%	32.2%	-65.1%
Operating profit margin	3.3%	4.2%	2.8%	3.5%	1.2%
Leasing and Facility-related	25	129	-143	-182	-84
YoY	-	416.0%	-	-	-
Operating profit margin	1.6%	5.3%	-7.0%	-9.0%	-2.5%
Food Service	-13	-89	-129	45	34
YoY	-	-	-	-	-24.4%
Operating profit margin	-0.7%	-3.1%	-2.8%	1.1%	1.1%
Other	-76	-109	-163	-97	-101
YoY	-	-	-	-	-
Operating profit margin	-41.8%	-76.2%	-100.0%	-105.4%	-38.7%
Segment profit adjustments	-1,221	-1,335	-1,482	-1,610	-1,733

Segment sales and profit (JPYmn)	FY03/19 Act.	FY03/20 Act.	FY03/21 Act.	FY03/22 Est.
Sales	98,232	105,241	104,257	105,700
YoY	4.5%	7.1%	-0.9%	1.4%
Community Pharmacy Network	92,284	99,617	99,214	100,146
YoY	-	7.9%	-0.4%	0.9%
% of total	93.3%	94.7%	95.2%	94.7%
Three other businesses	6,622	6,389	5,644	6,166
YoY	-	-3.5%	-11.7%	9.2%
% of total	6.7%	6.1%	5.4%	5.8%
Segment sales adjustments	-674	-764	-601	-612
Operating profit	1,428	1,615	3,429	3,500
YoY	-54.9%	13.1%	112.3%	2.1%
Operating profit margin	1.5%	1.5%	3.3%	3.3%
Community Pharmacy Network	3,313	3,743	5,703	5,733
YoY	-	13.0%	52.4%	0.5%
Operating profit margin	3.6%	3.8%	5.7%	5.7%
Three other businesses	-150	-70	-20	167
YoY	-	-	-	-
Operating profit margin	-	-	-0.4%	2.7%
Segment profit adjustments	-1,733	-2,057	-2,253	-2,400

Source: Shared Research based on company data

Note: Figures may differ from company materials due to differences in rounding methods.

Note: The company changed its segments from FY03/20. The new segmentation integrates the former Pharmaceuticals Network and Dispensing Pharmacy businesses with the manufacture and market pharmaceuticals business (included in the Other business) under the Community Pharmacy Network business. The Leasing and Facility-related and Food Service segments are unchanged, but they are included under "Other businesses" in the above table with the home-visit nursing care business (previously included in the Other segment).

Recent updates

Highlights

On June 18, 2021, Shared Research updated the report following interviews with Medical System Network Co., Ltd.

On May 7, 2021, the company announced earnings results for full-year FY03/21; see the results section for details.

For previous releases and developments, please refer to the News and topics section.

Trends and outlook

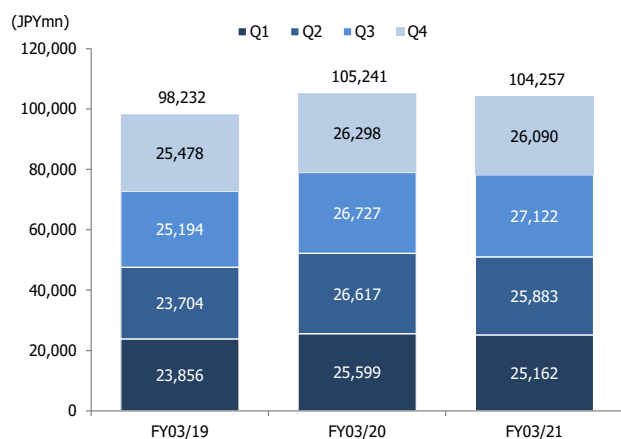
Quarterly trends and results

Cumulative (JPYmn)	FY03/20				FY03/21				FY03/21	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	% of Est.	FY Est.
Sales	25,599	52,216	78,943	105,241	25,162	51,045	78,167	104,257	101.2%	103,000
YoY	7.3%	9.8%	8.5%	7.1%	-1.7%	-2.2%	-1.0%	-0.9%		-2.1%
Gross profit	9,839	19,819	30,225	40,214	9,704	20,502	31,665	42,412		
YoY	8.4%	10.8%	9.8%	7.9%	-1.4%	3.4%	4.8%	5.5%		
Gross profit margin	38.4%	38.0%	38.3%	38.2%	38.6%	40.2%	40.5%	40.7%		
SG&A expenses	9,504	19,022	28,997	38,599	9,765	19,147	28,892	38,982		
YoY	7.2%	9.3%	9.5%	7.7%	2.7%	0.7%	-0.4%	1.0%		
SG&A ratio	37.1%	36.4%	36.7%	36.7%	38.8%	37.5%	37.0%	37.4%		
Operating profit	334	796	1,228	1,615	-61	1,355	2,773	3,429	100.9%	3,400
YoY	57.5%	67.2%	18.1%	13.1%	-	70.2%	125.8%	112.3%		110.5%
Operating profit margin	1.3%	1.5%	1.6%	1.5%	-	2.7%	3.5%	3.3%		3.3%
Recurring profit	323	784	1,208	1,560	-62	1,397	2,770	3,479	102.3%	3,400
YoY	68.2%	79.0%	19.6%	3.9%	-	78.2%	129.3%	123.0%		117.9%
Recurring profit margin	1.3%	1.5%	1.5%	1.5%	-	2.7%	3.5%	3.3%		3.3%
Net income	97	218	326	-895	-201	578	2,013	2,198	109.9%	2,000
YoY	-4.0%	83.2%	-12.4%	-	-	165.1%	517.5%	-		-
Net margin	0.4%	0.4%	0.4%	-	-	1.1%	2.6%	2.1%		1.9%
Quarterly (JPYmn)	FY03/20				FY03/21					
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4		
Sales	25,599	26,617	26,727	26,298	25,162	25,883	27,122	26,090		
YoY	7.3%	12.3%	6.1%	3.2%	-1.7%	-2.8%	1.5%	-0.8%		
Gross profit	9,839	9,980	10,406	9,989	9,704	10,798	11,163	10,747		
YoY	8.4%	13.3%	7.9%	2.5%	-1.4%	8.2%	7.3%	7.6%		
Gross profit margin	38.4%	37.5%	38.9%	38.0%	38.6%	41.7%	41.2%	41.2%		
SG&A expenses	9,504	9,518	9,975	9,602	9,765	9,382	9,745	10,090		
YoY	7.2%	11.4%	9.9%	2.6%	2.7%	-1.4%	-2.3%	5.1%		
SG&A ratio	37.1%	35.8%	37.3%	36.5%	38.8%	36.2%	35.9%	38.7%		
Operating profit	334	462	432	387	-61	1,416	1,418	656		
YoY	57.5%	75.0%	-23.4%	-0.3%	-	206.5%	228.2%	69.5%		
Operating profit margin	1.3%	1.7%	1.6%	1.5%	-	5.5%	5.2%	2.5%		
Recurring profit	323	461	424	352	-62	1,459	1,373	709		
YoY	68.2%	87.4%	-25.9%	-28.3%	-	216.5%	223.8%	101.4%		
Recurring profit margin	1.3%	1.7%	1.6%	1.3%	-	5.6%	5.1%	2.7%		
Net income	97	121	108	-1,221	-201	779	1,435	185		
YoY	-4.0%	572.2%	-57.3%	-	-	543.8%	1228.7%	-		
Net margin	0.4%	0.5%	0.4%	-	-	3.0%	5.3%	0.7%		

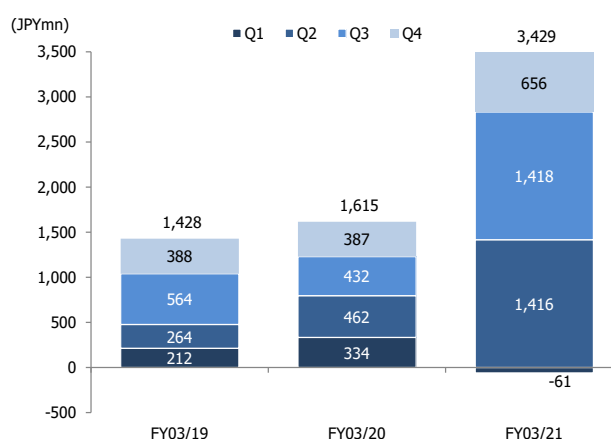
Source: Shared Research based on company data

Note: Figures may differ from company materials due to differences in rounding methods.

Quarterly sales



Quarterly operating profit



Source: Shared Research based on company data

Quarterly results

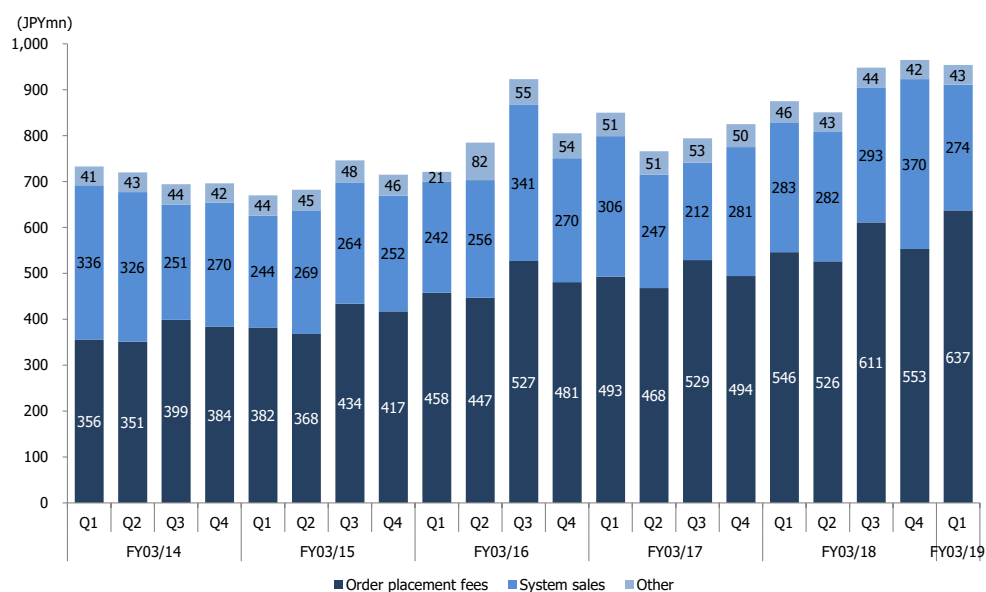
	FY03/20				FY03/21				FY03/21	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	% of FY	FY Est.
Sales	25,599	52,216	78,943	105,241	25,162	51,045	78,167	104,257	101.2%	103,000
YoY	7.3%	9.8%	8.5%	7.1%	-1.7%	-2.2%	-1.0%	-0.9%		-2.1%
Community Pharmacy Network	24,224	49,290	74,637	99,617	23,922	48,539	74,368	99,214	101.3%	97,908
YoY	7.4%	10.2%	9.1%	7.9%	-1.2%	-1.5%	-0.4%	-0.4%		-1.7%
% of total	94.1%	93.6%	93.8%	94.0%	94.5%	94.5%	94.6%	94.6%		
Leasing and Facility-related	760	1,829	2,659	3,425	723	1,438	2,194	2,940		
YoY	26.7%	21.3%	11.6%	3.2%	-4.9%	-21.4%	-17.5%	-14.2%		
% of total	3.0%	3.5%	3.3%	3.2%	2.9%	2.8%	2.8%	2.8%		
Food Service	730	1,434	2,128	2,797	612	1,248	1,874	2,474		
YoY	-7.4%	-9.6%	-10.7%	-11.5%	-16.2%	-13.0%	-11.9%	-11.5%		
% of total	2.8%	2.7%	2.7%	2.6%	2.4%	2.4%	2.4%	2.4%		
Other	38	79	122	165	51	110	171	229		
YoY	15.2%	-13.2%	-26.5%	-36.8%	34.2%	39.2%	40.2%	38.8%		
% of total	0.1%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%		
Segment sales adjustments	-154	-417	-603	-764	-154	-292	-442	-601		-590
Operating profit	334	796	1,228	1,615	-61	1,355	2,773	3,429	100.9%	3,400
YoY	57.5%	67.2%	18.1%	13.1%	-	70.2%	125.8%	112.3%		110.5%
Community Pharmacy Network	825	1,736	2,764	3,743	434	2,369	4,329	5,703	103.9%	5,489
YoY	28.5%	41.5%	18.5%	13.0%	-47.4%	36.5%	56.6%	52.4%		46.6%
Operating profit margin	3.4%	3.5%	3.7%	3.8%	1.8%	4.9%	5.8%	5.7%		
Leasing and Facility-related	-8	68	67	45	6	16	34	32		
YoY	-	580.0%	-	-	-	-76.5%	-49.3%	-28.9%		
Operating profit margin	-	3.7%	2.5%	1.3%	0.8%	1.1%	1.5%	1.1%		
Food Service	-12	-34	-38	-43	-19	-13	-2	-21		
YoY	-	-	-	-	-	-	-	-		
Operating profit margin	-	-	-	-	-	-	-	-		
Other	-21	-39	-56	-71	-11	-13	-17	-31		
YoY	-	-	-	-	-	-	-	-		
Operating profit margin	-	-	-	-	-	-	-	-		
Segment profit adjustments	-447	-934	-1,508	-2,057	-472	-1,003	-1,569	-2,253		-2,126

	FY03/20				FY03/21			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Sales	25,599	26,617	26,727	26,298	25,162	25,883	27,122	26,090
YoY	7.3%	12.3%	6.1%	3.2%	-1.7%	-2.8%	1.5%	-0.8%
Community Pharmacy Network	24,224	25,066	25,347	24,980	23,922	24,617	25,829	24,846
YoY	7.4%	13.1%	7.0%	4.6%	-1.2%	-1.8%	1.9%	-0.5%
% of total	96.6%	93.3%	94.2%	94.4%	94.5%	94.6%	94.7%	94.7%
Leasing and Facility-related	760	1,069	830	766	723	715	756	746
YoY	26.7%	17.7%	-5.0%	-18.3%	-4.9%	-33.1%	-8.9%	-2.6%
% of total	3.0%	4.0%	3.1%	2.9%	2.9%	2.7%	2.8%	2.8%
Food Service	730	704	694	669	612	636	626	600
YoY	-7.4%	-11.8%	-12.8%	-14.1%	-16.2%	-9.7%	-9.8%	-10.3%
% of total	2.9%	2.6%	2.6%	2.5%	2.4%	2.4%	2.3%	2.3%
Other	38	41	43	43	51	59	61	58
YoY	15.2%	-29.3%	-42.7%	-54.7%	34.2%	43.9%	41.9%	34.9%
% of total	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%
Segment sales adjustments	520	-263	-186	-161	-154	-138	-150	-159
Operating profit	334	462	432	387	-61	1,416	1,418	656
YoY	57.5%	75.0%	-23.4%	-0.3%	-	206.5%	228.2%	69.5%
Community Pharmacy Network	825	911	1,028	979	434	1,935	1,960	1,374
YoY	28.5%	80.0%	61.4%	-	-47.4%	112.4%	90.7%	40.3%
Operating profit margin	3.4%	3.6%	4.1%	-	1.8%	7.9%	7.6%	5.5%
Leasing and Facility-related	-8	76	-1	-22	6	10	18	-2
YoY	-	-	-	-	-	-86.8%	-	-
Operating profit margin	-	7.1%	-	-	0.8%	1.4%	2.4%	-
Food Service	-12	-22	-4	-5	-19	6	11	-19
YoY	-	-	-	-	-	-	-	-
Operating profit margin	-	-	-	-	-	0.9%	1.8%	-
Other	-21	-18	-17	-15	-11	-2	-4	-14
YoY	-	-	-	-	-	-	-	-
Operating profit margin	-	-	-	-	-	-	-	-
Segment profit adjustments	-447	-487	-574	-549	-472	-531	-566	-684

Source: Shared Research based on company data

Note: Figures may differ from company materials due to differences in rounding methods.

(Reference) Former Pharmaceuticals Network segment sales

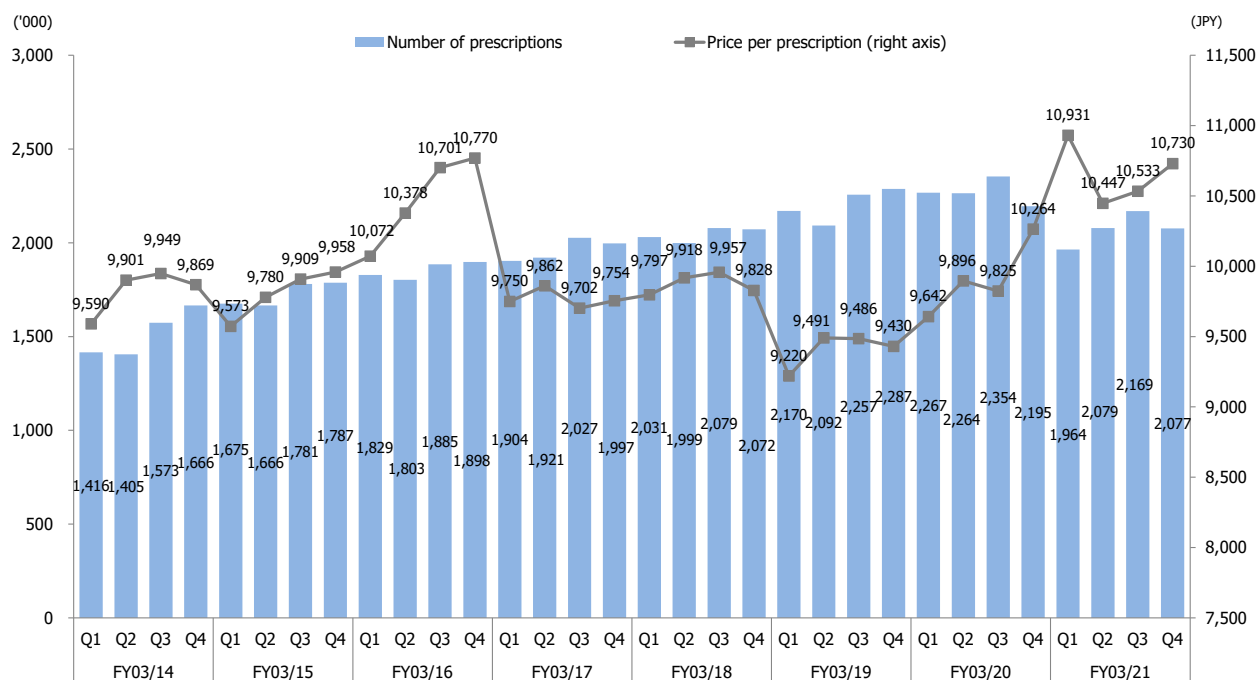


Source: Shared Research based on company data

Notes: Undisclosed from Q2 FY03/19

The former Pharmaceuticals Network segment was integrated into the new Community Pharmacy Network segment from FY03/20

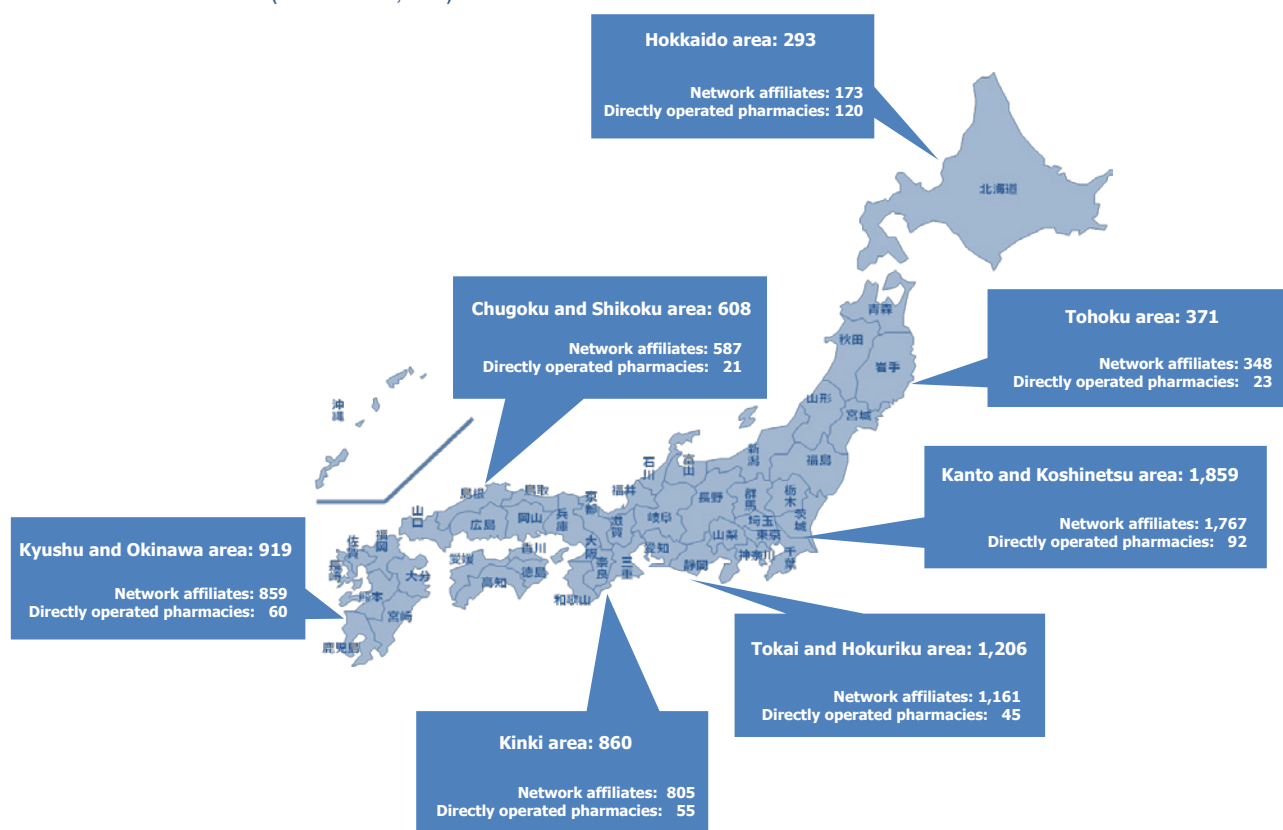
Quarterly trends in prescription volume and price per prescription (drug price + technical fees; Dispensing Pharmacy business; all stores)



Source: Shared Research based on company data

Note: NHI drug price and dispensing fee revisions were put into effect on April 1, 2014, April 1, 2016, and April 1, 2018.

