NIHON CHOUZAI Co.,Ltd.

3341 Tokyo Stock Exchange First Section

28-Oct.-15

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FISCO Ltd. Analyst
Hiroyuki Asakawa

Made the most progress in the industry in generic pharmaceuticals sales and home medical care services

Nihon Chouzai Co., Ltd.<3341> (hereinafter, "the Company") is a leading domestic dispensing-pharmacies company that ranks second in sales in the dispensing pharmacy industry. The Nihon Chouzai Group manufactures generic pharmaceuticals, so one of its characteristics is that it has a manufacturing function. It additionally has a staffing business for medical practitioners and a business for providing information and consulting, and it is developing its operations with a structure of four business departments.

The keys to its growth strategy for its Dispensing Pharmacy business are to expand its network of pharmacies and to increase the average spend per customer. When developing its pharmacy network, its basic approach is to adopt a strategy of responding flexibly in terms of the location and the type of pharmacy to be opened in order to capture demand, while not to reply on M&As but instead opening them organically. For average spend per customer, it is focusing on increasing sales of generic pharmaceuticals and expanding its home medical care services. Both are policies being promoted by the government and have the advantage of providing a high number of additional points for the total number of NHI points, and the Company has made the most progress in this area within its industry.

The Pharmaceuticals Manufacturing and Sales business recorded a segment operating income for the first time in FY3/13 and is currently experiencing its second expansion phase. In April 2013, the Company made a subsidiary of Choseido Pharmaceutical Co., Ltd. and it now handles almost 600 items after totaling the items it itself produces and those it purchases. The Company is currently focusing its efforts on expanding its production capacity and in addition to constructing a new building and acquiring a plant in FY3/15, in September 2015 it announced that it would also construct a new plant. The Nihon Chouzai Group plans to greatly increase its production capacity from 4.3 billion tablets a year at the end of FY3/15 to 15.6 billion tablets a year.

While the percentage of net sales provided by the Medical Practitioners Staffing business is low, it is leveraging its high profit margin to contribute more than 10% of operating income and it is growing as a business with presence. The Company is also utilizing the top-class status of its dispensing pharmacies to grow this business into an industry leading position in terms of the number of registered pharmacists and results. It is also steadily increasing the number of registered practitioners in the areas of doctors, nurses, and co-medical, while the changes in the ways of working in the medical industry are proving to be a fair wind and there are extremely high expectations for the growth potential of this business in the medium term.

The Company launched its Information Provision and Consulting business in January 2012 when it established its subsidiary, Japan Medical Research Institute Co., Ltd. Its business model envisages the utilization of big data acquired from the Dispensing Pharmacy business and it is expected to grow to be the fourth business in the future.

The Company has embarked on a three-year medium-term management plan, with FY3/18 set as the final year. The plan's main targets are to increase net sales by 50% and to double operating income in the final year of the plan compared to the FY3/15 results. At FISCO, we consider that it is fully possible that it will achieve these targets if it steadily implements the respective priority measures in each business department.

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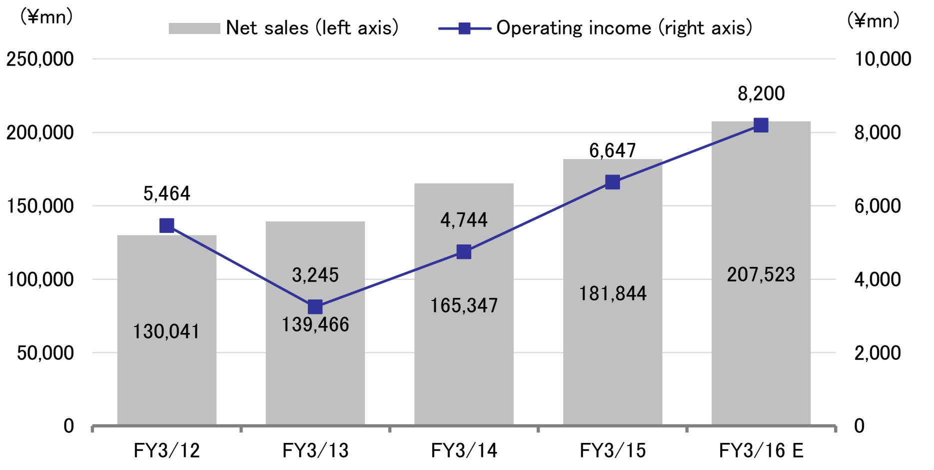
Check Point

