

BIPROGY Inc.
Earnings Announcement
for the First Quarter of the Fiscal Year Ending March 2023
held on August 3, 2022

Principal Questions and Answers

(with certain details modified in an attempt to provide readers with a deeper understanding.)

[Questioner A]

Q : The system services' order intake was so strong in the first quarter (Q1). May I ask what types of orders increased in light of industry and size? Do you think that this trend is sustainable?

A : We see orders generally increasing, regardless of industry and size. We think that this strength will continue. Customers have been impacted by COVID-19. However, depending upon industries, some customers have recovered their appetite for investment, which is conducive to the growth of our order intake and revenue in Q1.

Q : What caused a decrease in the revenue and profit of hardware in Q1? Did a shortage of semiconductor impact?

A : Factors such as a semiconductor shortage and a lockdown in China forced us to postpone posting sales of hardware products, specifically network devices produced by overseas manufacturers, as we experienced at the end of the previous fiscal year. Most of the sales that could not be posted in the previous fiscal year and were postponed are now posted. On the other hand, we postponed posting sales to the second quarter (Q2) and thereafter, despite our having expected to post in Q1. The put-off amount is almost equivalent to the old sales that we posted in Q1. Thus, impacts from the semiconductor shortage are neutralized in Q1. However, the hardware sales in Q1 are smaller than the same quarter of the previous fiscal year when we had posted sales of GIGA School projects and large-scale projects about electronic shelf tags.

Q : You put off posting hardware sales. May I ask how much you suffered impacts from the postponement? Also, if the sales subject to the postponement are mainly about overseas products, you are likely to pay more to purchase due to a depreciation of the yen. Are you prepared and do you think about passing on the increase in purchase costs to sales price, for example?

A : The amount of sales that we postponed posting in Q1 is approx. ¥2.0 billion. We expect rising prices of products caused by the weak yen. We would like to steer negotiations with customers with an eye towards redirecting the cost increase in sales prices as we propose to them.

[Questioner B]

Q : May I ask what caused an increase in the outsourcing order intake in Q1? Is the increase attributable to your posting a long-term project for a BankVision customer that decided to migrate to BankVision on Azure?

A : We have not posted as yet the project that you referred to in your question. We posted a project of system renewal for a customer related to real estate business in Q1.

Q : The landscape of your outsourcing business shows an increase in the Corporate DX-type outsourcing revenue and Service-based-type (business creation-type) outsourcing revenue, in contrast to a decline of revenue from Entrusted operation-type outsourcing. Do I correctly assume a boost in the outsourcing revenue towards your medium-term targets?

A : Our business creation-type outsourcing business has not delivered big revenue numbers. However, seeds of or base factors for the service are spreading steadily. We saw an increase in the quantity of system services order intake and system development projects in Q1. We know that many of them can be branched out into outsourcing services in the future. We aim to achieve our target values by diversifying new business projects into outsourcing service opportunities in an accelerated manner.

Q : May I ask how you think that you can make outsourcing service opportunities out of system development projects of the system services category?

A : Our customers operate no single business or service. Upon our enticing a customer to entrust us to perform services, with our leg in the door at the customer, we will likely expand our footprint through grapevine communications throughout the customer irrespective of the vertical authority levels, and will have other more services accepted at the customer. We will see an increase in business per customer. We would like to deepen relationship of trust with customers and understand them more through individual projects. This will help us offer more our outsourcing services and SaaS services. We have had good feedbacks from customers in response. We expect a growth of outsourcing business.

On the other hand, we operate businesses such as business creation-type outsourcing business that we provide services to a mass of customers who will pay use fees in return. This type of business will increase significantly when it crosses the breakeven point. We know that we need a bit more to reach the breakeven point.

[Questioner C]

Q : The gross margin of system services was improved in Q1. May I ask if it is due to some system services of high profitability? Or, can I correctly expect a continued improvement of the gross margin in Q2 and thereafter, as well? Also, can I ask about profitability about outsourcing? I see the gross margin of outsourcing increasing.

A : We had multiple highly profitable projects of system services in Q1. Also, we have had a good accumulation of order intake about small and medium-sized system services projects. Thus, we expect that we can keep the profitability of system services at a certain level in Q2 and thereafter. However, it would be difficult to keep the number at the same level as of Q1.

The profitability of outsourcing is improved, if not compared to the same quarter (Q1) of the previous fiscal year when we posted a project of high profitability. The improved outsourcing profitability was enabled as a result of multiple profitable projects piling up. We expect the outsourcing profitability to remain at this level. The profitability of outsourcing will increase at a geometric rate if outsourcing exceeds a break-even point with service-based-type (business creation-type) outsourcing as a driving force. We have not done that much to reach the stage.

[Questioner D]

Q : You suffered a significant decrease in the gross margin of outsourcing in the fourth quarter (Q4) of the previous fiscal year. It was due to an increase in the depreciation cost burden as a result of OptBAE beginning operations and initial allowances for stabilizing the operations. You have resumed your profitability level in Q1 of this fiscal year. Can I correctly understand that the factors that had driven down profits in Q4 of the previous fiscal year were settled?

A : The depreciation costs for OptBAE in Q4 remain unchanged. On the other hand, the costs for initial allowances were gone in Q1 of this fiscal year. Moreover, we plan new operations for OptBAE in the third quarter (Q3) and Q4, and thus we will see the economies of scale in the picture. Furthermore, we have seen profitability increasing in multiple projects as I said minutes ago. We expect that the profitability will not be dampened as much as it did in Q4.

Q : I remember that you referred to renovating your internal core system in this fiscal year, and that would push up costs by ¥2.0 billion approx. May I ask about any progress in Q1?

A : We saw a cost increase of approx. ¥0.3 billion in Q1. We expect a slight increase in the costs as we go through the rest of the entire quarters. Also, our assumptions that we made in the beginning of the fiscal year suggested a cost increase of approx. ¥2.0 billion driven up by renovating our internal core system. However, the cost will likely be slightly smaller than ¥2.0 billion. This is attributable to our finding more portions to be capitalized and amortized not processed as expenses when incurred than we assumed in the beginning.

[Questioner E]

Q : May I ask about your evaluation of the Q1 performance in comparison with the internal plan?

A : We found system services perform better than we had expected. On the other hand, we had expected that outsourcing would grow slightly more. Software projects included many low-margin products produced by other companies, and so we saw almost no profit in the

software segment. Hardware was smaller than the first quarter of the previous fiscal year when we had posted projects about GIGA School and electronic shelf tags. However, we see the hardware performance stay within our expectations in light of the first half of the fiscal year. The reason is that there are accumulations of order backlogs to be posted as revenue in Q2.

The outsourcing gross margin in Q1 is lower than a level that should be regarded as standard by all of you. We assume that the gross margin will be driven up in the second half of the fiscal year by the OptBAE beginning to serve customers in Q3 and Q4. We are watchful about how we will deliver the multiple projects in the future after we improved the profitability in Q1. Having said, our expectation at this point in time is that the gross margin will exceed 27%.

(Note)

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