Distribution of network members (as of March 31, 2021)



Source: Shared Research based on company data

Number of dispensing pharmacies by region

Region	Directly operated pharmacies	Affiliates	Total network members
Hokkaido	120	173	293
Tohoku	23	348	371
Kanto and Koshinetsu	92	1,767	1,859
Tokai and Hokuriku	45	1,161	1,206
Kinki	55	805	860
Chugoku and Shikoku	21	587	608
Kyushu and Okinawa	60	859	919
Total	416	5,700	6,116

Source: Shared Research based on company data (March 31, 2021)

Full-year FY03/21 earnings results (out May 7, 2021)

Overview

FY03/21 (April 2020–March 2021) earnings results

- ▷ Sales: JPY104.3bn (-0.9% YoY)
- ▷ Operating profit: JPY3.4bn (+112.3% YoY)
- ▷ Recurring profit: JPY3.5bn (+123.0% YoY)
- ▷ Net income*: JPY2.2bn (versus loss of JPY895mn in FY03/20)

*Net income attributable to owners of the parent

Company response and business conditions

Sales declined 0.9% YoY with the mainstay Community Pharmacy Network business declining 0.4% and the other three businesses falling a combined 11.7%. Among the Community Pharmacy Network business, the Pharmaceuticals Network business recorded a steady increase in new network members, while the Dispensing Pharmacy business saw a 9.4% drop in the number of prescriptions filled owing to fewer medical examinations as a result of the COVID-19 pandemic. This decline in the number of prescriptions filled was the main reason for the drop in sales.

On the profit front, profit margins improved due to an increase in Pharmaceuticals Network business network members, progress promoting the switch to generics in the Dispensing Pharmacy business, streamlined operations, improved productivity, and reduced expenses. Of the JPY1.8bn increase in operating profit, JPY1.4bn was derived from the Dispensing Pharmacy business. The company also turned into the black at the net income level, due to JPY907mn in proceeds from the sale of some shares in a non-equity-method affiliate in December 2020, booked as extraordinary gains.

Breakdown of FY03/21 (April 2020–March 2021) results by segment

Note: Reported sales and earnings at the segment level include intra-group sales and transfers between segments.

Community Pharmacy Network

- ▷ Segment sales: JPY99.2bn (-0.4% YoY)
- ▷ Segment profit: JPY5.7bn (+52.4% YoY)
- ▷ This is a new segment that integrates the former Pharmaceuticals Network business, the Dispensing Pharmacy business, and the manufacture and market pharmaceuticals business (mainly Feldsenf Pharma) previously included in Other.

Pharmaceuticals Network

Despite the loss of some major customers due to the emergence of competitors, the number of new network members continued to increase, driven by the need for improved distribution efficiency. As of end-March 2021, network members numbered 6,116 (+871 versus end-FY03/20), consisting of 416 directly operated pharmacies and 5,700 affiliates. By end-March 2021, the company's market share (number of pharmacies basis) exceeded 10%.

Dispensing Pharmacy

Reflecting the decline in medical examinations in the wake of the pandemic, the number of prescriptions filled during the period declined 9.4% despite a 7.7% hike in average prescription prices due to an increase in long-term prescriptions. However, the company notes segment profits increased thanks to efforts to promote the switch to generics as an economic alternative with stable supply, as well as to streamline operations, optimize personnel deployment, and reduce overtime. As of end-March 2021, the group had 416 dispensing pharmacies, one care plan center, and eight cosmetics/drug stores.

Manufacture and market pharmaceuticals

This business aims to provide a stable supply of good-quality, low-priced generic drugs. As of end-March 2021, the company was selling 34 different ingredients and 68 products. Sales exceeded JPY1bn and the business turned profitable.

Digital shift

Subsidiary PharmaShift Co., Ltd. was established on October 1, 2020, to create a “new pharmaceutical platform” for the digital age. In March 2021 the subsidiary launched the “Your Family Pharmacy” service utilizing its official LINE account. The number of registered friends increased from 10,000 as of April 2, 2021 to over 50,000 by May 28, 2021. Furthermore, the number of pharmacies adopting the service reached 168 as of April 2021.

Leasing and Facility-related

- ▷ Segment sales: JPY2.9bn (-14.2% YoY)
- ▷ Segment profit: JPY32mn (-28.7% YoY)

Reasons for declines in sales and profit

In FY03/21, the spread of COVID-19 limited sales activities for the company’s serviced elderly housing facilities, leading to sluggish growth in occupancy. There were also pandemic-related postponements of certain construction projects. As of end-March 2021, the company reported stable occupancy rates at three out of its five properties, while for the remaining two, at Wisteria Senri-Chuo it reported an occupancy rate of 78.1% (with 64 out of 82 units occupied), and at Wisteria Minami Ichijo it reported an occupancy rate of 67.2% (with 78 out of 116 units occupied).

Food Service

- ▷ Segment sales: JPY2.5bn (-11.6% YoY)
- ▷ Segment loss: JPY21mn (versus loss of JPY43mn in FY03/20)

Loss improved

While there was a decline in the number of meals supplied due to the pandemic, losses narrowed owing to the company’s withdrawal from unprofitable facilities.

Other (mostly home-visit nursing care)

- ▷ Segment sales: JPY229mn (+38.6% YoY)
- ▷ Segment loss: JPY31mn (versus loss of JPY71mn in FY03/20)

For details on previous quarterly and annual results, please refer to the Historical performance and financial statements section.

Company forecast for FY03/22

Recent performance and FY03/22 company forecast

(JPYmn)	FY03/20			FY03/21			FY03/22		
	1H Act.	2H Act.	FY Act.	1H Act.	2H Act.	FY Act.	1H Est.	2H Est.	FY Est.
Sales	52,216	53,025	105,241	51,045	53,212	104,257	51,850	53,850	105,700
YoY	9.8%	4.6%	7.1%	-2.2%	0.4%	-0.9%	1.6%	1.2%	1.4%
Cost of sales	32,397	32,630	65,027	30,542	31,303	61,845			
Gross profit	19,819	20,395	40,214	20,502	21,910	42,412			
Gross profit margin	38.0%	38.5%	38.2%	40.2%	41.2%	40.7%			
SG&A expenses	19,022	19,577	38,599	19,147	19,835	38,982			
SG&A ratio	36.4%	36.9%	36.7%	37.5%	37.3%	37.4%			
Operating profit	796	819	1,615	1,355	2,074	3,429	1,400	2,100	3,500
YoY	67.2%	-14.0%	13.1%	70.2%	153.2%	112.3%	3.3%	1.3%	2.1%
Operating profit margin	1.5%	1.5%	1.5%	2.7%	3.9%	3.3%	2.7%	3.9%	3.3%
Recurring profit	784	776	1,560	1,397	2,082	3,479	1,750	2,250	4,000
YoY	79.0%	-27.0%	3.9%	78.2%	168.3%	123.0%	25.3%	8.1%	15.0%
Recurring profit margin	1.5%	1.5%	1.5%	2.7%	3.9%	3.3%	3.4%	4.2%	3.8%
Net income	218	-1,113	-895	578	1,620	2,198	750	1,050	1,800
YoY	83.2%	-	-	165.1%	-	-	29.8%	-35.2%	-18.1%
Net margin	0.4%	-2.1%	-0.9%	1.1%	3.0%	2.1%	1.4%	1.9%	1.7%

Source: Shared Research based on company data

Note: Figures may differ from company materials due to differences in rounding methods.

- ▷ Sales: JPY105.7bn (+1.4% YoY)
- ▷ EBITDA: JPY6.5bn (+1.2% YoY; adopted as a new yardstick for profitability)
- ▷ Operating profit: JPY3.5bn (+2.1% YoY)
- ▷ Recurring profit: JPY4.0bn (+15.0% YoY)
- ▷ Net income*: JPY1.8bn (-18.1% YoY)
- ▷ EPS: JPY59.70 (-17.7% YoY)

*Net income attributable to owners of the parent

Sales forecast by segment

Community Pharmacy Network segment: Sales of JPY100.1bn (+0.9% YoY), segment profit of JPY5.7bn (+0.5% YoY)

Other three businesses: Sales of JPY6.2bn (+9.2% YoY), segment profit of JPY167mn (versus a loss of JPY20mn in FY03/21)

Adjustments: -JPY612mn for sales, -JPY2.4bn for segment profit

Background to earnings forecasts

In the dispensing pharmacy industry, earnings traditionally have been at the mercy of biennial NHI drug price revisions. The first-ever “off-year” revision took place in April 2021, with revisions applied to some 70% of all pharmaceuticals on the NHI drug price list. Going forward, drug price revisions will take place annually (incorporating the off-year revisions), and Medical System Network foresees further deterioration in the business climate for dispensing pharmacies, heightening the need for operational stability. On the other hand, the company noted progress has been made in winning the understanding of wholesalers on previously promoted improvements to drug distribution.

The company sees this change in the business climate as an opportunity for the Community Pharmacy Network segment's Pharmaceuticals Network business to continue expanding the number of network members by providing a dispensing pharmacy operating platform. The company aims to increase the number of network members by 1,184 to 7,300 by end-March 2022. In the Dispensing Pharmacy business, the company aims to restore sales and continue improving profitability by focusing on filling more prescriptions through strengthening family pharmacy functions, utilizing its LINE official account to enhance communication with customers and enhancing the quality of pharmacists through introduction of the new education system (CP

Step). At the Leasing and Facility-related business, the company seeks to stabilize earnings by targeting 90% occupancy for all serviced residences for the elderly.

Medium-term plan (out May 8, 2018)

Core strategies of the fifth medium-term plan

Comparison with fourth medium-term plan

Medical System Network announced its fifth medium-term plan (FY03/19–FY03/22) at the time of its earnings announcement for FY03/18. The company had previously reviewed its medium-term plans every three years. The fourth medium-term plan that ended in FY03/18, was preceded by a plan covering FY03/13–15. Starting from the fifth medium-term plan, however, the company changed the term to four years, which would be in line with the cycle of medical treatment fee revisions.

Core strategies: Details and company targets

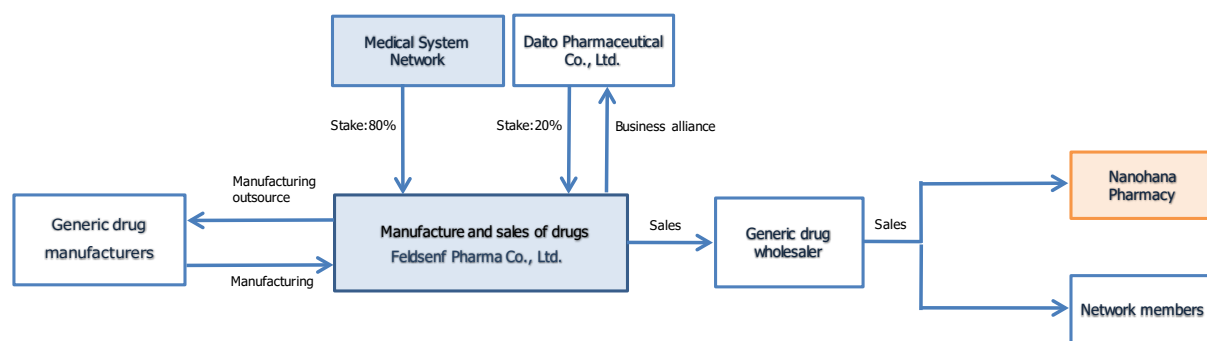
The core strategies of the fifth medium-term plan are as follows. The first four are in response to the NHI drug price and dispensing fee revisions implemented in April 2018. The third strategy is linked to the company's full-scale entry into the generic drug business (manufacture and sales), and the company expects earnings contribution from its consolidated subsidiary Feldsenf Pharma, which will have a central role in managing the business. Regarding the fifth strategy, given that the construction of a new serviced elderly housing facility was near completion as of end FY03/18, the company intends to focus on boosting occupancy rates for these units. Also, having made continued investments into these new facilities up until now, the company sees the period covered by the fifth medium-term plan as a time to focus on stepping up its financial base.

- ▷ Drive collective efforts of all network members to expand the pharmaceuticals network and provide management support to small and mid-tier pharmacies that help sustain community-based medical care; also improve drug distribution efficiency through collective efforts.
- ▷ Position directly operated pharmacies as medical institutions and raise their caliber; promote their family pharmacy functions, allowing them to take initiative in resolving issues surrounding community medical care.
- ▷ Assist government-driven efforts to increase generic drug utilization and help develop efficient drug distribution systems by expanding manufacture and sales of quality generic drugs.
- ▷ Strengthen collaboration among group businesses and take a unified approach in providing community care functions (medical care, long-term care, and disease prevention) that are considered essential to the community-based integrated care system.
- ▷ Improve cash flows, take further steps to achieve efficient management structure, and fortify financial base.

We understand that in the mid- to long-term, Feldsenf Pharma, a generic drugs subsidiary (manufacture and sales) established by the company, will take on a significant role in Medical System Network's generic drug business cited in the third strategy. In the final year of the fifth medium-term plan, the company plans on sourcing around 50% of its consolidated operating profit from the Supply Chain Management (SCM) business, which is the combination of the generic drugs business centering on Feldsenf Pharma, and the Pharmaceuticals Network business.

Medical System Network has not changed its basic policy outlined above, even after the change in business environment due to the spread of COVID-19 in FY03/20. It provides specific policies for each business in the core Community Pharmacy Network segment. In the Pharmaceuticals Network business, the company will continue to maintain and increase network members. In the Dispensing Pharmacy business, the company aims to strengthen the family pharmacy function of its directly operated Nanohana Pharmacies. In the manufacture and market pharmaceuticals business, the company seeks to increase the product lineup of generic drugs sold as well as the number of network members that sell its products. In May 2021, the company announced a change to its fifth medium-term plan final year (FY03/22) sales and profit forecasts to reflect the impact of the COVID-19 pandemic.

Feldsenf Pharma's generic drugs supply chain



Source: Shared Research based on company data

According to information released by the company in February 2018, Feldsenf Pharma's product lineup only comprised six generic drug APIs and 13 products, but the subsidiary looks to expand and improve the lineup, which would also include existing generic drugs. At end-FY03/20, Feldsenf Pharma's product lineup had grown to 23 generic drug APIs and 51 products, with a target of 100 products at end-FY03/22. Feldsenf Pharma is unmatched by industry peers in that it can lower transport costs, control production based on demand from network members (affiliates and directly operated pharmacies), and has a strategy to reduce delivery charges. We believe Feldsenf Pharma, by fulfilling its given role, will not only help raise the generic drugs ratio at Medical System Network pharmacies but also contribute to the company's consolidated results. The company targets an increase in the number of pharmacies selling its products to 1,000 at end-FY03/21.

Numerical targets (as of when plan was announced)

The company outlined numerical targets for FY03/22 (the final year of the fifth medium-term plan) as follows: JPY120.0bn in sales, JPY5.0bn in operating profit (consolidated EBITDA of JPY7.5bn), equity ratio of over 30%, and 5,000 network members (when initially announced). The number of pharmacies looking to become network members continues a steady increase. With more pharmacies having sought to become network members since the April 2018 NHI drug price revision, the company cleared the 5,000-member target in FY03/20, two years earlier than initially planned. In FY03/21, the number network members surpassed 6,000, exceeding a market share of 10% (number of pharmacies basis). In terms of earnings forecasts, the company revised its FY03/20 forecasts to reflect the impact of COVID-19 and associated significant change in the operating environment. The company initially issued its full-year FY03/21 forecast in a range form and revised the forecast on November 6, 2020. As for the numerical targets for FY03/22, the final year of its fifth medium-term plan, the basic policy is unchanged but announced when reporting FY03/21 results that the forecasts need to reflect the continuing impact of COVID-19 pandemic and NHI price revisions.

(Reference) Numerical targets for the fifth medium-term plan (at time of announcement)

(JPYmn)	FY03/17	FY03/18	FY03/19		FY03/20	FY03/22
	Act.	Act.	Act.		Est.	Target
Sales	88,865	93,977	98,232	Sales	103,000	120,000
Pharmaceuticals Network	3,237	3,639	3,951	Pharmaceuticals Network	97,461	-
Dispensing Pharmacy	81,650	87,172	90,706	Three other businesses	6,113	-
Operating profit	2,113	3,163	1,428	Operating profit	2,500	5,000
Pharmaceuticals Network	1,718	1,949	2,331	Pharmaceuticals Network	4,783	-
Dispensing Pharmacy	2,314	3,060	1,068	Three other businesses	-240	-
EBITDA	4,717	5,711	4,200	EBITDA	-	7,500
Recurring profit	2,109	3,250	1,501	Recurring profit	2,400	-
RPM	2.4%	3.5%	1.5%	RPM	2.3%	-
Net income	571	1,022	462	Net income	650	-
Equity ratio	20.1%	16.9%	15.6%	Equity ratio	-	30% or higher
Pharmaceuticals Network members	1,770	2,509	3,790	Pharmaceuticals Network members	5,000	5,000
No. of regional pharmacies	377	399	420	No. of regional pharmacies	-	-

Source: Shared Research based on company data

Note: Figures may differ from company materials due to differences in rounding methods.

Note: Segment figures include internal transactions.

Business

Business model

Medical System Network provides dispensing pharmacy support services to its own pharmacies and to affiliates. Based on the FY03/19 results reported under the former segment classifications, approximately 90% of the company's sales came from the operation of dispensing pharmacies (Dispensing Pharmacy business*). The dispensing pharmacy support service (Pharmaceutical Network business*), while highly profitable, accounts for a smaller portion of overall sales than operation of dispensing pharmacies. As such, the company can be considered a pharmacy chain that also extends its services to non-directly operated pharmacies.

*The Dispensing Pharmacy business and the Pharmaceutical Network business were formerly independent reportable segments. The two businesses were consolidated into the new Community Pharmacy Network segment in FY03/20.

The dispensing pharmacy support service developed by Medical System Network is provided not only to directly-operated pharmacies but also to non-group dispensing pharmacies (affiliates). The Dispensing Pharmacy business generated about 30% of operating profit (unadjusted for internal transactions) in FY03/19 while the Pharmaceuticals Network business accounted for about 70%, suggesting high OPM for the latter considering the segment's small share of sales.

Dispensing pharmacies in Japan are regulated by the nation's universal healthcare insurance system governed by the Ministry of Health, Labour and Welfare (MHLW). The system requires the separation of prescription and dispensary practices, where patients receive prescriptions from physicians at medical institutions and have them filled at dispensing pharmacies by a pharmacist. Under the universal healthcare insurance system, the cost of medication is split between patients and their insurance plans. When a pharmacy dispenses drugs, it collects the patient co-payment (30% of total cost for most company employees) in cash and obtains dispensing fee receivables for the insurance plan portion (70%), for which a reimbursement claim is later submitted. The prices for drugs and medical services are set by the regulatory authorities.

Overview of business segments

Medical System Network comprised five business segments until FY03/19. The mainstay segments were Pharmaceuticals Network and Dispensing Pharmacy. These two segments were consolidated into the Community Pharmacy Network segment along with the manufacture and market pharmaceuticals business (previously included in the Other business and operated by Feldsenf Pharma). PharmaShift Co., Ltd, was established on October 1, 2020 to operate the Family Pharmacy Support Service. The new Community Pharmacy Network segment from FY03/21 comprises the Pharmaceuticals Network, Dispensing Pharmacy, manufacture and market pharmaceuticals, and digital shift businesses. The company does not disclose a sales and profit breakdown by business.

As peripheral business in healthcare and care-related businesses, the company maintains its three segments; Leasing and Facility-related, Food Service, and Other businesses. The main business in the Other business segment is home-visit nursing care. Each business segment continues to be operated by respective core subsidiaries.