- Embarking on the manufacturing of generic pharmaceuticals to realize the "separation of prescribing and dispensing"
- Managing pharmacies to respond flexibly to the government's requirements for pharmacy operations
- The main targets in its new medium-term management plan are to increase net sales by 50% and double operating income

Trends in consolidated results



Source: prepared by FISCO from the FY3/15 financial reports briefing materials

Company Outline

Embarking on the manufacturing of generic pharmaceuticals to realize the "separation of prescribing and dispensing"

(1) Company history

The Company was established in 1980 in Sapporo by current President and Representative Director Hiroshi Mitsuhara. As a qualified pharmacist, President Mitsuhara questioned whether the approach of dispensing in pharmacies by pharmacists the pharmaceuticals prescribed by doctors in hospitals was best for patients and decided to embark on a pharmacy business with the corporate philosophy of "Realizing the true separation of prescribing and dispensing" as the ideal condition to improve drug therapy. In 1995, the Company relocated its headquarters to Tokyo and established a foothold as a nationwide company, and subsequently in 2011, it succeeded in opening a pharmacy in every prefecture in the country.

In 2000, it established the subsidiary, Nihon Chouzai Pharma Staff Co., Ltd. thereby launching a staffing business for doctors, nurses, pharmacists and other medical practitioners. This company has steadily expanded its business scope and today, after being integrated with the subsidiary Medical Resources Co., Ltd. that was established separately in 2006, it undertakes the Company's Medical Practitioners Staffing business.

In the Company's history, the establishment of Nihon Generic Co., Ltd. in 2005 was a step of similar importance to the founding of the Company itself. President Mitsuhara considered that generic pharmaceuticals would play a major role in realizing the "separation of prescribing and dispensing," and with the opportunity provided by the enforcement of the revised Pharmaceutical Affairs Act in 2005 (currently, the Pharmaceutical and Medical Devices Act), he decided to embark on the manufacture of generic pharmaceuticals. Nihon Generic struggled for a while after it first began in business, but it increased the number of items it produced and established a production system and in FY3/13, the Pharmaceuticals Manufacturing and Sales business segment recorded an operating income for the first time. Subsequently, the scope of this business has been further expanded with the acquisition of Choseido Pharmaceutical in 2013, and also the Kasukabe plant of Teva Pharma Japan Inc. in 2015.