Affiliated companies (as of May 31, 2021)

Segment	Company	Location	Ratio of voting rights
Dispensing Pharmacy	Hokkaido Institute for Pharmacy Benefit Co., Ltd.	Sapporo, Hokkaido	100.0%
	Nanohana Hokkaido Co., Ltd.	Sapporo, Hokkaido	100.0%
	Clinics Co., Ltd.	Sapporo, Hokkaido	100.0%
	Nanohana Tohoku Co., Ltd.	Hachinohe, Aomori	100.0%
	Nanohana East Japan Co., Ltd.	Minato-ku, Tokyo	100.0%
	Metro Pharmacy Co., Ltd.	Minato-ku, Tokyo	100.0%
	Nanohana Central Co., Ltd.	Nagoya, Aichi	100.0%
	Nanohana West Japan Co., Ltd.	Toyonaka, Osaka	100.0%
	Total Medical Service Co., Ltd.	Kasuya, Fukuoka	100.0%
	Nagatomi Pharmacy Co., Ltd.	Oita, Oita	100.0%
	Feldsenf Pharma Co., Ltd.	Sapporo, Hokkaido	80.0%
Digital Shift	PharmaShift Co., Ltd.	Minato-ku, Tokyo	51.0%
Leasing and Facility	Paltecno Co., Ltd.	Sapporo, Hokkaido	100.0%
Food Service	Sakura Foods Co., Ltd.	Kasuya, Fukuoka	100.0%
Other	Agrimas Corp. *	Ota-ku, Tokyo	77.7%
	Home-Visit Nursing Care Station Himawari Co., Ltd.	Nerima-ku, Tokyo	100.0%

Source: Shared Research based on data from the company website.

Notes: *Not consolidated

**Company names for Apotec Co., Ltd. and Kyoei Pharmacy Co., Ltd. were changed to Nanohana Tohoku Co., Ltd. and Nanohana West Japan Co., Ltd. as of April 1, 2019.

***Home-visit Nursing Care Station Himawari will be consolidated through absorption-type merger from July 1, 2021 (announced in May 2021)

Community Pharmacy Network

The Community Pharmacy Network business is a new segment created in FY03/20 from consolidating the Pharmaceuticals Network, Dispensing Pharmacy, and a part of the Other (manufacture and market pharmaceuticals business) segments. The new Family Pharmacy Support Service business was also added from FY03/21.

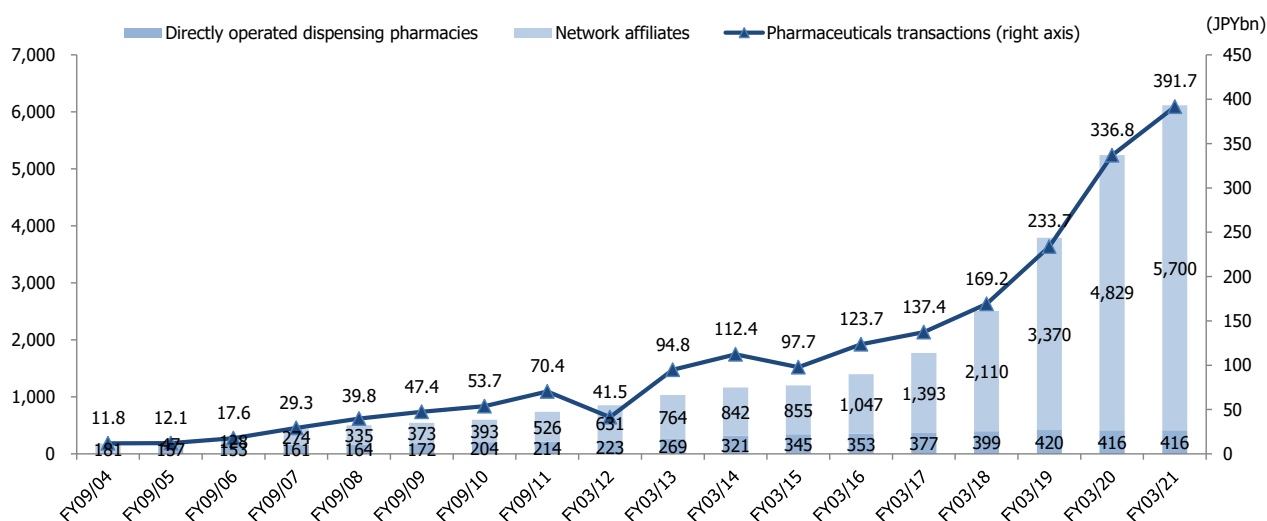
The company cited following two reasons for the reorganization:

- ▷ To accommodate expansion of the company's business scope to the entire supply chain accompanied by the rise in pharmaceuticals network members and full-scale development of the manufacture and market pharmaceuticals business
- ▷ To transition to a structure that can provide value to the entire supply chain while taking into account possible conflicts of interest between business segments due to the aforementioned changes

Pharmaceuticals Network business (former Pharmaceuticals Network segment)

The core Pharmaceuticals Network business offers comprehensive support for operating pharmacies, ranging from the sourcing of drugs to pharmacist training and financing. It can be broken down into four major functions: Pharmaceuticals supply chain management, slow moving inventory clearance, pharmacist training, and financing.

Network members and pharmaceuticals transactions



Note: Figures for FY09/04 are totals of directly operated dispensing pharmacies and affiliates only.
Source: Shared Research based on company data

Four functions

(1) Pharmaceuticals supply chain management

Medical System Network negotiates terms of business with drug wholesalers on behalf of its network members. Typically, dispensing pharmacies have to negotiate prices separately with each wholesaler. However, the company represents its network members collectively in negotiations with wholesalers around the country. The wholesalers benefit from the company's services in a number of ways. They can receive payment from all network members two months after closing instead of the standard three months, which reduces interest expenses. The company's collection service helps them minimize the cost of recovering outstanding payments for pharmaceutical products. The online ordering system improves and optimizes inventory control for pharmacies, reducing order frequency and emergency deliveries, thus lowering wholesaler costs. These cost-saving advantages give the company the power to negotiate better prices with wholesalers. Price negotiation is crucial to dispensing pharmacies that interact with multiple drug wholesalers since the difference between the actual drug sourcing cost and official price of prescription drugs represents their profit stream, but it is also a source of heavy operational burden.

In negotiating terms with wholesalers, Medical System Network adopts the law of one price. Instead of using order volume as bargaining power (making lower price a condition for large orders), it negotiates with all wholesalers based on a common price per each pharmaceutical product. Further, the company does not get involved in the transactions and relationships between the pharmacies and their regular suppliers* (wholesalers). Members can choose which wholesaler to buy from on the basis of service and other conditions, not price. This system lowers the hurdle for dispensing pharmacies thinking of joining the network, but wants to keep existing trading accounts with their regular suppliers, and appeals to wholesalers as well, because they can maintain relationships with existing customers. It is thus a win-win for both retailers and wholesalers. The company also benefits, because it can attract new network members by allowing them to maintain their existing accounts.

Medical System Network is also focusing on handling generics, whose use is being strongly promoted by MHLW. The company gathers and analyzes detailed information such as interview forms** mainly about drugs added to the NHI list that it receives from pharmaceutical companies. The company then negotiates with wholesalers about stable supply of the product, price, and other conditions, and provides information on the product to network members if it concludes that it can be dispensed safely by the pharmacists. The company also provides a substantial support system to its affiliates to increase their handling of generics, including an inventory management system with the same features as the generic drug recommendation system used by its directly operated pharmacies.

*Regular supplier/trading account: A relationship between retailer and wholesaler whereby the retailer has a trading account with the wholesaler. For a retailer, a regular supplier is a wholesaler with which it has a history of doing business.

****Interview form: Pharmaceutical Interview Form (IF), whose purpose is to supplement information that is not fully covered in package inserts of prescription drugs. These forms are supplied by pharmaceutical companies and provide all-round product information. Japan Society of Hospital Pharmacists (JSHP) sets IF drafting guidelines and instructs pharmaceutical companies to distribute the forms. Historically produced by pharmacists interviewing companies, the current format was established in 1988.**

(2) Slow moving inventory clearance service (dead stock exchange)

This system allows for the exchange of dead stock pharmaceuticals among network members. A pharmaceutical product can no longer be dispensed once it expires, so the disposal of dead stock becomes a cost burden on dispensing pharmacies. The primary objective of the system is to reduce inventory disposal losses substantially by registering members' dead stock in the system and matching the stock with other members that can use it. Charges for matched dead stock can be settled together with order placement commissions to Medical System Network, so member pharmacies do not need to make payments to each other.

The MHLW has identified wasted pharmaceuticals as a cost burden that needs to be addressed in healthcare reforms. Note that Medical System Network has acquired a patent for this system.

(3) Pharmacist training support

An attractive training system can improve staff loyalty and draw talented recruits to dispensing pharmacies. The company holds nationwide training courses for pharmacists including those working at network pharmacies in collaboration with training organization Iyaku Sogo Kenkyukai (ISK). These workshops are run by dispensing pharmacies and online courses are also available. The workshops cover topics such as simulated patient training, POS* training, case studies, and customer relations training. Certification by Japan Pharmacists Education Center (JPEC; a public interest incorporated foundation) requires attendance at, and gaining credits for workshops run by JPEC and registered organizations that provide group and practical training sessions such as Japan Society of Hospital Pharmacists (JSHP) and Japan Pharmaceutical Association (and their regional chapters). ISK is one of the few private-sector organizations registered as a provider of various certification programs for pharmacists. Medical System Network and ISK help pharmacies run training sessions and apply for accreditation, which enables them to become members of the ISK organization and run JPEC accredited training courses. ISK issues attendance stickers to pharmacists who attend these courses. This is an incentive for network pharmacies, because it helps them recruit pharmacists.

*POS: Problem Oriented System. A predetermined logical and scientific resolution approach used in team medical care, wherein patient information and healthcare professionals' records are shared to clearly ascertain patient medical problems from each professional's point of view.

(4) Financing support

In Japan, the cost of prescription drugs is borne by patients and the public health insurance programs (such as social insurance for company employees and the National Health Insurance [NHI] for non-employees). Dispensing pharmacies receive the patient co-payment over the counter when dispensing drugs and the portion covered by insurance becomes dispensing fee receivables until it gets monetized two months later when pharmacies receive payment from the insurance programs. Under the company's financing support service (optional), these receivables are purchased and securitized, and directly operated pharmacies are provided cash funding more than a month earlier than the payment from insurance programs. This service offers dispensing pharmacies stable low-cost financing, as unlike financing from a bank, no collateral is required. There are also no restrictions on how the funds can be utilized. Social insurance and NHI claims can be securitized separately. Dispensing fee receivables are converted into small-lot securities through financial institutions and sold to investors for capital recovery.

Dispensing Pharmacy business (former Dispensing Pharmacy segment)

Scale

The Dispensing Pharmacy business (operation of dispensing pharmacies) is a core business that accounts for about 90% of the company's sales and about half of its operating profit. The group's dispensing pharmacies had been operating under the umbrella of a holding company Pharmaholdings Co., Ltd., which was the company's subsidiary until October 2017, when it was absorbed by the company. As of May 2019, the group's dispensing pharmacies are operated through seven consolidated subsidiaries. Another subsidiary, Hokkaido Institute for Pharmacy Benefit Co., Ltd., publishes specialized books for pharmacists and other healthcare professionals and analyzes pharmaceuticals-related data.

The Dispensing Pharmacy business operates the group's directly operated pharmacies. The company provides support services through its pharmaceuticals network to both its directly-operated pharmacies and non-directly operated pharmacies (affiliates). Directly operated pharmacies and affiliates make up the company's pharmaceuticals network, but the affiliates are not included in the scope of the Dispensing Pharmacy business. The numbers of both affiliates and directly operated pharmacies continue to rise. The total value of drug orders (which dictates the company's commission revenue) tends to rise in line with the increase in network members, although there have been periods when the value declined due to drug price revisions.

Affiliates and directly operated pharmacies are found in most areas nationwide, although the home base of Hokkaido has the highest concentration of the latter followed by the Kanto and Koshinetsu area. The highest concentration of affiliates is in the Kanto and Koshinetsu area followed by the Tokai and Hokuriku area (for recent regional patterns see the figures Distribution of network members and Number of pharmacies by region in the Trends and Outlook section). As of end-March 2021, the number of directly operated pharmacies and non-directly operated pharmacy members of the Pharmaceuticals Network (affiliates) stood at 6,116, exceeding 10% of the 60,171 pharmacies in Japan (MHLW survey) and ranking first in the domestic market. The total value of drug orders was JPY391.7bn (+16.3%), representing the largest scale in Japan.

Directly operated pharmacies

Functions provided by the company's directly operated dispensing pharmacies do not dramatically differ from those of other dispensing pharmacies, although one distinguishing characteristic is that they tend to be located in residential areas where homes and medical institutions coexist (categorized by the company as the medical mall format including medical plazas). As such, they are well suited to take on the "family pharmacy" function advocated by MHLW. The company aims to strengthen the family pharmacy functions of its pharmacies by offering consultation services concerning nutrition, health, and self-care.

The company regularly provides guidance to directly operated pharmacies. It sets a bar for their financial performance, and when the pharmacies fail to meet those targets, the company investigates the cause and seeks possible solutions. It also advises pharmacy managers, on matters including potential closures. With such guidance, the company continues to promote revitalization of pharmacies, and in FY03/19 it closed 15 outlets while opening eight new stores and acquiring three through M&A.

Market position of directly operated Nanohana Pharmacy

The number of Nanohana brand pharmacies totaled 416 at end-March 2021. The following table compares sales and pharmacy numbers for other major pharmacy chains as of their fiscal year-ends. Unlisted companies and companies mainly operating dispensaries within drugstores are excluded. While Medical System Network brand pharmacies rank within the top 10, it has far fewer outlets than the top-ranking pharmacy chains.

Number of dispensing pharmacies

	FY end	Sales (JPYmn)	No. of pharmacies
1 Ain Holdings	April	292,615	1,088
2 Qol	March	161,832	811
3 Toho Holdings	March	96,124	777
4 Sogo Medical Holdings	March	-	748
5 Nihon Chouzai	March	278,951	670
6 Suzuken	March	96,439	592
7 Kraft	-	193,700	580
8 Medical System Network	March	90,706	416
9 Aisei Pharmacy	March	64,185	396
10 Pharmarise Holdings	May	40,417	312

Source: Shared Research based on data from each company's websites and materials

Note: Sales figures are aggregate of dispensing pharmacy segment, Aisei Pharmacy Co., Ltd. and Kraft Inc. (Sakura Pharmacy) are unlisted, Sogo Medical Holdings was delisted in April 2020, and companies that are primarily drugstore chains were excluded.

Note: Based on earnings announcement data disclosed as of June 2021.

Initiatives in line with the distribution improvement guidelines

The company has taken steps in line with the MHLW objective of reducing medical expenses through streamlining distribution to establish a more efficient supply chain that bolsters online ordering, reduces product returns, and lowers delivery frequency. Particularly noteworthy is its local network initiatives.

A local network aims to foster collaboration among local affiliates of the company's pharmaceuticals network within a community with the following four objectives:

- ▷ Information sharing by affiliates of available pharmaceuticals and inventories
- ▷ Enhanced distribution for the entire region
- ▷ Cooperation on at-home medical care, facility sharing, holding study sessions and exchange meetings
- ▷ Product sharing, interaction and collaboration among employees, and knowledge sharing

Efforts to streamline Nanohana Pharmacy operations

Several measures have been taken to streamline operations of the directly operated pharmacy chain, Nanohana Pharmacy.

- ▷ Reduce time required to input medication history and register drugs to be reviewed: Tablet computers are provided to each pharmacist thus making work more flexible and enabling utilization of free time between dispensing work. Average time required for this task was reduced from 60 minutes to 30 minutes a day.
- ▷ Reduce time spent on ordering drugs: Full adoption of in-house developed automated drug ordering system reduced the time spent on ordering drugs from a daily average of 30 minutes to less than 10 minutes.
- ▷ Reduce patient waiting time: Improvement of waiting time measurement system helped identify causes of long waiting time. A successful case showed that waiting time was cut by about five minutes three months after the identified problem was solved.
- ▷ Optimization of staffing: Setting standard working hours for pharmacists and staff (appropriate number of staff) for each pharmacy and installing management tools enabled the company to gauge appropriate staffing for any given week or any given day of the week.

Manufacture and market pharmaceuticals business (formerly in the Other business)

Business overview

The manufacture and market pharmaceuticals business was transferred from the Other business to the Community Pharmaceutical Network business in FY03/20. It is operated by consolidated subsidiary Feldsenf Pharma Co., Ltd., which was established in September 2016 to manufacture and market ethical drugs. It does not have manufacturing capabilities or facilities but aims to develop an efficient pharmaceutical distribution system from manufacturing through the filling of prescriptions at the pharmacy by building a collaborative relationship with pharmaceutical manufacturers with capability to provide a stable supply of high-quality, lower-priced generic drugs. In 2018, it formed a business alliance with Daito Pharmaceutical Co., Ltd. (TSE1: 4577), which manufactures and supplies ethical drugs to Feldsenf Pharma.

Feldsenf Pharma started marketing generic drugs from 2018. It mainly supplies directly-operated pharmacies and network members, but eyes expanding its lineup of in-house brand generic drugs to become a supplier to dispensing pharmacies and medical institutions nationwide.

Business scale, profit trends

In FY03/19, Feldsenf Pharma started out with 17 active pharmaceutical ingredients (API) across 34 items, and expanded to 34 API across 68 products at FY03/21. Management aims to further expand the product lineup of in-house drugs and sales tie-up products. In FY03/21, the company supplied its products to directly-operated pharmacies and to 1,116 network members. It reported sales exceeding JPY1bn and it was profitable at the operating level.

Digital shift business (established in FY03/21)

Family Pharmacy Support Service

The company established a joint venture, PharmaShift Inc. in September 2020 with OPT, Inc. (unlisted), a core subsidiary of Digital Holdings (TSE1: 2389). Medical System Network holds a 51% equity stake while RePharmacy, Inc (wholly-owned subsidiary of OPT, Inc) holds the remaining 49%. PharmaShift's main business is Family Pharmacy Support Service. Medical System Network created the digital shift business as a new business with establishment of PharmaShift. In the joint venture, PharmaShift is mainly in charge of customer development while OPT focuses on system development.

Family Pharmacy Support Service engages in and pursues the following three points:

- *Facilitates smooth communication between patients and pharmacies by leveraging official LINE accounts and aggregating patients' medical information
- *Contributes to strengthening functionality and enhancing efficiency of family pharmacies while also supporting non-dispensing businesses such as health and nutrition counseling
- *Building an information infrastructure that can be linked with various other businesses such as physicians by aggregating information obtained from having strengthened functionality of family pharmacies

Utilization of official LINE accounts

The plan is to integrate various functions based on the LINE communication app to facilitate communication between patients and pharmacies using the official LINE account. Specifically, Medical System Network looks to incorporate functions such as prescription transmittal, electronic medication records, surveys of pharmacy visits, and follow-ups during medication. In collaboration with OPT, it aims to develop products using the LINE official account based on a common platform for dispensing pharmacies so that it can provide the products not only to directly-operated and network member pharmacies, but to all pharmacies nationwide.

In FY03/21, the Family Pharmacy Support Service utilizing the official LINE account launched from March 15, 2021 and the number of registered friends grew from 10,000 on April 2 to over 30,000 as of May 6. As of end-March 2021, 36 pharmacies had adopted the service, expanding to 168 pharmacies by end-April. According to the company, the number of prescriptions sent to pharmacies that have adopted the service more than double that of those that have not. Safe management of personal information is a high priority, so proactive measures being taken include no need to fill out personal information on the LINE Talk screen, making service available on external website apps, and utilizing highly secure domestic servers.

LINE is a messaging application developed and operated by LINE Inc (unlisted). The LINE messaging application has achieved substantial market penetration in Asian countries such as Japan, Thailand, and Taiwan.

Leasing and Facility-related

Planning and development of medical buildings and medical plazas

In addition to private practice clinics, the company engages in the planning and development of facilities that house multiple medical clinics (medical buildings and medical plazas). The real estate business is mainly operated by subsidiary Nihon Leben, which was a subsidiary, but was absorbed in October 2017.

This business supports development of clinics that goes beyond just real estate brokerage. The focus is on providing a broad range of support to physicians looking to start a practice, beginning with the stage of formulating a basic business plan for the clinic, and spanning the creation of a management philosophy and strategy, investigating the medical area, selecting real estate property, overseeing design and construction, financing, and processing the business start-up application.

The company develops medical malls* where multiple medical institutions are located in one area, which benefit both patients and physicians. Grouping various medical institutions in the same premises provides patients with opportunities to receive

one-stop treatment from multiple specialists. It is also more efficient for physicians, as they can lower costs by sharing facilities and benefit from synergies in patient traffic and advertising.

*Medical mall: Where several specialized clinics and dispensing pharmacies are located in the same building or area. It is called a medical building when they are in the same building and a medical plaza when they are located in the same area.

Medical malls have different formats. For the building format where tenants are only clinics and dispensing pharmacies, the building is often constructed based on the assumption that clinics will move in, so the floor space and specifications are designed accordingly. Another type is a medical area located within a shopping mall or a commercial facility attached to a train station; since station users and local residents frequent these commercial facilities, they can see their physicians after shopping or on their way home. A third format is a congregation of multiple detached clinics in the same area, often established along suburban main roads where land is easy to acquire.

An example of a medical building developed by the company is the Leben Building in Sapporo, Hokkaido. Standing near a general hospital in Sapporo, in an area where multiple specialty clinics are also located, the building houses four clinics, including surgery and internal medicine, and a Nanohana Pharmacy. An example of a medical plaza is the Shizunai Aoyagi district, located in Hidaka, Hokkaido, with five clinics, including internal medicine and otolaryngology, and two Nanohana Pharmacies. The company notes the latter is a medical mall with roots in the local community, and has been attracting attention as a model case for supporting regional medical care in cities experiencing depopulation and aging.

Planning and development of long-term care facilities

The company plans and develops serviced elderly housing facilities that collaborate with medical institutions, long-term care centers, and dispensing pharmacies to ensure an environment where residents can live safely with peace of mind. Wisteria N17, located in Sapporo, Hokkaido, is the company's first serviced elderly housing facility. Standard services include daily safety checks and 24-hour on-call emergency service while fee-based services such as meal catering and long-term care services are also available. Wisteria N17 is also networked with local medical institutions such as the general hospital, specialty clinics, dental clinics, and dispensing pharmacies. The company's fourth facility, Wisteria Senri-Chuo (Toyonaka, Osaka Prefecture), was launched in 2016, and the fifth facility, Wisteria Minami Ichijo (Sapporo, Hokkaido), was opened in November 2018.

According to the company, investment for expansion of serviced elderly housing facilities came to an end in FY03/19, and it is now taking measures to boost occupancy rates at the Wisteria series facilities, especially for the Wisteria Senri-Chuo and Wisteria Minami Ichijo. The company plans to focus on building a community where medical care and long-term care are offered as one, with dispensing pharmacies, hospitals, and long-term care and childcare facilities surrounding the serviced elderly housing facilities.

Food Service

The company provides meals to hospitals and welfare facilities. The meal catering service is provided by Total Medical Service, Kyushu Iryo Shoku Co., Ltd. (merged with Total Medical Service in April 2018), and Sakura Foods Co., Ltd. (wholly owned subsidiary of Total Medical Service) in the Kyushu and Chugoku areas (Fukuoka, Saga, Nagasaki, Oita, Kumamoto, Miyazaki, Kagoshima, and Yamaguchi prefectures).

Other

The major business in this segment is home-visit nursing care carried out by subsidiary Home-Visit Nursing Station Himawari Co., Ltd., which is slated for an absorption-type merger from July 1, 2021. In addition, the manufacture and market pharmaceuticals business, conducted by subsidiary Feldsenf Pharma Co., Ltd., was consolidated into the newly established Community Pharmacy Network segment from FY03/20.

The home-visit nursing care business dispatches specialized nurses to patients' homes to check on their conditions, and provides appropriate nursing care and advice. It collaborates with physicians, healthcare and long-term care professionals, and pharmacists at the company's Nanohana Pharmacy.

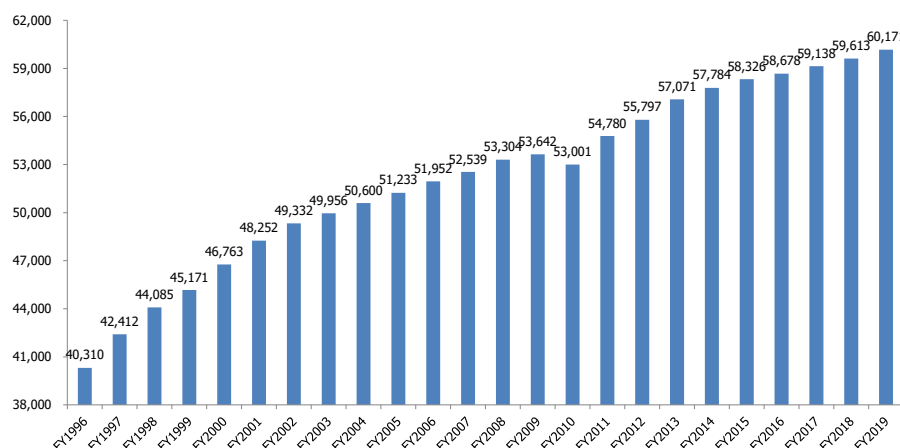
Market and value chain

Continued growth in the dispensing pharmacy market

Dispensing pharmacies fill prescriptions issued by medical institutions. This is based on the separation of prescribing and dispensing functions, in an effort to raise the quality of medical care by letting physicians focus on examining patients and determining appropriate treatment while allowing pharmacists to specialize in dispensing drugs, managing medication history, and providing guidance on usage. According to the Japan Pharmaceutical Association (JPA), the separation accelerated sharply from 1997 when the Ministry of Health and Welfare (the predecessor of MHLW) instructed 37 national hospitals to adopt complete separation (more than 70% of prescriptions must be filled outside the hospital). The out-of-hospital dispensing ratio exceeded 50% nationwide for the first time in 2003. According to JPA estimates, the average ratio rose to 70% by 2016.

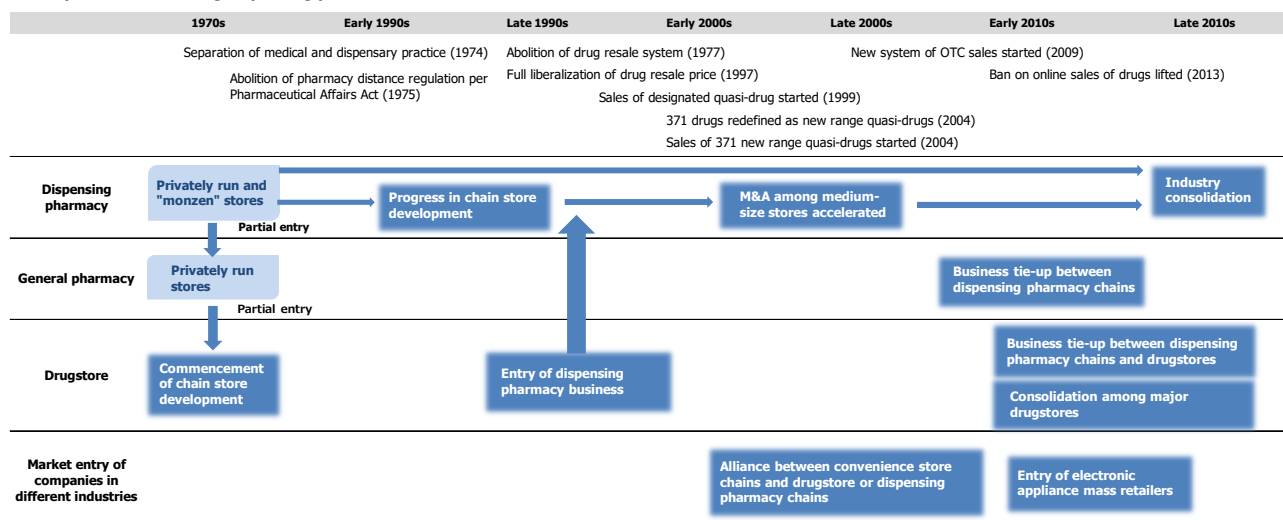
The number of dispensing pharmacies steadily increased as separation of prescribing/dispensing advanced and pharmacies that previously marketed OTC drugs became dispensing pharmacies. There was also a pronounced increase in independent pharmacies operating near large hospitals—so-called “monzen” (Japanese meaning “in front of the gate”) pharmacies. Another factor driving growth has been the expansion of drugstores into the dispensary business. Prescription volumes issued by medical institutions have also been rising.

Number of dispensing pharmacies



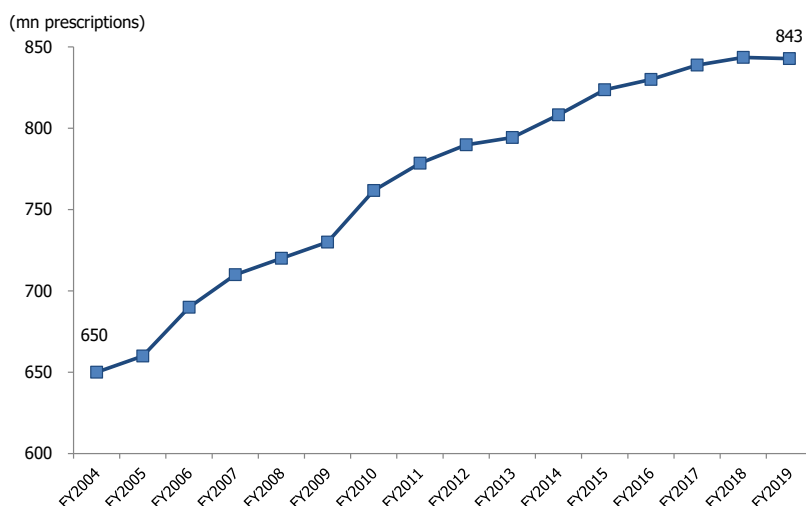
Source: Shared Research based on MHLW's Report on Public Health Administration and Services
Note: 2010 does not include some of Miyagi or Fukushima Prefectures' data.

Developments surrounding dispensing pharmacies



Source: Shared Research based on MHLW's Report on Public Health Administration and Services

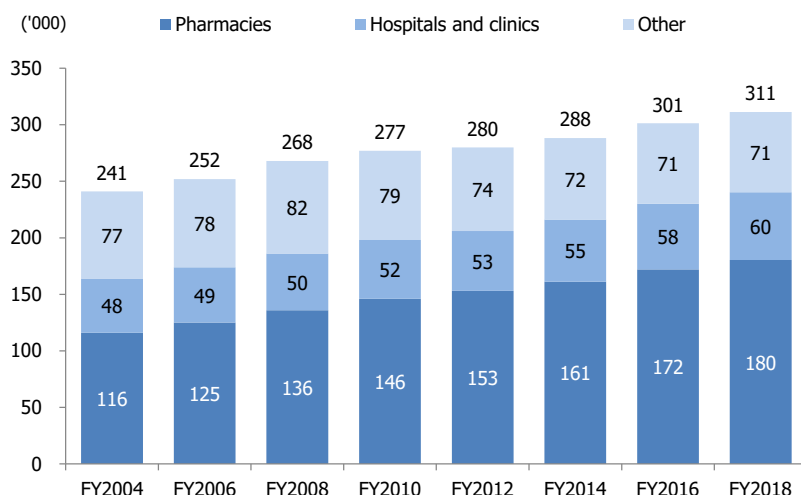
Prescription volume



Source: Shared Research based on MHLW's Trends in Prescription Medicine Costs

Relative to the increase in the elderly population, the number of dispensing pharmacists has not kept pace with the increase in pharmacies, and securing sufficient staffing is a pressing issue, particularly for small and mid-tier pharmacies.

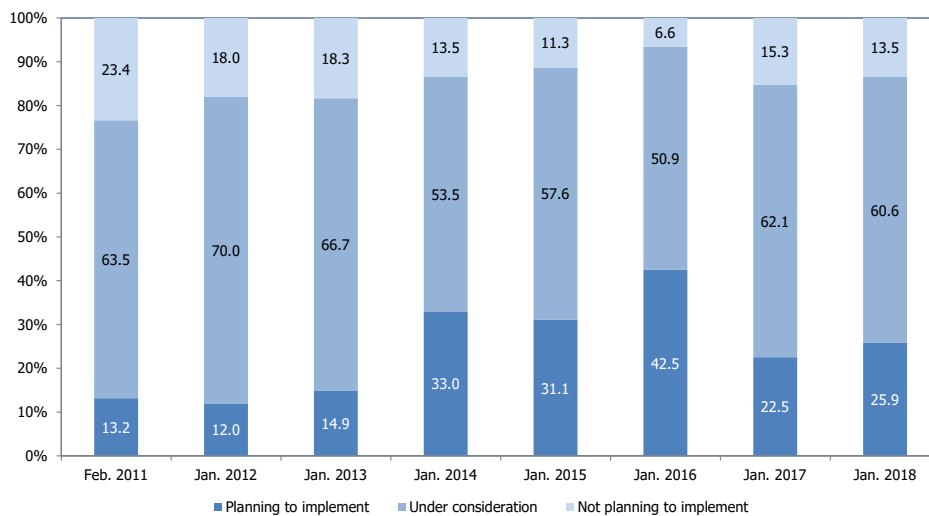
Pharmacist numbers



Source: Shared Research based on MHLW's Report on Survey of Physicians, Dentists and Pharmacists

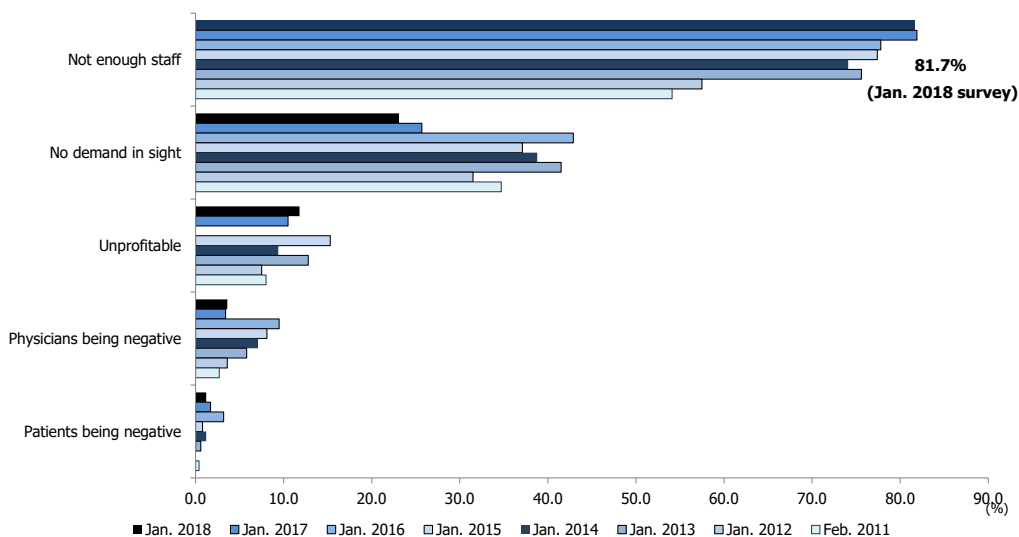
A 2018 Nippon Pharmacy Association (NPhA) survey of member pharmacies showed that the percentage of pharmacies planning to embark on home-based medication management and guidance services, one of the new roles being promoted by MHLW, is not expanding. Most respondents cited labor shortages as the main reason. MHLW is also advocating for 24-hour availability as a means to improve patient convenience, but this service will also likely increase labor costs for dispensing pharmacies.

Survey results on home-based medication management service



Source: Shared Research based on data from Nippon Pharmacy Association Committee for Expansion of Pharmacist Functionality, Report on 2017 Survey of Member Pharmacists (February 2018)

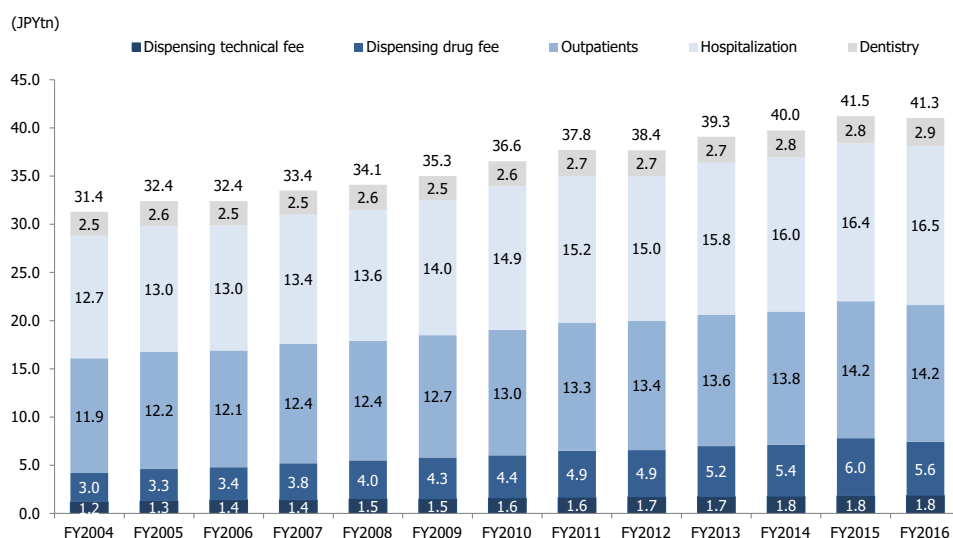
Reasons cited for not providing home-based medication management service



Source: Shared Research based on data from Nippon Pharmacy Association Committee for Expansion of Pharmacist Functionality, Report on 2017 Survey of Member Pharmacists (February 2018)

The motivation behind MHLW's push to expand these roles for pharmacies is a response to steadily rising medical costs in Japan, and, as the Japanese population ages, reducing unnecessary drug use will be essential to maintaining sound healthcare spending. For the same reason, MHLW is also encouraging pharmacies to take on a more patient-centered approach rather than to focus primarily on pharmaceuticals.

(Reference) Drug expenditures



Source: Medical costs and dispensing drug expenditures compiled by Shared Research based on MHLW's Statistics of Medical Care Activities in Public Health Insurance

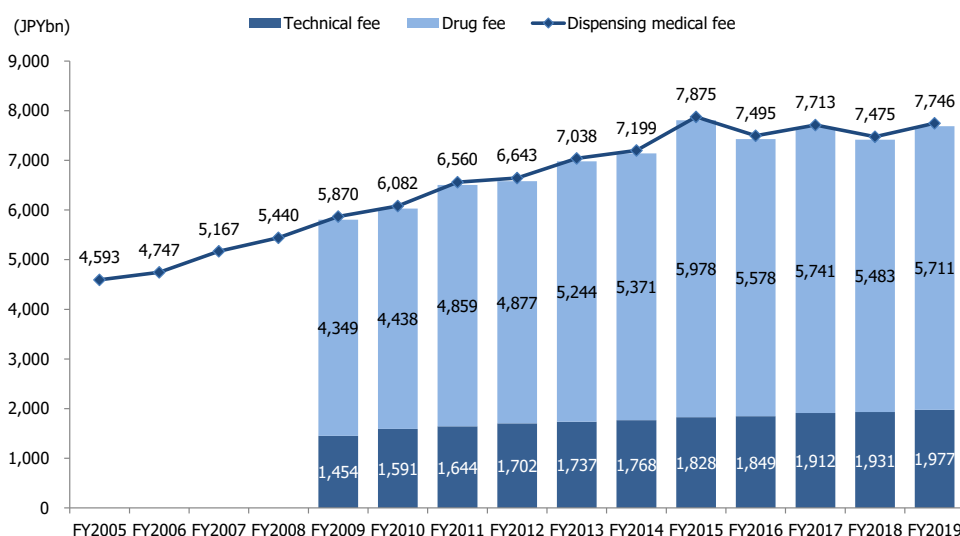
MHLW wants dispensing pharmacies to expand their role from just filling prescriptions to providing comprehensive care to patients as a family pharmacy. This push has made the shortage of pharmacists an even more pressing issue.

Role of dispensing pharmacies in community-based integrated care system: transforming to family, regional pharmacies

Environment facing smaller pharmacies: dispensing fee revisions

The dispensing fee revision implemented in April 2014 reduced the basic dispensing fee for pharmacies that receive more than 90% of their prescriptions from specific medical institutions. The government enacted the changes after reassessing medical care finances amid chronic fiscal deficits, a health insurance program on the verge of collapse, and continually expanding long-term care expenditures. Further reductions in dispensing fees are likely. In addition, faced with concerns of rising medical costs, the government opted to expand the functions of pharmacies rather than increase physician numbers. Thus, it has promoted home medical care services such as prescription delivery and offered preferential treatment to dispensing pharmacies that can provide a 24-hour on-call service. These trends put smaller pharmacies (such as those near large hospitals) at a disadvantage. At a time of flat dispensing fee expenditures, it is crucial for community pharmacies to strengthen their family pharmacy functions and strengthen services that directly earn revenues such as technical fees.

Dispensary charges



Source: Shared Research based on MHLW's Trends in Prescription Medicine Costs

MHLW initiates “Guidelines for the Improvement of Commercial Transaction Practices of Ethical Drugs”

The “Guidelines for the Improvement of Commercial Transaction Practices of Ethical Drugs” (so-called distribution improvement guidelines) were adopted starting April 2018. Issued by MHLW, the guidelines targeting industry members reflect the ministry’s initiative to shift the role of spearheading improvement in prescription drug distribution from the distributors to the government. Items of note on the relationship between drug wholesalers and medical institutions/dispensing pharmacies include the avoidance of excessive discounts. According to these guidelines, offering prices involving excessive discounts that do not reflect the actual value of pharmaceuticals, such as using a benchmark without considering transaction terms, is incompatible with the current NHI drug price system (where individual drug price reflects the value). The guidelines urge wholesalers and medical institutions/dispensing pharmacies also to consider distribution costs and stable provision/sourcing of pharmaceuticals, and to take a comprehensive perspective on each price negotiation, seeing it as an extension of the price negotiations between drug manufacturers and wholesalers.

Key points from the “distribution improvement guidelines”

- ▷ Items of note between manufacturers and wholesalers:
- ▷ Elimination of negative primary margins, presentation of appropriate prices
- ▷ Items of note between wholesalers and medical institutions/dispensing pharmacies:
- ▷ Rapid settlement of transaction prices and promotion of individual drug unit price transactions
- ▷ In principle, all drugs should have individual drug unit prices (no bundling contracts)
- ▷ At a minimum, the percentage of individual drug unit price contracts must exceed previous year levels
- ▷ Adjustment of excessive price discounts that do not reflect pharmaceuticals value and distribution costs
- ▷ Ensured efficiency and safety of distribution
- ▷ Avoidance of costly practices such as frequent and emergency deliveries that can impede stable supply

MHLW will establish a consultation office to support guideline compliance and plans to proactively disclose cases as they come up. In addition to confirming compliance, it will also check to see if the guidelines’ intent and substance are reflected in medical fees.

FY2020 medical fee revision

The FY2020 medical fee revision called for a 0.46% net medical fee reduction, comprised of a 0.55% increase in core medical fees and 1.01% reduction in NHI drug prices (official price of medicines).

Net medical fee revision -0.46% = core medical fee +0.55% + drug reimbursement price -1.01%

The increase in the core medical fee includes +0.53% for medical fees, +0.59% for dental fees, and +0.16% for dispensing fees. In contrast, the reduction in the NHI drug prices includes -0.99% for pharmaceuticals prices and -0.02% for medical material prices. The result of the revisions is a shift from a merchandise-based approach to a patient-centered one, evidenced by the expansion of guidance fees for pharmacists who interact with patients, and the recognition of pharmacies that contribute to community-based medical care such as through provision of medication information to hospitals.

Medical fee revision (%)

Year of revision	FY2002	FY2004	FY2006	FY2008	FY2010	FY2012	FY2014	FY2016	FY2018	FY2020
Core medical fees (actual)	-1.30	±0.00	-1.36	+0.38	+1.55	+1.379	+0.10	+0.49	+0.55	+0.55
Dispensing fee	-1.30	+0.00	-0.60	+0.17	+0.52	+0.46	+0.04	+0.17	+0.19	+0.16
Drug prices (actual)	-1.40	-1.05	-1.80	-1.20	-1.36	-1.375	-1.36	-1.33	-1.74	-1.01
NHI basis	-6.30	-4.20	-6.70	-5.20	-5.75	-6.00	-5.64	-5.57	-7.48	-4.38
Consumption tax addition	-	-	-	-	-	-	+1.36	-	-	-
Total (nominal)	-2.70	-1.05	-3.16	-0.82	+0.19	+0.004	+0.10	-0.84	-1.19	-0.46

Source: Shared Research based on company data

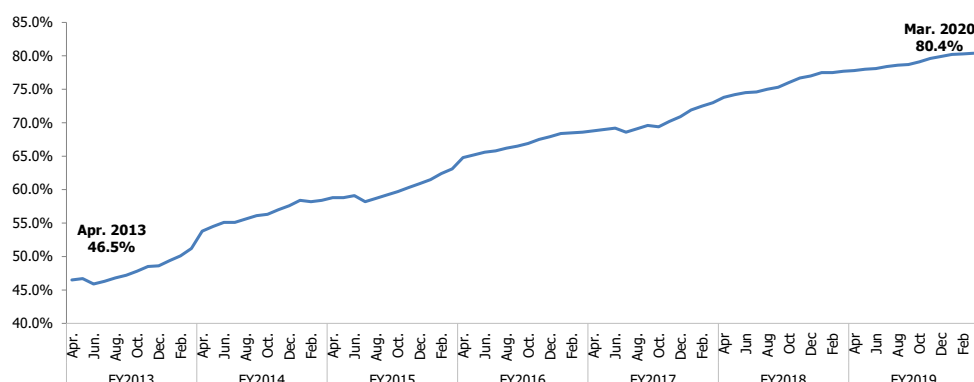
The key point regarding dispensing fees raised around the time of the FY2018 revision is a reassessment of the role of dispensing pharmacies with an emphasis on patient-centered service. Specifically, it promotes evaluation of family pharmacies and pharmacists, patient-centric businesses and at-home medical care; and promotes the use of generic drugs. It also encourages the proper assessment of large pharmacies operating near medical institutions. On generic drug utilization, MHLW is continuing efforts to improve utilization rates, and the FY2020 medical fee revision includes components that will further stimulate generic drug use.

Mid-year revision of NHI drug price

NHI drug price revisions, previously held once every other year, were shifted to an annual basis effective from 2021 with the first mid-year revision conducted in April 2021. The reasoning behind the shift was that the stance of the Japanese government and MHLW intending to reduce healthcare expenditures by reflecting the drop in market values more quickly onto the official reimbursement pricing.

As of May 2021, about 14,228 drugs were listed as ethical drugs used in healthcare services provided by health insurance for reimbursement under the NHI scheme and 12,180 of them were subject to this mid-year price revision. The first mid-year revision was applied to drugs for which the pricing differential between official reimbursement price and actual market price was 0.625x of the average 8.0% divergence (divergence of 5.0% or higher). A breakdown of the 12,180 drugs for which reimbursement prices were revised shows 1,350 were new drugs (59% of new drugs), 1,490 were long-listed drugs (88% of long-listed drugs), 8,200 were generic drugs (83% of generic drugs), and 1,140 were products in the other categories commercialized before 1967 (31% of other drugs). Most of generic and long-listed drugs were subject to this price revisions. Shared Research anticipates the impact of the NHI price revision will be far-reaching, not limited to generic and brand drug manufacturers but extended to pharmaceutical distribution-related companies and dispensing pharmacies.

Generic drug ratio



Source: Shared Research based on MHLW's Recent Trends of Dispensing Medical Costs (electronically processed)

Industry peers (dispensing pharmacy chains)

As industry peers we selected listed companies that operate dispensing pharmacies as their mainstay business. Comparing the operating profit margin of the business segments that operated dispensing pharmacies, Ain Holdings (TSEI: 9627) had the highest OPM. Profit margins declined across the board in FY2017 owing to the diminished impact of major drugs for hepatitis C. The whole industry was affected by the NHI medical fee revision in FY2019, with almost all companies recording lower profit margin than in the previous fiscal year. Medical System Network's segment profit for the Dispensing Pharmacy business ranks around the middle among its peers.

Comparison of profit margins of industry peers' pharmacy operation segments

Ticker	Company	FY end	FY2016	FY2017	FY2018	FY2019	FY2020	FY2021
2796	Pharmarise Holdings	May	2.6%	2.0%	3.5%	2.3%	3.4%	-
3034	Qol	March	5.8%	5.1%	6.4%	4.7%	4.7%	4.4%
3341	Nihon Chouzai	March	5.6%	5.0%	6.0%	4.2%	4.2%	4.3%
4350	Medical System Network	March	4.2%	2.8%	3.5%	3.6%	3.8%	5.7%
4775	Sogo Medical Holdings	March	5.0%	6.3%	6.5%	5.0%	-	-
7649	Sugi Holdings	February	5.6%	5.3%	5.4%	5.3%	5.5%	5.6%
9627	Ain Holdings	April	9.1%	8.6%	9.5%	7.5%	7.9%	-

Source: Shared Research based on each company's data and websites (as of end-May 2021)

Notes:* Values for Medical System Network are profit margins of the Community Pharmacy Network business from 2019.

** Sogo Medical Holdings: FY2016 earnings are total profit margins as segment information is regional, transitioned to a holding company (9277) in October 2018 and delisted on April 17, 2020.

*** Sugi Holdings: Total company profit margins since there is only one segment.

Main industry peers

Ticker	Company	Latest full-year earnings			Description
		Sales (JPYmn)	OPM	ROE	
2796	Pharmarise Holdings	51,030	1.9%	9.6%	Middle-tier pharmacy chain. Leverages partnerships with regional drug wholesalers to acquire local dispensing chains. Has a reputation for community care support. Established joint ventures with Higuchi and FamilyMart to develop pharmacies.
3034	Qol	161,832	4.6%	8.2%	Major pharmacy chain. Started as monzen pharmacy. Opened stores with Lawson and Bic Camera. Also developing MR and pharmacist dispatch business.
3341	Nihon Chouzai	278,951	2.9%	7.3%	Second-ranked dispensing pharmacy chain. Nationwide expansion centered on monzen pharmacies in Kanto-Koshinetsu area. Established generic drug manufacturing subsidiary, also developing in-house drugs. Referral & placement of medical staff such as pharmacists.
4350	Medical System Network	98,232	1.5%	4.3%	Dispensing pharmacy holding company that also operates a pharmaceutical information intermediary network business. Started in Hokkaido, but expanding nationwide through M&A.
7649	Sugi Holdings	602,510	5.6%	11.0%	Developed drugstore/dispensing pharmacy, Sugi Pharmacy, in its stronghold Tokai area. The holding company also has discount stores.
-	Sogo Medical Holdings	-	-	-	Started with hospital room TV and equipment rental business. Entered dispensing pharmacy business, and expanded from local Kyushu to Kinki, Chubu, and East Japan areas. Also engages in medical practice support and hospital revitalization consulting business.
9627	Ain Holdings	292,615	5.5%	8.5%	Top-ranked dispensing pharmacy chain. Originated in Hokkaido, expanded into metropolitan areas, with nationwide coverage of mainly monzen pharmacies. Concluded capital and business tie-up with Seven & I Holdings.

Source: Shared Research based on company data

Note: Sogo Medical Holdings (4775) became Sogo Medical HD (9277) in October 2018 and delisted on April 17, 2020.

Medical System Network ranks among the top ten dispensing pharmacy chains by sales. They all have negative cash flow from investment activities, which we attribute to their strategies of achieving growth by absorbing smaller local dispensing pharmacies (these smaller pharmacies account for 90% of the market). In contrast, Medical System Network has two growth options: integrate pharmacies into the Nanohana Pharmacy group through capital investment, or allow the smaller pharmacy to continue operating independently and bring them into the company group as affiliates (i.e., network users).

Financials of industry peers

(JPYmn)	Medical System Network (4350)			Pharmarise Holdings (2796)			Qol (3034)		
	FY03/19 Cons.	FY03/20 Cons.	FY03/21 Cons.	FY05/18 Cons.	FY05/19 Cons.	FY05/20 Cons.	FY03/19 Cons.	FY03/20 Cons.	FY03/21 Cons.
Sales	98,232	105,241	105,241	54,562	51,728	51,030	144,783	165,411	161,832
Gross profit	37,271	40,214	40,214	7,950	7,342	7,391	17,863	21,094	21,102
SG&A expenses	35,842	38,599	38,599	6,771	6,702	6,403	10,812	13,361	13,737
Operating profit	1,428	1,615	1,615	1,179	640	987	7,050	7,733	7,364
Recurring profit	1,501	1,560	1,560	1,092	590	976	7,208	8,024	7,403
Net income	462	-895	-895	-28	23	526	3,970	4,067	3,365
ROE	4.3%	4.3%	4.3%	-0.5%	0.4%	9.6%	10.5%	10.3%	8.2%
ROA (RP-based)	2.3%	2.3%	2.3%	4.5%	2.4%	3.9%	7.9%	8.1%	7.3%
Operating profit margin	1.5%	1.5%	1.5%	2.2%	1.2%	1.9%	4.9%	4.7%	4.6%
Total assets	68,935	66,464	66,464	24,265	24,217	25,228	94,236	102,872	100,571
Net assets	10,761	9,418	9,418	5,624	5,619	5,895	39,017	41,001	41,834
Equity ratio	100.0%	100.0%	100.0%	21.8%	21.9%	22.4%	41.1%	39.4%	40.9%
Operating CF	2,840	4,232	4,232	1,330	895	1,572	5,773	4,468	12,912
Investing CF	-5,921	-2,383	-2,383	-527	-501	-734	-8,287	-8,670	-3,065
Financing CF	4,338	-1,687	-1,687	-894	354	-766	2,906	-225	-6,114
Cash and deposits	11,520	0	0	3,643	4,393	4,464	193	15,766	19,498
Interest-bearing debt	38,897	37,558	37,558	10,550	11,138	10,375	28,873	32,650	29,721
Net debt	27,377	37,558	37,558	6,907	6,745	5,911	28,680	16,884	10,223
	Nihon Chouzai (3341)			Sugi Holdings (7649)			Sogo Medical Holdings (-)		
	FY03/19 Cons.	FY03/20 Cons.	FY03/21 Cons.	FY02/19 Cons.	FY02/20 Cons.	FY02/21 Cons.	FY03/19 Cons.	FY03/20 Cons.	FY03/21 Cons.
Sales	245,687	222,147	278,951	488,464	541,964	602,510	144,630	-	-
Gross profit	41,975	46,372	49,374	142,300	162,182	181,291	22,715	-	-
SG&A expenses	35,242	38,779	41,267	116,483	132,420	147,590	17,303	-	-
Operating profit	6,733	7,593	8,106	25,817	29,762	33,701	5,411	-	-
Recurring profit	6,077	7,405	8,409	27,237	31,473	35,333	5,607	-	-
Net income	3,792	6,697	3,538	17,940	20,782	21,120	3,246	-	-
ROE	9.2%	15.2%	7.3%	10.9%	11.9%	11.0%	8.7%	-	-
ROA (RP-based)	3.3%	4.1%	4.5%	10.5%	10.9%	10.7%	6.1%	-	-
Operating profit margin	2.7%	2.8%	2.9%	5.3%	5.5%	5.6%	3.7%	-	-
Total assets	178,677	185,551	186,262	265,481	313,757	345,933	93,560	-	-
Net assets	41,073	47,072	49,868	166,563	182,750	200,629	38,669	-	-
Equity ratio	23.0%	25.4%	26.8%	62.7%	58.2%	58.0%	41.0%	-	-
Operating CF	13,572	13,192	11,213	22,894	45,353	34,027	3,852	-	-
Investing CF	-1,770	-2,731	-7,767	-22,362	-18,422	-29,254	-6,624	-	-
Financing CF	-10,516	-7,955	-2,806	-13,897	-4,895	-5,274	-945	-	-
Cash and deposits	29,749	32,254	32,893	34,311	56,347	55,845	10,733	-	-
Interest-bearing debt	82,391	63,624	44,365	0	0	0	22,373	-	-
Net debt	52,642	31,370	11,472	-34,311	-56,347	-55,845	11,640	-	-
	Ain Holdings (9627)								
	FY04/18 Cons.	FY04/19 Cons.	FY04/20 Cons.						
Sales	268,386	275,596	292,615						
Gross profit	47,993	45,363	46,861						
SG&A expenses	28,371	29,295	30,793						
Operating profit	19,623	16,067	16,068						
Recurring profit	20,130	16,637	16,822						
Net income	10,567	9,029	9,179						
ROE	13.5%	9.0%	8.5%						
ROA (RP-based)	11.8%	8.9%	8.8%						
Operating profit margin	7.3%	5.8%	5.5%						
Total assets	183,435	189,021	193,451						
Net assets	96,733	103,922	111,003						
Equity ratio	52.7%	54.9%	57.3%						
Operating CF	21,657	14,788	17,747						
Investing CF	-5,282	-19,985	-11,474						
Financing CF	17,623	-10,681	-7,837						
Cash and deposits	63,233	47,495	45,931						
Interest-bearing debt	18,861	11,957	6,074						
Net debt	-44,372	-35,538	-39,857						

Source: Shared Research based on each company's data

Note: *Sogo Medical (4775) became Sogo Medical HD (9277) in October 2018 and delisted on April 17, 2020.

Strengths and weaknesses

Strengths

- Management support network service available to small and mid-tier pharmacies:** Small pharmacies and mid-tier regional chains (90% of the market) fall behind major nationwide chains in buying power versus drug wholesalers and means to optimize pharmaceuticals inventory. However, by joining the company's network and becoming an affiliate, they can tap into majors-class strength and infrastructure without giving up their autonomy to a major pharmacy chain. The process does not involve a business transfer, so the hurdle for joining the network is relatively low. The company has a network system boasting the largest pharmaceuticals order volume in Japan, and negotiates procurement terms with suppliers on behalf of its members. It is also the only company that offers a dead stock clearance service, which matches members' inventory surpluses with deficiencies to reduce costly write-offs. This service cuts operating costs of network members by 1.3% (company estimate) on average even after factoring for the network usage fee. From the company's standpoint, an increase in network members translates to revenue growth from rising commissions and greater buying power in the pharmaceuticals market.
- Certified pharmacist training support system that appeals to pharmacies struggling with pharmacist shortage:** The company's Pharmaceuticals Network business collaborates with a training organization to support pharmacists (both network member pharmacists and others) enrolled in a certification program authorized by the Japan Pharmacists Education Center (JPEC). Aimed at raising the skill level of pharmacists, the JPEC program certifies those pharmacists who have completed their credit requirements through participation in various training courses (40 credits within four years and 30 credits every three years thereafter). The certification is one of the criteria of a "family pharmacist," whose pharmacy becomes eligible to charge an additional family pharmacist guidance fee. The company mainly utilizes its directly operated pharmacies and affiliates to help the training organization Iyaku Sogo Kenkyukai (ISK) run its accredited training courses nationwide. The service strengthens pharmacists' loyalty to their employers and improve recruitment outcomes. ISK is one of the few private-sector organizations registered with JPEC as a training organization and is authorized to issue the proof of attendance stickers that JPEC issues at its training courses.
- Regional dispensing pharmacy strategy in line with administrative guidance:** A distinguishing feature of the company's dispensing pharmacies is their high concentration in medical malls. This is in line with MHLW's vision for the role of pharmacies in the face of an aging society, and the company's outlet-location strategy benefits from the revised insurance point system. MHLW has revised dispensing fees to encourage a shift away from the pharmacy model linked to specific hospitals (pharmacies operating adjacent to large hospitals) and toward the family pharmacy and regional medical care models that accept prescriptions from a wide range of medical institutions. The company's strategy of opening pharmacies in medical complexes is in line with MHLW guidance and works to its favor in terms of dispensing fee eligibility.

Weaknesses

- Potential conflict of interest between M&A-driven pharmacy chain expansion and support services for small pharmacies:** The Pharmaceuticals Network business provides non-directly operated pharmacies (i.e., affiliates) access to the company's proprietary system, thus allowing them to maintain management independence, but this has the potential negative effect of impeding growth of the Dispensing Pharmacy business. While the company's peers are expanding through acquisition of smaller pharmacies, the availability of membership to the Pharmaceuticals Network system is a possible lifeline to smaller pharmacies that could encourage them to delay M&A action.
- Low profit margins for dispensing pharmacies without drugstore function:** The Dispensing Pharmacy business OPM of about 3.0% (based on disclosed data through FY03/19) is 2–5pp below that of other major chains. This is mainly because most of the company's dispensing operations are limited to prescription drugs and are not accompanied by drugstore functions handling items such as OTC drugs, long-term care products, and toiletries. Many of the other major chains have adopted the strategy to boost pharmacy profit margins by integrating drugstore operations with added floor space for food products and cosmetics. The company is looking to expand its product offerings to include various long-term care products like adult diapers as part of a family pharmacy service, but it will take time to transition to this business format.
- Relatively small assets a disadvantage in acquisitions:** The company is at a disadvantage versus the major players in terms of asset scale when it comes to acquisitions targeting pharmacy chain expansion. Looking at the M&A-based increases

in outlet numbers over the past three years, industry leader Ain Holdings acquired more than 100 pharmacies while Medical System Network was flat YoY in FY03/21. From the perspective of regional expansion, about 30% of the company's pharmacies are located in Hokkaido while less than 10% are located in Tokyo and Osaka, despite their high population density. In total assets, an important indicator of the buyer's financial strength in an M&A deal, comparable companies range in the JPY100.0bn mark and over, while Medical System Network significantly falls behind at around JPY64.0bn. In order to advance acquisitions and increase pharmacy outlets in regions other than its home ground Hokkaido, the company will need to be able to demonstrate its financial strength to the sell-side companies' management as well as M&A intermediaries.

Historical performance and financial statements

Income statement

Income statement (JPYmn)	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.	FY03/21 Cons.
Sales	25,411	54,827	66,182	75,548	87,715	88,865	93,977	98,232	105,241	104,257
YoY	-	-	20.7%	14.2%	16.1%	1.3%	5.8%	4.5%	7.1%	-0.9%
Cost of sales	16,451	35,415	43,445	47,072	54,913	54,700	57,369	60,961	65,027	61,845
Gross profit	8,960	19,412	22,737	28,476	32,801	34,164	36,607	37,271	40,214	42,412
YoY	-	-	17.1%	25.2%	15.2%	4.2%	7.2%	1.8%	7.9%	5.5%
Gross profit margin	35.3%	35.4%	34.4%	37.7%	37.4%	38.4%	39.0%	37.9%	38.2%	40.7%
SG&A expenses	7,603	17,365	20,646	25,835	29,018	32,050	33,444	35,842	38,599	38,982
SG&A ratio	29.9%	31.7%	31.2%	34.2%	33.1%	36.1%	35.6%	36.5%	36.7%	37.4%
Operating profit	1,357	2,047	2,091	2,641	3,783	2,113	3,163	1,428	1,615	3,429
YoY	-	-	2.2%	26.3%	43.2%	-44.1%	49.7%	-54.9%	13.1%	112.3%
Operating profit margin	5.3%	3.7%	3.2%	3.5%	4.3%	2.4%	3.4%	1.5%	1.5%	3.3%
Non-operating income	81	150	250	457	275	378	405	288	361	361
Non-operating expenses	124	284	321	349	380	279	291	333	343	312
Recurring profit	1,315	1,912	2,020	2,540	3,860	2,109	3,250	1,501	1,560	3,479
YoY	-	-	5.6%	25.8%	52.0%	-45.4%	54.1%	-53.8%	3.9%	123.0%
Recurring profit margin	5.2%	3.5%	3.1%	3.4%	4.4%	2.4%	3.5%	1.5%	1.5%	3.3%
Extraordinary gains	25	59	155	169	88	57	19	49	48	914
Extraordinary losses	41	65	404	415	470	260	976	128	1,586	426
Income taxes	702	1,018	1,073	1,315	1,599	1,262	1,271	962	918	1,769
Implied tax rate	54.1%	53.4%	60.6%	57.3%	46.0%	66.2%	55.4%	67.7%	4172.7%	44.6%
Net income attrib. to non-controlling interests	78	133	29	92	158	72	0	-2	0	0
Net income	518	756	668	885	1,720	571	1,022	462	-895	2,198
YoY	-	-	-11.6%	32.4%	94.4%	-66.8%	79.0%	-54.8%	-293.7%	-345.6%
Net margin	2.0%	1.4%	1.0%	1.2%	2.0%	0.6%	1.1%	0.5%	-0.9%	2.1%

Source: Shared Research based on company data

Note: Figures may differ from company materials due to differences in rounding methods.

Changed fiscal year-end in FY03/12; started fifth medium-term plan from FY03/19

Medical System Network changed its fiscal year-end from September to March effective FY03/12, resulting in an irregular six-month term for October 2011–March 2012; sales in FY03/12 were approximately half the FY09/11 figure.

The third medium-term plan (FY03/13–FY03/15) began the following year. We believe the company has also applied plan targets to its business strategy from FY03/16 and beyond (the fourth medium-term plan), i.e., to increase the number of network member pharmacies and grow its own dispensing pharmacies. The five key initiatives of the fifth medium-term plan, which started in FY03/19, are as follows. We note that OPM has remained in the 1% range in FY03/19 and FY03/20 amid a severe business environment such as NHI medical fee revisions and price negotiations with wholesalers but recovered to the 3% level in FY03/21 owing to growth of the Pharmaceuticals Network business and improved profitability of the Dispensing Pharmacy business.

1. Expand Pharmaceuticals Network business
2. Strengthen family pharmacy functions of company-run dispensing pharmacies
3. Grow generics drugs business
4. Enhance collaboration between group companies to provide community care functions needed under the community-based integrated care system as a group
5. Strengthen financial position

SG&A expenses

SG&A expenses (JPYmn)	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.
Salaries and allowances	2,806	6,364	7,489	9,266	10,406	12,088	12,481	13,467	14,195
Provision for employee bonuses	582	685	724	939	1,062	1,133	1,418	1,333	1,393
Retirement benefit expenses	88	172	195	264	329	361	466	457	596
Provision for directors' bonuses	32	64	68	76	55	47	35	33	41
Provision for directors' stock benefits					33	52	38	33	35
Taxes and dues	853	1,913	2,350	3,870	4,479	4,374	4,420	4,692	5,691
Depreciation	270	658	802	945	1,029	1,052	1,491	1,624	1,811
Amortization of goodwill	177	487	669	849	917	1,009	1,056	1,147	1,217
Other	2,142	5,509	6,612	7,537	8,486	9,630	9,559	15,827	16,648
Total SG&A expenses	7,603	17,365	20,646	25,835	29,018	32,050	33,444	35,842	38,599

Source: Shared Research based on company data

Extraordinary losses in excess of JPY400mn were booked in each of the three years between FY03/14–FY03/16; these were mainly impairment losses at pharmacies that failed to reach projected earnings. The company monitors the profitability of each pharmacy based on specific criteria and provides guidance when they are not met. If improvements are not made within a specified period of time, the company closes the pharmacy and sells off the business rights. In FY03/20, the company booked an impairment charge on fixed assets of existing stores and shares in acquired companies to reflect the impact of the spread of COVID-19.

Balance sheet

Balance sheet (JPYmm)	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.	FY03/21 Cons.
ASSETS										
Cash and deposits	2,072	2,092	3,106	2,499	2,081	2,252	10,201	11,703	11,722	10,118
Notes and accounts receivable	2,597	1,514	2,802	2,484	2,614	2,223	2,332	2,420	2,313	2,646
Inventories	1,796	2,219	2,732	3,846	3,431	4,053	3,520	4,297	4,452	4,408
Other	629	614	664	709	927	958	868	1,528	940	994
Allowance for doubtful accounts	-3	-6	-6	-7	-7	-10	-11	-12	-12	-12
Total current assets	8,902	8,271	10,941	11,023	10,783	11,098	18,736	21,055	20,578	19,313
Total tangible fixed assets	9,976	11,472	15,976	17,249	20,253	21,246	24,129	25,721	25,126	24,634
Total intangible assets	5,040	8,263	12,399	13,554	13,481	13,833	15,045	16,235	14,615	13,572
Investment securities		54	179	157	524	583	812	726	483	397
Long-term loans										
Other	2,728	2,771	3,645	3,631	3,838	4,008	4,066	5,217	5,686	6,549
Allowance for doubtful accounts	-43	-42	-26	-29	-33	-32	-31	-21	-26	-20
Investment and other assets	2,685	2,783	3,798	3,759	4,329	4,559	4,847	5,922	6,143	6,926
Total fixed assets	17,701	22,518	32,173	34,564	38,063	39,639	44,023	47,879	45,885	45,134
Total assets	26,603	30,789	43,114	45,587	48,847	50,737	62,759	68,935	66,464	64,448
LIABILITIES										
Notes and accounts payable	5,158	5,616	7,798	8,598	9,525	9,144	9,416	10,198	10,021	9,258
Short-term debt	3,856	5,119	12,922	9,214	6,910	3,863	7,463	9,158	8,905	10,210
Income taxes payable	582	459	578	599	1,065	413	1,135	695	454	1,556
Other	3,097	3,181	3,582	3,215	3,561	3,500	3,755	3,793	3,916	4,394
Total current liabilities	12,693	14,375	24,880	21,626	21,061	16,920	21,769	23,844	23,296	25,418
Long-term debt	7,029	8,758	10,948	15,391	14,859	20,186	26,329	29,739	28,653	22,348
Deferred tax assets	1	1	1	1	1	1				
Other	1,200	1,419	1,933	2,434	2,660	2,985	4,075	4,590	5,096	5,493
Total fixed liabilities	8,230	10,178	12,882	17,826	17,520	23,172	30,404	34,329	33,749	27,841
Total liabilities	20,923	24,553	37,762	39,452	38,581	40,092	52,174	58,173	57,045	53,260
NET ASSETS										
Capital stock	1,091	1,091	1,091	1,091	1,932	1,932	2,097	2,128	2,128	2,128
Capital surplus	924	901	901	901	1,742	1,742	1,160	1,185	1,183	1,182
Retained earnings	3,281	3,836	4,300	4,980	6,467	6,735	7,459	7,616	6,414	8,305
Treasury stock	0	-45	-1,181	-1,147	-328	-302	-275	-233	-206	-344
Valuation differences on securities	-5	3	2	11	15	49	143	83	-37	-24
Foreign currency translation adjustments										
Other	-52	-40	-31	-28	-17	23	52,316	58,239	56,945	53,154
Non-controlling interests	436	493	273	338	469	514	2	0	0	23
Total net assets	5,680	6,236	5,352	6,136	10,265	10,644	10,584	10,761	9,418	11,187
Total liabilities and net assets	26,603	30,789	43,114	45,588	48,846	50,736	62,759	68,935	66,464	64,448
Working capital	-765	-1,883	-2,265	-2,268	-3,480	-2,868	-3,564	-3,481	-3,256	-2,204
Total interest-bearing debt	10,885	13,877	23,870	24,605	21,769	24,049	33,792	38,897	37,558	32,558
Net debt	8,813	11,785	20,763	22,120	19,708	21,814	23,591	27,194	25,836	22,440

Source: Shared Research based on company data

Note: Figures may differ from company materials due to differences in rounding methods.

Assets: Assets expanded from 2012–13 on business growth

The company's business transformed in 2012–13, due in part to the formulation of its third medium-term plan. The company's consolidated subsidiary Pharmaholdings Co., Ltd., which operates dispensing pharmacies, entered a business alliance in December 2012 with Hanshin Dispensing Pharmacy Co., Ltd. (now equity-method subsidiary Hanshin Dispensing Holding Co., Ltd.). In July 2013, the two companies established a joint venture, H&M Co., Ltd. The main purpose of the joint venture was joint sourcing and distribution of pharmaceuticals, purchase of medical devices, and clearance of dead stock. H&M's chief goal is not to win pricing concessions from drug wholesalers as a result of buying power due to large-volume procurement, but to collaborate with drug wholesalers to set economically rational prices. This is the core objective of the company's Pharmaceuticals Network business.

Assets have continued to increase under the fourth medium-term plan and beyond. The company has sought to increase the number of dispensing pharmacies by M&A, but has carefully monitored the performance of pharmacies and booked impairment charges or disposed of those whose earnings have not improved. Under the fifth medium-term plan, assets have shrunk reflecting the impact of the COVID-19 pandemic since FY03/20. The company booked an impairment charge of JPY1.5bn in FY03/20. .

Liabilities: External financing

Liabilities rose during this period as the number of directly operated pharmacies increased in line with a rising network member count. The increase in current assets, which is working capital, was especially pronounced in FY03/14, when in addition to the increase in current assets, tangible fixed assets increased JPY4.5bn (+JPY2.5bn for buildings, +JPY1.9bn for land) and intangible fixed assets increased JPY4.1bn (JPY4.1bn increase in goodwill). Assets also increased in FY03/15 (buildings and structures +JPY237mn, land +JPY640mn, goodwill +JPY961mn). Growing demand for funds was met primarily through external financing. Short-term borrowings increased by about JPY7.0bn to JPY102.7bn in FY03/14, while long-term borrowings increased by about JPY4.5bn to JPY14.2bn in FY03/15 and has continued to gradually rise. Short- and long-term borrowings have been over JPY30.0bn since FY03/18. Profits increased in FY03/21 while interest-bearing debt declined YoY.

Net assets: Capital stock increase in FY03/16

The company increased capital and retired treasury stock in FY03/16, lifting the equity ratio in line with one of the third medium-term plan targets of achieving a ratio of 20% or higher. At the same time, management shored up the balance sheet through reducing short-term borrowing by JPY6.2bn YoY. Improving its financial position remains a key initiative of its fifth medium-term plan.

Cash flow statement

Cash flow statement (JPYmn)	FY03/12	FY03/13	FY03/14	FY03/15	FY03/16	FY03/17	FY03/18	FY03/19	FY03/20	FY03/21
	Cons.	Cons.	Cons.	Cons.	Cons.	Cons.	Cons.	Cons.	Cons.	Cons.
Cash flows from operating activities (1)	1,566	3,790	3,706	3,838	6,409	3,084	6,699	2,840	4,232	5,205
Pre-tax profit	1,298	1,907	1,770	2,294	3,479	1,906	2,293	1,422	22	3,967
Depreciation	354	841	1,077	1,209	1,362	1,594	1,491	1,624	1,811	1,859
Goodwill amortization	177	487	669	849	917	1,009	1,056	1,147	1,217	1,136
Change in accounts receivable	-325	1,739	382	935	191	812	496	500	285	-239
Change in inventories	8	-74	-173	-689	455	-472	759	-620	-140	72
Change in accounts payable	102	-558	365	-295	683	-765	-569	69	-328	-864
Cash flows from investing activities (2)	-1,248	-5,425	-7,559	-3,958	-5,040	-3,909	-6,848	-5,921	-2,383	-1,485
Purchase of tangible fixed assets	-805	-1,625	-4,180	-2,360	-3,674	-2,170	-4,050	-3,094	-1,351	-1,375
Purchase of intangible fixed assets	-1	-13	-44	-93	-273	-192	-190	-82	-107	-154
Purchase, sale, and redemption of investment securities	2	1	129	-267	-19	-39	-16	102	18	18
Change in loans (net of long- and short-term)	18	-245	-56	-106	-106	-38	-95	-3	-102	-233
Free cash flow (1+2)	318	-1,635	-3,853	-120	1,369	-825	-149	-3,081	1,849	3,720
Cash flows from financing activities	425	1,654	4,864	-483	-1,792	998	8,050	4,338	-1,687	-5,312
Change in short-term borrowings	1,293	685	7,255	-4,334	-2,314	-3,241	2,598	1,471	-505	0
Change in long-term borrowings	-489	1,846	-250	4,816	-896	5,292	7,292	3,701	-376	-4,634
Acquisition of treasury stock	0	-129	-1,155	1,005	0	0	0	0	0	0
Dividends paid	-162	-276	-221	-190	-229	-297	-297	-304	-305	0

Source: Shared Research based on company data

Note: Figures may differ from company materials due to differences in rounding methods.

Cash flows from operating activities

Cash flow from operating activities since FY03/12, when the accounting period was changed, has trended around JPY3.7bn–3.8bn, approximately half of which is derived from pre-tax profit, except for FY03/16–FY03/17 when profits fluctuated sharply. FY03/16–FY03/17 earnings were impacted by a number of temporary factors and a changing business environment owing to NHI drug price and dispensing fee revisions. The company notes temporary factors that boosted FY03/16 profits such as JPY242mn in gains from the sale of real estate, JPY100mn in subsidies for opening a serviced elderly housing facility, and a JPY90mn tax benefit from acquisition of subsidiary shares. The decline in FY03/17 profits was exacerbated by factors such as drug price and dispensing fee revisions, a winding down of major hepatitis C drug sales, and the absence of temporary factors that boosted FY03/16 profits. Operating cash flow in FY03/19 declined by half YoY owing to the April 2018 NHI price revision, but turned positive again in FY03/20 and FY03/21 as earnings recovered.

Depreciation and goodwill have been steadily increasing (except during the abbreviated accounting period) on business expansion owed to an upswing in the number of directly operated pharmacies, and this has had a positive impact on cash flow. Accounts receivable and accounts payable tend to fluctuate from year-end to year-end, showing no set pattern as the timing of receivable collections and the debt repayment period varies. Further, fiscal years with negative cash flow for inventory assets are common. We think this is due to the nature of Medical System Network's business of handling prescription drugs, which calls for the maintenance of sufficient inventories to avert shortage versus prescriptions.

Cash flows from investing activities

Cash flow from investing activities has been consistently negative for the 10 years through FY03/17 owing to a business expansion strategy that leverages alliances and M&A. The cash flow deficit from investing activities has been especially pronounced since the third medium-term plan was initiated in FY03/13. Prior to that, it was typically in the JPY1.0bn–3.0bn range, but then expanded to the JPY4.0bn–7.0bn range. In FY03/14, the company posted its largest cash flow deficit in 10 years, but this was mostly due to acquisition of tangible fixed assets: JPY4.2bn for serviced elderly housing facilities and land/buildings for new pharmacies and JPY4.2bn for shares acquired through M&A and from business transfers. Even in other fiscal years, the acquisition of land and buildings had a major impact on cash flow from investing activities—JPY3.7bn in FY03/16 and JPY3.1bn in JPY03/19, accounting for the bulk of the deficit in both years. The company commented that Wisteria Minami Ichijo would be the last elderly housing planning and development project for a while.

The company aims to make its network system an industry standard by expanding the number of affiliates and to improve the profitability of the Dispensing Pharmacy business, and these remain objectives of the fourth medium-term plan and fifth medium-term plan starting in FY03/19, which targets expansion of its network and improving profitability of the Dispensing

Pharmacy business. As the company continues to invest in business expansions, free cash flow has been negative since the start of the third medium-term plan, with the exception of FY03/16 when free cash flow turned positive due to temporary factors that sharply lifted profits, and FY03/20 and FY03/21, when there were few M&A deals.

Cash flows from financing activities

Financing will be indispensable as the company looks to continue expanding its business. In addition to using internal funds, the company raises funds through short- and long-term borrowing. We list the relatively large-scale financings of the past 10 years below. Most were short- and long-term borrowings, of which a large majority was for business expansion, such as purchase of real estate for new pharmacies and M&A.

In FY03/14, there was a JPY1.2bn cash flow deficit due to a share buyback accompanying the restructuring of an affiliated company. In FY03/16, cash flow saw a JPY2.8bn surplus as the company increased capital and sold treasury shares to improve its financial standing. Total borrowing also increased JPY5.2bn in FY03/19, but JPY3.9bn was invested in M&A, including the acquisition of Nagatomi Pharmacy. There were few M&A deals in FY03/20 and FY03/21 because the company prioritized improving profitability of existing stores.

Historical performance

Q3 FY03/21 earnings results (out February 5, 2021)

Overview

Consolidated results for cumulative Q3 FY03/21 (April–December 2020)

- ▷ Sales: JPY78.2bn (-1.0% YoY)
- ▷ Operating profit: JPY2.8bn (+125.8% YoY)
- ▷ Recurring profit: JPY2.8bn (+129.3% YoY)
- ▷ Net income*: JPY2.0bn (+517.5% YoY)

*Net income attributable to owners of the parent

- ▷ Business conditions and company initiatives: The Pharmaceuticals Network business recorded a steady increase in new network members. The Dispensing Pharmacy business saw a drop in the number of prescriptions filled owing to an increase in long-term prescriptions as the COVID-19 pandemic led to fewer medical examinations. The Community Pharmacy Network segment as a whole reported a 0.4% YoY fall in sales. Among other three businesses, sales also decreased YoY at the Leasing and Facility-related business and the Food Service business, and consolidated sales were down 1.0% YoY as a consequence.
- ▷ At the profit level, operating profit improved by 125.8% YoY. Within the Community Pharmacy Network segment, the Dispensing Pharmacy business registered profit growth on measures to promote the switch to generics, streamline operations, improve productivity, and reduce expenses. The Pharmaceuticals Network business also put up a solid performance, contributing to profit growth. Although the Leasing and Facility-related business experienced lower profit, the Food Service business and Other (home-visit nursing care) business both managed to rein in losses. All of the above combined to produce a sharp increase in companywide operating profit. YoY growth in net income attributable to owners of the parent expanded as the company booked extraordinary gains in connection with the sale of some shares in an equity-method affiliate in December 2020.

Breakdown of results by segment

Note: Reported sales and earnings at the segment level include intra-group sales and transfers between segments.

Community Pharmacy Network

This is a new segment that integrates the former Pharmaceuticals Network business, the Dispensing Pharmacy business, and the manufacture and market pharmaceuticals business (mainly Feldsenf Pharma) previously included in Other.

- ▷ Results for cumulative Q3 FY03/21 (April–December 2020)
- ▷ Segment sales: JPY74.4bn (-0.4% YoY)
- ▷ Segment profit: JPY4.3bn (+56.6% YoY)
- ▷ Pharmaceuticals Network: The number of new network members continued to increase, driven by the need for improved distribution efficiency. As of end-December 2020, network members numbered 5,745 (up 500 versus end-FY03/20), consisting of 413 directly operated pharmacies and 5,332 affiliates. As of end-January 2021, the number was 5,845; the company grew network member numbers by 100 in one month, despite increased competition.
- ▷ Dispensing Pharmacy: Reflecting the decline in medical examinations in the wake of the pandemic, the volume of long-term prescriptions increased while the number of prescriptions filled during the period was down. As the result of the decline in the number of prescriptions filled, growth in the drug charge per prescription (9.9%) exceeded growth in the technical fee per

prescription (4.1%). Consequently, on a companywide basis, the prescription unit price (comprised of the drug charge per prescription and technical fee per prescription) grew 8.6% YoY. Shared Research believes that profitability in the Dispensing Pharmacy business is improving, as following September 2020 revisions to the Pharmaceutical and Medical Device Act, the company has sought to streamline negotiations for procurement prices. In addition, it has worked to promote the switch to generics as an economic alternative with stable supply, streamline operations, optimize personnel deployment, and reduce overtime. As of end-December 2020, the group had 413 dispensing pharmacies, one care plan center, and nine cosmetics/drug stores.

- ▷ Manufacture and market pharmaceuticals business: This business aims to provide a stable supply of good-quality, low-priced generic drugs. As of end-December 2020, the company was selling 33 different ingredients and 66 products.
- ▷ Digital Shift: Spearheaded by subsidiary PharmaShift Co., Ltd., the Digital Shift business was established to promote digital transformation of dispensing pharmacies. When reporting earnings for cumulative Q3 FY03/21, the company disclosed results from a PharmaShift trial of the Family Pharmacy Support Service (utilizing an official LINE account) at 10 directly operated pharmacies. According to Medical System Network, results were even better than anticipated, with one in three pharmacy customers and roughly half of those using LINE agreeing to “friend registration.” The company also has organized a Digital Pharmacy Consortium comprising seven companies who will now progressively implement the Family Pharmacy Support Service across their pharmacy networks, with an initial goal of rolling out the service at 2,000 pharmacies by end-December 2021. With the aforementioned September 2020 revisions to the Pharmaceutical and Medical Device Act, pharmacists are now obliged to follow up with customers during drug use periods. For dispensing pharmacies, building closer relationships with patients is a pressing issue to be addressed.

Leasing and Facility-related

Results for cumulative Q3 FY03/21 (April–December 2020)

- ▷ Segment sales: JPY2.2bn (-17.5% YoY)
- ▷ Segment profit: JPY34mn (-49.3% YoY)
- ▷ The decline in sales and profit reflected pandemic-related postponements of certain construction projects; on the plus side, the company saw solid growth in leasing revenues and occupancy numbers at its serviced elderly housing facilities. As of end-December 2020, the company reported stable occupancy rates at three out of its five properties; as for the remaining two, at Wisteria Senri-Chuo it reported an occupancy rate of 76.8% (with 63 out of 82 units being occupied), and at Wisteria Minami Ichijo it reported an occupancy rate of 66.4% (with 77 out of 116 units being occupied). According to the company, Wisteria Senri-Chuo turned profitable in 1H and remained in the black in Q3 (October–December 2020). Wisteria Minami Ichijo remained in the red in Q3 as growth in occupancy stalled against the backdrop of the pandemic. Medical System Network plans to carry out sales activities targeting an occupancy rate of over 90% at all facilities. The company continues its marketing efforts aimed at getting its occupancy rate up to 90% by end-FY03/21 while taking all due precautions to prevent COVID-19 infections.

Food Service

Results for cumulative Q3 FY03/21 (April–December 2020)

- ▷ Segment sales: JPY1.9bn (-11.9% YoY)
- ▷ Segment loss: JPY2mn (versus loss of JPY38mn in cumulative Q3 FY03/20)

- ▷ Loss shrank: Sales fell as the COVID-19 pandemic led to a decline in the number of meals supplied and the company withdrew from unprofitable facilities. At the same time, though, the exit from unprofitable facilities caused losses to narrow, as did price negotiations and improvement in costs for food ingredients procurement.

Other

The main business is home-visit nursing care.

Results for cumulative Q3 FY03/21 (April–December 2020)

- ▷ Segment sales: JPY171mn (+40.2% YoY)
- ▷ Segment loss: JPY17mn (versus loss of JPY56mn in cumulative Q3 FY03/20)

1H FY03/21 earnings results (out November 6, 2020)

Overview

Consolidated results for 1H FY03/21 (April–September 2020)

- ▷ Sales: JPY51.0bn (-2.2% YoY)
- ▷ Operating profit: JPY1.4bn (+70.2% YoY)
- ▷ Recurring profit: JPY1.4bn (+78.2% YoY)
- ▷ Net income*: JPY578mm (+165.1% YoY)

*Net income attributable to owners of the parent

- ▷ Business conditions and company response: The Pharmaceuticals Network business recorded a steady increase in new affiliates, posting a sales increase of JPY359mn YoY, while the Dispensing Pharmacy business saw a drop in the number of prescriptions filled owing to fewer medical examinations as a result of the COVID-19 pandemic, resulting in sales declining JPY1.2bn. On the profit front, the Pharmaceuticals Network and Dispensing Pharmacy businesses contributed JPY342mn and JPY255mn respectively to profit growth; at the latter, mainly the shift to generic drugs and reductions to labor and other costs were more than sufficient to offset the adverse impact of lower prescription volumes.

Breakdown of results by segment

Note: Reported sales and earnings at the segment level include intra-group sales and transfers between segments.

Community Pharmacy Network

This is a new segment disclosed from FY03/20 that integrates the former Pharmaceuticals Network business, the Dispensing Pharmacy business, and the manufacture and market pharmaceuticals business (mainly Feldsenf Pharma) previously included in Other.

Results for 1H FY03/21 (April–September 2020)

- ▷ Segment sales: JPY48.5bn (-1.5% YoY)
- ▷ Segment profit: JPY2.4bn (+36.5% YoY)
- ▷ Pharmaceuticals Network division: The number of new affiliates continued to increase steadily in Q2 (July–September 2020), driven by strong needs for improved pharmaceutical distribution efficiency. As of end-September 2020, network members numbered 5,636 (+391 versus end-FY03/20), consisting of 409 directly operated pharmacies and 5,227 affiliated pharmacies, despite the loss of some major customers. The company launched the inventory management system Medisys VAN in Q2

FY03/21 and as of end-September 2020, the system, along with Drug VAN, had been adopted by 1,023 network members (+110 versus end-FY03/20; excludes directly operated pharmacies).

- ▷ Dispensing Pharmacy division: In 1H, dispensing fees were down 2.4% YoY for all pharmacies and down 3.4% on a comparable-store basis. Although the number of prescriptions filled is on a recovery trajectory, in 1H the number was down YoY due to the decline in medical exams in the wake of the pandemic. Prescription volumes in Q2 FY03/21 totaled 4.0mn (-10.8% YoY) for all pharmacies and 3.9mn (-11.6% YoY) on a comparable-store basis. Looking at monthly trends since April, the pace of decline was the fastest in May 2020 for both all pharmacies and on a comparable-store basis and has slowed during Q2 (July–September 2020). On the profit front, Shared Research thinks the division has reduced costs thanks to progress in efforts to lower labor and others costs at directly operated pharmacies and the switch to generic drugs. As of end-September 2020, the group had 409 dispensing pharmacies, one care plan center, and eight cosmetics/drug stores.
- ▷ Manufacture and market pharmaceuticals division: This business aims to provide a stable supply of good-quality, low-priced generic drugs. As of end-September 2020, the company was selling 32 different ingredients and 63 products. In 1H, the company reinforced marketing to affiliates.

Leasing and Facility-related

Results for 1H FY03/21 (April–September 2020)

- ▷ Segment sales: JPY1.4bn (-21.4% YoY)
- ▷ Segment profit: JPY16mn (-76.5% YoY)
- ▷ The decline in sales and profit reflected pandemic-related postponements of certain construction projects to 2H or later; on the plus side, the company saw solid growth in leasing revenues and occupancy numbers at its serviced elderly housing facilities. As of end-September 2020, the company reported stable occupancy rates at three of its five properties; as for the remaining two, at Wisteria Senri-Chuo it reported an occupancy rate of 81.7% (with 67 out of 82 units occupied), and at Wisteria Minami Ichijo it reported an occupancy rate of 62.1% (with 72 out of 116 units occupied). It seems all commercial units available for tenants have already been taken. The company plans to continue taking all due precautions to prevent novel coronavirus infections while continuing its marketing efforts aimed at getting its overall occupancy rate up to 90% by the end of the fiscal year.

Food Service

Results for 1H FY03/21 (April–September 2020)

- ▷ Segment sales: JPY1.2bn (-13.0% YoY)
- ▷ Segment loss: JPY13mn (versus loss of JPY34mn in 1H FY03/21)
- ▷ Loss narrowed: The decline in sales reflected the company's withdrawal from unprofitable facilities and a decline in the number of meals supplied in the catering service in the wake of the pandemic, but the company has reassessed costs such as food ingredients procurement.

Other

The main business is home-visit nursing care.

Results for 1H FY03/21 (April–September 2020)

- ▷ Segment sales: JPY110mn (+39.2% YoY)
- ▷ Segment loss: JPY13mn (versus loss of JPY39mn in 1H FY03/20)

Q1 FY03/21 earnings results (out August 7, 2020)

Overview

Q1 FY03/21 (April–June 2020) earnings results

- ▷ Sales: JPY25.2bn (-1.7% YoY)
- ▷ Operating loss: JPY61mn (profit of JPY334mn in Q1 FY03/20)
- ▷ Recurring loss: JPY62mn (profit of JPY323mn in Q1 FY03/20)
- ▷ Net loss*: JPY201mn (profit of JPY97mn in Q1 FY03/20)

*Net income/loss attributable to owners of the parent

- ▷ Company response and business conditions: Performance was strong at the core Community Pharmacy Network segment. The Pharmaceuticals Network business recorded a steady increase in new affiliates, while the Dispensing Pharmacy business saw a rise in the average value of prescriptions filled in tandem with growth in long-term prescriptions filled, but the number of prescriptions filled stagnated owing to fewer medical examinations as a result of COVID-19.

Segment performance

Community Pharmacy Network

This is a new segment that integrates the former Pharmaceuticals Network business, the Dispensing Pharmacy business, and the manufacture and market pharmaceuticals business (mainly Feldsenf Pharma) previously included in Other.

Q1 FY03/21 (April–June 2020) segment earnings results

- ▷ Segment sales: JPY23.9bn (-1.2% YoY; includes internal sales or transfers between segments; same hereafter)
- ▷ Segment profit: JPY434mn (-47.4% YoY)
- ▷ Pharmaceuticals Network division: The number of new affiliates continued to increase, driven by the need for improved distribution efficiency. As at end-June 2020, the number of network members was 5,617 (up 372 from end-FY03/20). This consisted of 415 directly operated pharmacies and 5,202 affiliates.
- ▷ Dispensing Pharmacy division: The average value of prescriptions filled rose in tandem with growth in long-term prescriptions and an increase in high-value prescriptions filled, but the number of prescriptions filled fell sharply due to fewer medical examinations as a result of COVID-19. As at end-June 2020, there were 415 dispensing pharmacies, one care plan center, and eight cosmetic/drug stores.
- ▷ Manufacture and market pharmaceuticals division: This business aims to provide a stable supply of good-quality, low-priced generic drugs. The company sold 29 ingredients and 60 products as of end-June 2020.

Leasing and Facility-related

Q1 FY03/21 (April–June 2020) segment earnings results

- ▷ Segment sales: JPY723mn (-5.0% YoY)
- ▷ Segment profit: JPY6mn (loss of JPY8mn in Q1 03/20)
- ▷ The reason for lower sales and profit improvement: Although leasing revenue and rise in occupancy at the company's serviced elderly housing facilities were generally brisk, the postponement of some construction projects associated with COVID-19 contributed to the sales decline. The number of occupied units as of end-June 2020 was 67 out of 82 units total (occupancy rate: 81.7%) at Wisteria Senri-Chuo, and 73 out of 116 units total (occupancy rate: 62.9%) at Wisteria Minami Ichijo. The company is carrying out sales activities that take into account measures to prevent the spread of COVID-19 toward achieving its target occupancy rates of 90%.

Food Service

Q1 FY03/21 (April–June 2020) segment earnings results

- ▷ Segment sales: JPY612mn (-16.2% YoY)
- ▷ Segment loss: JPY19mn (loss of 12mn in Q1 FY03/20)
- ▷ Loss expands: Withdrawal from certain unprofitable facilities and a decrease in the number of meals supplied due to COVID-19 hurt profits.

Other

The main business is home-visit nursing care.

Q1 FY03/21 (April–June 2020) segment earnings results

- ▷ Segment sales: JPY51mn (+34.2% YoY)
- ▷ Segment loss: JPY11mn (loss of JPY21mn in Q1 FY03/20)

Full-year FY03/20 earnings results (out May 8, 2020)

Overview

FY03/20 (April 2019 to March 2020) earnings results

- ▷ Sales: JPY105.2bn (+7.1% YoY)
- ▷ Operating profit: JPY1.6bn (+13.0% YoY)
- ▷ Recurring profit: JPY1.6bn (+3.9% YoY)
- ▷ Net loss*: JPY895mn (profit of JPY462mn)

*Net income/loss attributable to owners of the parent

- ▷ Business environment: NHI drug price and dispensing fee revisions were conducted in April 2018. Dispensing pharmacies had to streamline their management structures following the implementation of the MHLW's "Guidelines for the Improvement of Commercial Transaction Practices of Ethical Drugs," whose purpose was to ensure stable supply of ethical drugs.
- ▷ Company response and business conditions: Performance was strong at the core Community Pharmacy Network segment, fueled by steady expansion in the Pharmaceuticals Network business and contributions to the Dispensing Pharmacy business from pharmacies acquired in FY03/19 via M&A. There was also a rise in the average value of prescriptions filled in tandem with growth in long-term prescriptions and an increase in high-value prescriptions filled, which contributed to sales. However, since January 2020, the number of prescriptions filled stagnated owing to fewer medical examinations as a result of the spread of COVID-19 and a low rate of influenza transmission compared to previous years. As a result, the number of prescriptions filled was fewer than expected at the Dispensing Pharmacy business, which weighed on profits.
- ▷ The company posted a net loss, because it booked a JPY1.5bn impairment loss consisting mainly of a JPY1.3bn charge on fixed assets of stores whose profitability had deteriorated in the Dispensing Pharmacy business and goodwill of acquired subsidiaries, and a JPY112mn charge related to the Food Service business. Shared Research thinks that the increased impairment loss is due in part to preparing ahead for a worsening business environment due to the spread of COVID-19.

Segment performance

Community Pharmacy Network

This is a new segment that integrates the former Pharmaceuticals Network business, the Dispensing Pharmacy business, and the manufacture and market pharmaceuticals business (mainly Feldsenf Pharma) previously included in Other.

Full-year FY03/20 (April 2019 to March 2020) segment earnings results

- ▷ Segment sales: JPY99.6bn (+7.9% YoY; includes internal sales or transfers between segments; same hereafter)
- ▷ Segment profit: JPY3.7bn (+13.0% YoY)
- ▷ Pharmaceuticals Network division: The number of new affiliates showed a strong increase driven by the need for improved distribution efficiency. As at end-March 2020, the number of network members was 5,245 (up 1,455 from end-FY03/19). This consisted of 416 directly operated pharmacies and 4,829 affiliates. Membership has been increasing steadily amid worsening business conditions for dispensing pharmacies, such as annual NHI drug price revisions and price negotiations with wholesalers.
- ▷ Dispensing Pharmacy division: In addition to the contribution from stores acquired via M&A, sales at existing pharmacies remained steady. However, the number of prescriptions filled slowed in Q4 due to the effects of the COVID-19 outbreak, such as a drop in customer traffic (associated with an increase in long-term prescriptions) and a reduction in the number of influenza patients as a result of rigorous antivirus measures to prevent the spread of COVID-19. Accordingly, Q4 saw a rise in the price per prescriptions due to the increase in long-term prescriptions, but the number of prescriptions filled turned down. This was reflected in solid sales, but difficulty in adding value such as technical fees charged per prescription, which led to lower profits. Overall, the company's sales surpassed the initial forecast, but OPM was 0.9pp lower than expected. As at end-March 2020, there were 416 dispensing pharmacies, one care plan center, and eight cosmetic/drug stores.
- ▷ Manufacture and market pharmaceuticals division: This business aims to provide a stable supply of good-quality, low-priced generic drugs. The company sold 23 ingredients and 51 products as of end-March 2020.

Leasing and Facility-related

Full-year FY03/20 (April 2019 to March 2020) segment earnings results

- ▷ Segment sales: JPY3.4bn (+3.2% YoY)
- ▷ Segment profit: JPY45mn (loss of JPY84mn in FY03/19)
- ▷ The reason for sales and profit growth: Steady inflow of leasing revenue and rise in occupancy at the company's serviced elderly housing facilities contributed to earnings growth. The number of occupied units as of end-March 2020 was 67 out of 82 units total at Wisteria Senri-Chuo, and 71 out of 116 units total at Wisteria Minami Ichijo. The number of occupied units is trending up, and the company continues to carry out aggressive sales activities targeting an occupancy rate of over 90%.

Food Service

Full-year FY03/20 (April 2019 to March 2020) segment earnings results

- ▷ Segment sales: JPY2.8bn (-11.5% YoY)
- ▷ Segment loss: JPY43mn (profit of 34mn in FY03/19)
- ▷ Business reforms: Despite withdrawal from certain unprofitable facilities and pricing adjustments made to contracts, segment profit fell from higher labor costs as the company employed temporary resources in response to staff shortage. The company booked a JPY112mn impairment loss in FY03/20.

Other

The main business is home-visit nursing care.

Full-year FY03/20 (April 2019 to March 2020) segment earnings results

- ▷ Segment sales: JPY165mn (+17.1% YoY)
- ▷ Segment loss: JPY71mn (loss of JPY101mn in FY03/19)

Other information

History

Date	Description
Sep 1999	Established Medical System Network (capital stock: JPY10mn) in Chuo Ward, Sapporo, to streamline hospital operation and pharmaceuticals distribution
Mar 2002	Registered shares on Osaka Stock Exchange NASDAQ Japan market (now JASDAQ)
Dec	Acquired 100% of Pharmaholdings and Nihon Leben shares, making them wholly owned subsidiaries
Feb 2005	Established joint venture MM Net with Mitsui & Co. (capital JPY200mn, Medical System Network held 51% equity stake, but dissolved alliance and absorbed MM Net in 2013)
Oct	Pharmaholdings acquired 100% of Sunmedic Co., Ltd. (now Nanohana East Japan Co., Ltd.) shares, making it a wholly owned subsidiary
	Pharmaholdings acquired 100% of Hankyu Kyoei Pharmacy (now Kyoei Pharmacy) shares, making it a wholly owned subsidiary
Jan 2007	Acquired 100% of CR Medical (now Nanohana Central Co., Ltd.), making it a wholly owned subsidiary
Mar	Acquired 100% of Hokkaido Hiclips (now SMO-MDS) shares, making it a wholly owned subsidiary
Sep 2008	Listed shares on the Second Section of the Tokyo Stock Exchange
Jun 2010	Listed shares on the First Section of the Tokyo Stock Exchange
Nov 2012	Formed business alliance with Hanshin Dispensing Pharmacy (switched to alliance with parent Hanshin Pharmacy Holdings when the holding company was established in December 2012)
May 2013	Formed business alliance with FamilyMart
Jul	Pharmaholdings and Hanshin Dispensing Holdings established joint venture, H&M Co.
Nov	Pharmaholdings acquired 98.96% of Total Medical Service shares through public tender offer, making it a subsidiary
Jan 2015	Concluded comprehensive strategic alliance with Fuyo General Lease Co., Ltd
Mar	Formed business alliance with Sogo Clinical Holdings (now EP-Sogo)
Apr	Formed business alliance with EM Systems
May	Concluded capital tie-up with Sogo Clinical Holdings (now EP-Sogo)
Jun	Formed business alliance with Yakuju Corporation
May 2016	Pharmaholdings acquired 100% of Home-Visit Nursing Care Station Himawari Co. shares and entered home-visit nursing care business
Oct	Formed business alliance with Zoo Corporation
Jan 2017	Formed business alliance with Career Brain
May	Formed business alliance with Okura Information System
Jun	Sold shares of SMO-MDS (no longer a subsidiary)
Oct	Absorbed subsidiaries System Four, Pharmaholdings, and Nihon Leben
Jan 2018	Acquired all shares in Apotec and made it a wholly owned subsidiary
	Formed business alliance with Polaris Co., Ltd.
Feb	Feldsenf Pharma Co., Ltd. formed business alliance with Daito Pharmaceutical Co., Ltd.
Jun	Feldsenf Pharma Co., Ltd. started sales of generic drugs
Jan 2019	Acquired all shares in Nagatomi Pharmacy Corporation and made it a wholly owned subsidiary
Apr	Acquired A-system Co., Ltd. in an absorption-type merger
Feb 2020	Dissolved H&M Co., Ltd, terminating business tie-up with I&H Co., Ltd.
Oct	Established PharmaShift Co., Ltd., a joint venture with Opt, Inc.

Source: Shared Research based on company data (as of March 2021)

News and topics

February 2021

On February 5, 2021, the company announced revisions to its full-year earnings forecast.

Revised full-year FY03/21 consolidated earnings forecast

▷ Sales:	JPY103.0bn (previous forecast: JPY103.0bn)
▷ Operating profit:	JPY3.4bn (JPY2.5bn)
▷ Recurring profit:	JPY3.4bn (JPY2.5bn)
▷ Net income*:	JPY2.0bn (JPY1.4bn)
▷ EPS:	JPY65.94 (JPY45.50)

*Net income attributable to owners of the parent

Reasons for revision

The company revised up its profit estimates at all levels, because profitability of its core Community Pharmacy Network segment is likely to be better than expected. In cumulative Q3, the total value of drug orders by network members were ahead of forecast in the Community Pharmacy Network segment, and although the number of prescriptions filled declined as expected in the Dispensing Pharmacy business, the price per prescription trended higher than expected. The company also made more progress than expected in group-wide efforts to streamline operations, improve productivity, and cut costs through rigorous control of expenses. All of these factors contributed to the upward revision of profit estimates.

On the same day, the company announced an additional contribution to its Board Benefit Trust (BBT).

At the Board of Directors meeting held on the same day, the company resolved to contribute additional funds to its Board Benefit Trust (BBT). The additional contribution is summarized below (see company press release for details).

- 1) Date of additional contribution to BBT: February 19, 2021 (planned)
- 2) Amount of additional contribution: JPY120mn
- 3) Type of shares to be acquired: Common stock issued by the company
- 4) Period when shares are acquired: February 19–April 22, 2021 (planned)
- 5) Method of acquiring shares: Open market purchase

December 2020

On December 15, 2020, the company announced the recording of extraordinary gains (gains from the sale of shares in an affiliate) and revisions to its full-year consolidated earnings forecast.

At the Board of Directors meeting held the same day, the company resolved to sell a portion of its shareholding in Genex Inc. (headquartered in Nagoya, Aichi Prefecture; hereinafter, Genex), an affiliate not accounted for by the equity method. It expects to record gains from the sale of shares in the affiliate as extraordinary gains in Q3 FY03/21 parent and consolidated results.

Reason for the share transfer

Medical System Network invested in Genex in December 2015 with the aim to strengthen its purchasing power, build a logistics system, and improve distribution efficiency in generic drugs. Under the terms of the investment, Genex supplied generic drugs to the group's directly operated pharmacies and pharmaceuticals network affiliates. Genex now wishes to accept the management participation of a fund run by private equity company J-STAR Co., Ltd. (headquartered in Chiyoda-ku, Tokyo), in order to further raise its enterprise value and take measures toward listing on the stock exchange in the future. To realize this, Genex asked Medical System Network whether it could purchase a portion of the Genex shares held by Medical System Network. The company agreed to the request after carefully considering Genex's management plan and the effects of the change in its

capital policy. Further, the company concluded that there would be no significant change in its business relationship with Genex and that the favorable collaborative relationship between the two companies would be maintained following the transfer.

As a result of the above share transfer, Genex will be excluded from the company's scope of an affiliate not accounted for by the equity method. Medical System Network will record extraordinary gains from the transfer and has revised its forecast for full-year FY03/21 accordingly, as shown below.

Revised full-year FY03/21 consolidated earnings forecast

Sales:	JPY103.0bn (previous forecast: JPY103.0bn)
Operating profit:	JPY2.5bn (JPY2.5bn)
Recurring profit:	JPY2.5bn (JPY2.5bn)
Net income*:	JPY1.4bn (JPY750mn)
EPS:	JPY45.50 (JPY24.73)

*Net income attributable to owners of the parent

November 2020

On November 6, 2020, the company announced a revised forecast for the full-year FY03/21.

Revised full-year FY03/21 consolidated earnings forecast

Sales:	JPY103.0bn (previous forecast: JPY103.5–105.5bn)
Operating profit:	JPY2.5bn (JPY1.2–2.2bn)
Recurring profit:	JPY2.5bn (JPY1.1–2.1bn)
Net income*:	JPY750mn (no forecast given previously)
EPS:	JPY24.73 (no forecast given previously)

*Net income attributable to owners of the parent

Reasons for revision

At the time of its FY03/20 results announcement on May 8, 2020, the company issued range estimates for FY03/21 sales, operating profit, and recurring profit, explaining that it did not have a good basis at that time on which to make more precise estimates as to how much the COVID-19 pandemic would impact full-year earnings. Although exactly when the pandemic will come to an end remains to be seen, with the first six months of the fiscal year in the rearview mirror and more data in hand, the company has been able to fine-tune its projections and revise its forecast based on this new information.

The main impetus for the revision at this time is the Dispensing Pharmacy business, where the company had initially expected to see the worst of the pandemic-driven downturn (resulting from cutbacks in patient exams at hospitals among other factors) no later than July, with performance then gradually recovering from there. However, the company sees the fallout from the pandemic lingering through the end of the fiscal year, and with this weighing on its performance, does not expect the recovery it is currently seeing to take this business back to where it was last year. With prescriptions related to the flu, hay fever, and other types of seasonal maladies also expected to be down this year, the company sees consolidated sales for the full year coming in below the lower end of its initial range estimate. In contrast, the company sees full-year earnings coming in above the upper end of its initial range estimate, owed to its promotion of the shift to generic drugs (which have the advantage of being affordable and can be reliably procured) and accelerated efforts to increase worker productivity and cut costs through optimal staff allocation and reductions in overtime.

September 2020

On September 28, 2020, the company announced that it had signed an agreement to establish a joint venture with OPT, Inc.

The company announced that it had signed an agreement to establish a joint venture with OPT, Inc. (core subsidiary of Digital Holdings, Inc. [TSE1: 2389]). The purpose of the joint venture is to create a new pharmaceutical platform suited for the digital age by maximizing use of the two companies' management resources.

The joint venture is to be established on October 1, 2020 and scheduled to begin services in January 2021. Details are as follows:

- ▷ Company name: PharmaShift Co., Ltd.
- ▷ Location: Minato-ku, Tokyo
- ▷ Main business: Family pharmacy support business
- ▷ Capital: JPY50mn
- ▷ Shareholding: Medical System Network 51.0%, RePharmacy (wholly owned subsidiary of OPT) 49.0%

The three main business objectives of the joint venture are as follows:

- 1) Provide means for stress-free communication between patients and dispensing pharmacies and integrate medical information provided by patients by using official LINE account
- 2) Support pharmacies in strengthening their family pharmacy functions and streamlining their businesses so that they can enhance non-dispensing services such as health and diet counseling
- 3) In the longer term, improve the efficiency of healthcare and augment the value of dispensing pharmacies by integrating information gained by pharmacies strengthening their family pharmacy functions and building an information platform shared by other medical professionals such as doctors, as well as professionals in other fields

The impact of this joint venture on the company's FY03/21 forecasts is unknown at this stage.

August 2020

On August 17, 2020, the company announced that its subsidiary Feldsenf Pharma obtained approval to manufacture and market generic drugs.

The company announced that as of the same day, its consolidated subsidiary Feldsenf Pharma Co., Ltd. (headquartered in Sapporo, Hokkaido) obtained approval to manufacture and market one generic drug API and three products (pregabalin orally disintegrating [OD] tablets 25mg/75mg/150mg). See the company press release for details.

July 2020

On July 15, 2020, the company announced the launch of inventory management system Medisys VAN.

The company announced it will promote its own branded version (Medisys VAN) of Okura Information System Co., Ltd.'s (headquarters: Marugame, Kagawa Prefecture) drug inventory management system Drug VAN to its pharmaceuticals network affiliates.

Drug VAN is a long-established (commercialized for over 15 years) system with an installed base of 3,000 users that has been continuously upgraded to reflect user requests. The company notes the system will streamline pharmacy operations through additional functions such as automatic calculation of optimized inventory corresponding to medical billing data, automated ordering, and inventory information sharing among multiple pharmacies.

Medisys VAN is the company's pharmaceuticals network service that incorporates the company's patented dead stock exchange (slow moving inventory clearance service) and generic drug recommendation functions. Affiliate pharmacy owners are the target users. Adoption of the company's system will help optimize overall network inventory management and streamline drug distribution through reduced frequency of returns and emergency deliveries and expansion of drug inventory sharing among affiliates.

June 2020

On June 19, 2020, the company announced the launch of sales of generic drugs (five ingredients and eight products) by consolidated subsidiary Feldsenf Pharma Co., Ltd.

The company announced that consolidated subsidiary Feldsenf Pharma began selling five generic drug APIs and eight products from June 19, 2020, the date NHI drug prices applied.

On the same day, the company announced management changes at its consolidated subsidiaries.

The company announced changes to representative directors at its consolidated subsidiaries Paltecno Co., Ltd. and Feldsenf Pharma Co., Ltd.

1. Paltecno Co., Ltd. (effective June 11, 2020)

Name:	New position	Current position
Tatsushi Muraoka	Chairman	President
Fumitaka Nakamura*	President	-

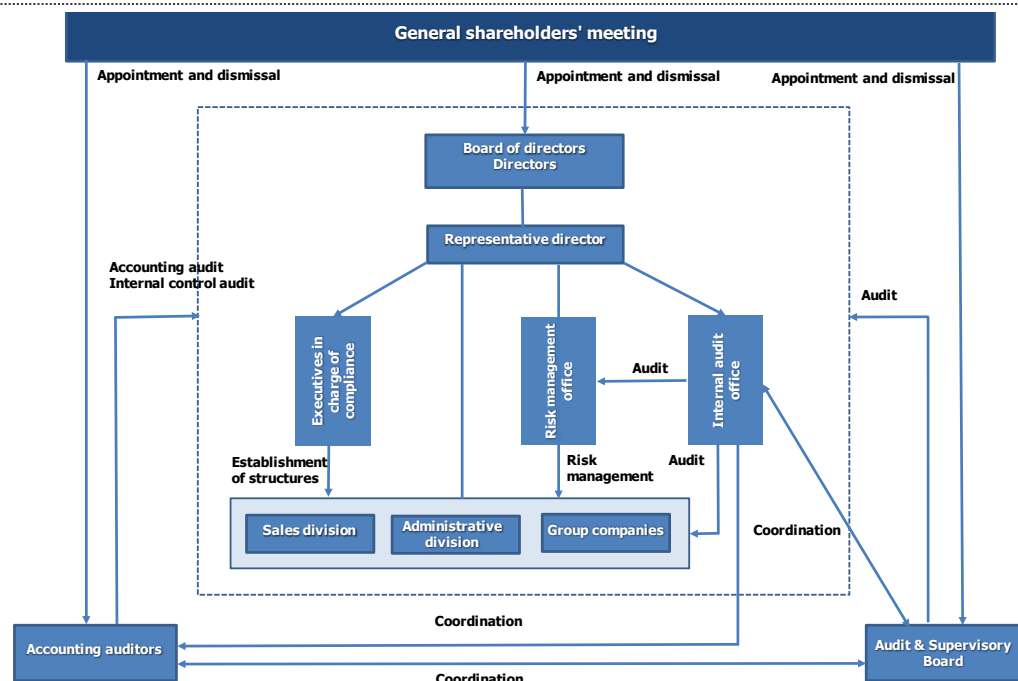
* Also serves as General Manager of Project Promotion Office at Medical System Network

2. Feldsenf Pharma Co., Ltd. (effective June 18, 2020)

Name:	New position	Current position
Inao Tajiri*	Chairman	President
Kiwamu Nakada	President	Director

*Also serves as President of Medical System Network

Corporate governance and top management



Source: Shared Research based on company data

Top management

President and director (Representative Director) Inao Tajiri

Mar 1974	Joined Ichino Yamagata Pharmaceutical Co., Ltd.
Jan 1981	Joined Medical Yamagata Pharmaceutical Co., Ltd.
Nov 1989	Representative director of Medical Yamagata Pharmaceutical Co., Ltd.
Jun 1991	Director of Akiyama Aiseikan Co., Ltd. (now Suzuken Co., Ltd)
Sep 1999	Established Medical System Network and became representative director and president (current)
Apr 2000	President (current) of Social Welfare Corporation Nomad-Fukushikai
Dec 2004	Representative director of Nihon Leben Co., Ltd.
Feb 2005	Representative director of MM Net Co., Ltd.
Apr 2013	President and representative director of SMO-MDS Co., Ltd.
Jul 2013	Vice president and representative director of H&M Co., Ltd.
Jun 2015	President and representative director of H&M Co., Ltd.
Jan 2016	President of Social Welfare Corporation Hokushikai
Sep 2016	President and representative director of Feldsenf Pharma Co., Ltd.
Jun 2020	President and representative director (current) of Feldsenf Pharma Co., Ltd.

Source: Shared Research based on company data (as of June 2020)

Corporate governance

The company recognizes the importance of legal compliance and corporate ethics, and aims to continuously enhance corporate value through rapid decision-making and improved management soundness. While looking to aggressively expand its business in line with growth of the overall medical market, Medical System Network is aware of the importance of ensuring a fair management system and accordingly maintains a flexible meeting of the board of directors, has developed a system to monitor business execution, and has enhanced internal controls. The company further recognizes that management of subsidiaries is especially crucial to internal control, and thus aims to enhance corporate governance by ensuring thorough compliance, building a risk management system, and establishing a system for reporting financial and other important matters.

Board of directors

A board of directors with 14 members (including three outside directors) was established as the decision-making body. Regular board meetings are held monthly and extraordinary meetings are also conducted as needed. The company adopted an executive officer system in June 2017, and developed a system to enhance and clearly separate management decision-making, management oversight, and business execution functions.

Board of auditors

The board of auditors is comprised of three members (two full-time corporate auditors and one part-time) and meets once monthly in addition to extraordinary meetings as needed. Two of the three members are outside auditors.

Compliance

Management has established the Medical System Network Group Charter of Corporate Behavior, a Code of Conduct for corporate ethics and compliance, and the basic regulations to clarify the company's basic stance on corporate ethics and compliance. The company appoints an officer in charge of compliance as stipulated in its group compliance basic regulations, under whose supervision a compliance department has been established to develop a compliance system for the group.

Risk management

The company has established an organization and management system based on Medical System Network Group Risk Management Basic Rules that enables efficient execution of duties through the clarification of directors' authorities and responsibilities. Discussions of important matters by each group company's board of directors are held after preliminary consultations with the company. In addition, appropriate management control of subsidiaries is conducted in accordance with management regulations for affiliated companies. Reports of business results, financial status, and important matters are received at regularly scheduled Board of Directors and other important meetings. A system is in place for the prompt reporting of serious risk factors such as compliance violations.

Internal and corporate audits

The Internal Audit Office is in charge of internal auditing and its manager is responsible for drafting the basic internal audit plan prior to the start of the fiscal year, obtaining approval by the President and Representative Director, and formulating an implementation agenda based on the basic internal audit plan. Three corporate auditors (including two outside auditors) attend regular and extraordinary meetings of the board of directors to observe the performance of duties by company officers such as directors and Internal Audit Office managers as part of a system to audit performance of directors and the status of internal controls. Auditing efficiency is further enhanced through mutual cooperation and information-sharing with the accounting auditor and the Internal Audit Office.

Dividend policy

The company's basic policy on dividends is to maintain stable disbursements to shareholders in line with earnings while retaining sufficient internal reserves to reinforce its financial position, expand business operations, and develop human resources. Since FY03/13, dividends have been paid twice a year—an interim dividend and a fiscal year-end dividend. The dividend decision-making bodies are the general shareholders meeting for year-end dividends and the board of directors for interim dividends. The articles of incorporation stipulate the board of directors has the authority to decide on interim dividends through a resolution.

Major shareholders

Top shareholders	Shares held	Shareholding ratio
KBL EPB S.A. 107704 (Standing proxy: Mizuho Bank, Ltd. Settlement Dept.)	3,528,800	11.51%
S&S G.K.	2,769,100	9.03%
Yasuyuki Okinaka	2,506,000	8.17%
Jiro Akino	2,218,800	7.24%
Japan Trustee Services Bank, Ltd. (Trust Account)	1,748,600	5.70%
The Master Trust Bank of Japan, Ltd. (Trust Account)	1,326,400	4.32%
EP-Sogo Co., Ltd.	800,000	2.61%
Inao Tajiri	689,900	2.25%
Medical System Network Employees Stockholding Association	609,500	1.98%
Yoshiaki Homma	400,100	1.30%
SUM	16,597,200	54.16%

Source: Shared Research based on company data (as of March 31, 2020)

Employees

Segment	No. of employees	No. of temporary employees	Total
Pharmaceuticals Network	2,755	466	3,221
Pharmacists	1,315	283	1,598
Leasing and Facility-related	116	17	133
Food Service	192	310	502
Other	25	10	35
Corporate (administration)	117	8	125
Total	3,205	812	4,017

Source: Shared Research based on company data (as of March 31, 2020)

Note: The sum of temporary employees does not equal to the total due to differences in rounding methods (based on eight-hour work days).

Profile

Company Name	Head Office
Medical System Network Co., Ltd.	24-3 Kitajuno-Nishi, Chuo-ku, Sapporo, Hokkaido
Phone	Exchange Listing
+81-11-612-1069	First Section of the Tokyo Stock Exchange
Established	Listed On
September 1999	June 2010
Website	Fiscal Year-End
http://www.msnw.co.jp/	March
IR Contact	IR Web
Corporate Planning Department	https://www.msnw.co.jp/ir/

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Ai Holdings Corporation	Elecom Co., Ltd.	Kumiai Chemical Industry Co., Ltd.	SANIX INCORPORATED
AI inside Inc.	en Japan Inc.	Lasertec Corporation	Sanrio Company, Ltd.
AirTrip Corp.	Estore Corporation.	Locondo, Inc.	SATO HOLDINGS CORPORATION
and factory, inc.	euglena Co., Ltd.	LUCKLAND CO., LTD.	SBS Holdings, Inc.
ANEST IWATA Corporation	FaithNetwork Co., Ltd.	Marumae Co., Ltd.	Seikagaku Corporation
AnGes Inc.	Ferrotec Holdings Corporation	MATSUI SECURITIES CO., LTD.	Seria Co.,Ltd.
Anicom Holdings, Inc.	FIELDS CORPORATION	Media Do Co., Ltd.	Serverworks Co.,Ltd.
Anritsu Corporation	Financial Products Group Co., Ltd.	Medical System Network Co., Ltd.	SHIFT Inc.
Apaman Co., Ltd.	First Brothers Col, Ltd.	MEDINET Co., Ltd.	Shikigaku Co., Ltd
ARATA CORPORATION	FreeBit Co., Ltd.	MedPeer, Inc.	SHIP HEALTHCARE HOLDINGS, INC.
Artspark Holdings Inc.	Gamecard-Joyco Holdings, Inc.	Mercuria Investment Co., Ltd.	SIGMAXYZ Inc.
AS ONE CORPORATION	GameWith, Inc.	Metaps Inc.	SMS Co., Ltd.
Ateam Inc.	GCA Corporation	Micronics Japan Co., Ltd.	Snow Peak, Inc.
Aucfan Co., Ltd.	Good Com Asset Co., Ltd.	MIRAIT Holdings Corporation	Solasia Pharma K.K.
AVANT CORPORATION	Grandy House Corporation	Monex Goup Inc.	SOURCENEXT Corporation
Axell Corporation	GIG Works Inc.	MORINAGA MILK INDUSTRY CO., LTD.	Space Value Holdings CO., LTD
Azbil Corporation	Hakuto Co., Ltd.	Mortgage Service Japan Limited.	Star Mica Holdings Co., Ltd.
AZIA CO., LTD.	Hamee Corp.	MRT Inc.	Strike Co., Ltd.
AZoom, Co., Ltd.	Happinet Corporation	NAGASE & CO., LTD	Sunnexa Group Inc.
Base Co., Ltd	Harmonic Drive Systems Inc.	NAIGAI TRANS LINE LTD.	Symbio Pharmaceuticals Limited
BEELOS Inc.	HENINGE K.K.	NanoCarrier Co., Ltd.	Synchro Food Co., Ltd.
Bell-Park Co., Ltd.	Hosokawa Micron Corporation	Net Marketing Co., Ltd.	TAIYO HOLDINGS CO., LTD.
Benefit One Inc.	Hope, Inc.	Net One Systems Co.,Ltd.	Takashimaya Company, Limited
B-lot Co.,Ltd.	HOUSEDO Co., Ltd.	Nichi-Iko Pharmaceutical Co., Ltd.	Take and Give Needs Co., Ltd.
Broadleaf Co., Ltd.	H2O Retailing Corporation	NIHON CHOUZAI Co.,Ltd.	TEAR Corporation
CanBas Co., Ltd.	IDOM Inc.	Nihon Denkei Co., Ltd.	Tenpo Innovation Inc.
Canon Marketing Japan Inc.	IGNIS LTD.	Nippon Commercial Development Co., Ltd.	3-D Matrix, Ltd.
Career Design Center Co., Ltd.	i-mobile Co.,Ltd.	Nippon Koei Co., Ltd.	The Hokkoku Bank,Ltd.
Carna Biosciences, Inc.	Inabata & Co., Ltd.	NIPPON PARKING DEVELOPMENT Co., Ltd.	TKC Corporation
CARTA HOLDINGS, INC	Infocom Corporation	NIPRO CORPORATION	TKP Corporation
CERES INC.	Infomart Corporation	Nisshinbo Holdings Inc.	Tsuzuki Denki Co., Ltd.
Chiyoda Co., Ltd.	Intelligent Wave, Inc.	Nisso Corporation	TOCALO Co., Ltd.
Chori Co., Ltd.	ipet Insurance CO., Ltd.	NS TOOL CO., LTD.	TOKAI Holdings Corporation
Chugoku Marine Paints, Ltd.	Itochu Enex Co., Ltd.	OLBA HEALTHCARE HOLDINGS,Inc.	Tokyu Construction Co., Ltd.
cocokara fine Inc.	ItoKuro Inc.	OHIZUMI MFG. CO., LTD.	TOYOBO CO., LTD.
COMSYS Holdings Corporation	JAFCO Co.,Ltd.	Oisix ra daichi Inc.	Toyo Ink SC Holdings Co., Ltd
COTA CO.,LTD.	JMDC Inc.	Ok Electric Industry Co., Ltd	Toyo Tanso Co., Ltd.
CRE, Inc.	JSB Co., Ltd.	ONO SOKKI Co., Ltd.	Tri-Stage Inc.
CREEK & RIVER Co., Ltd.	JTEC Corporation	ONWARD HOLDINGS CO.,LTD.	TSURUHA Holdings
Daichi Kigenso Kagaku Kogyo Co., Ltd.	J Trust Co., Ltd	Pan Pacific International Holdings Corporation	VISION INC.
Daiki Axis Co.,Ltd.	Japan Best Rescue System Co., Ltd.	PARIS MIKI HOLDINGS Inc.	VISIONARY HOLDINGS CO., LTD.
Daiseki Co., Ltd.	JINS HOLDINGS Inc.	PCA CORPORATION	V-cube,Inc.
Daiwabo Holdings Co.,Ltd.	JP-HOLDINGS, INC.	PIGEON CORPORATION	World Holdings Co., Ltd.
Demae-Can CO., LTD	KAMEDA SEIKA CO., LTD.	P3, inc.	YELLOW HAT LTD.
DIC Corporation	Kanamic Network Co.,LTD	QB Net Holdings Co., Ltd.	YOSHINOYA HOLDINGS CO., LTD.
Digital Arts Inc.	KANEMATSU CORPORATION	RACCOON HOLDINGS, Inc.	ZAPPALLAS, INC.
Digital Garage Inc.	kaonavi, inc.	Raysum Co., Ltd.	

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