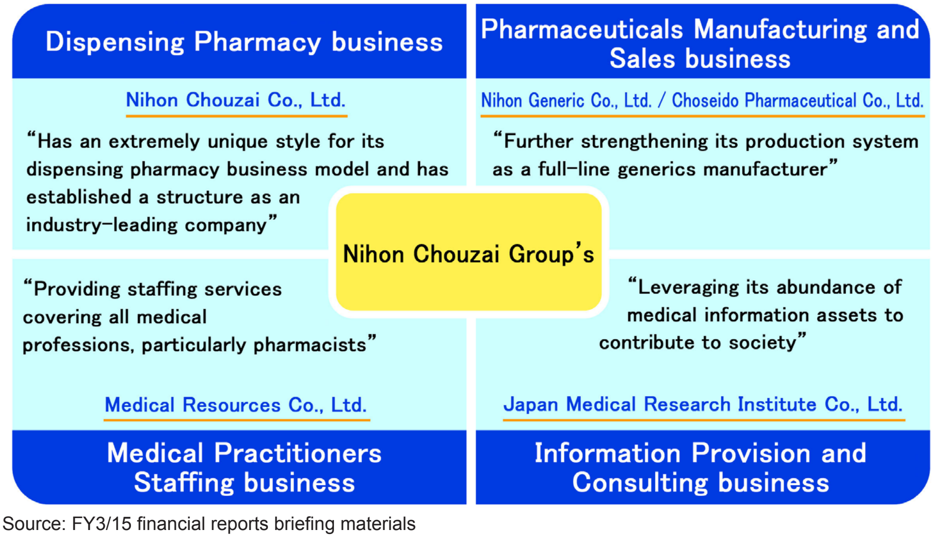
Company history

March 1980	Established Nihon Chouzai Co., Ltd. in Sapporo to manage dispensing pharmacies
April 1980	Opened the first pharmacy branch
August 1987	Opened a Tokyo branch
January 1994	Opened the Tohoku branch. Established the subsidiary Miyagi Nihon Chouzai Co., Ltd.
April 1995	Relocated the headquarters to Tokyo. Opened a Sapporo branch and a Kyushu branch
March 2000	Changed the corporate name of Miyagi Nihon Chouzai and established Nihon Chouzai Pharma Staff Co., Ltd.
October 2000	Opened an Osaka branch
September 2004	Listed on the Tokyo Stock Exchange (TSE) Second Section
January 2005	Established Nihon Generic Co., Ltd. as a subsidiary
September 2006	Listing upgraded to the TSE First Section
October 2006	Established Medical Resources Co., Ltd. as a subsidiary
July 2008	Merged Nihon Chouzai Pharma Staff and Medical Resources (with Medical Resources as the surviving company)
October 2010	Launched the manufacture of generic pharmaceuticals at Nihon Generic's Tsukuba plant
March 2011	Achieving the opening of a pharmacy in every prefecture in the country
January 2012	Established Japan Medical Research Institute Co., Ltd. as a subsidiary
April 2013	Made a subsidiary of Choseido Pharmaceutical Co., Ltd.
February 2015	Nihon Generic acquired the Kasukabe plant of Teva Pharma Japan Inc.

(2) Business outline

The structure in the Company is for the parent company and consolidated subsidiaries to be independently responsible for their businesses. As the Information Provision and Consulting business is included in the Dispensing Pharmacy business segment, the Company discloses information separately on three business segments; the Dispensing Pharmacy business, the Pharmaceuticals Manufacturing and Sales business, and the Medical Practitioners Staffing business. Each business segment is described in detail below, but in terms of the percentages of net sales they provided in FY3/15, the Dispensing Pharmacy business provided the overwhelmingly highest percentage, at 82.2%. However, the profitability of the Pharmaceuticals Manufacturing and Sales business and the Medical Practitioners Staffing business exceeds that of the Dispensing Pharmacy business, and in addition as the business segments are closely related, the situation is that each business has a sense of presence and importance.

Nihon Chouzai Group's business development



Source: FY3/15 financial reports briefing materials

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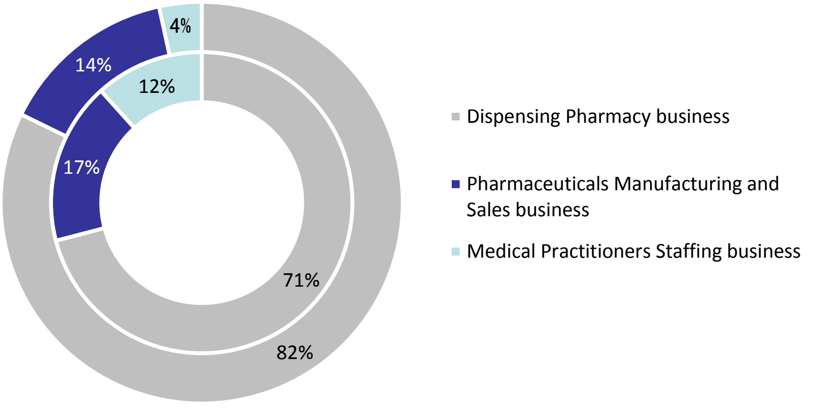
Percentages of net sales and operating income by business segment (FY3/15)



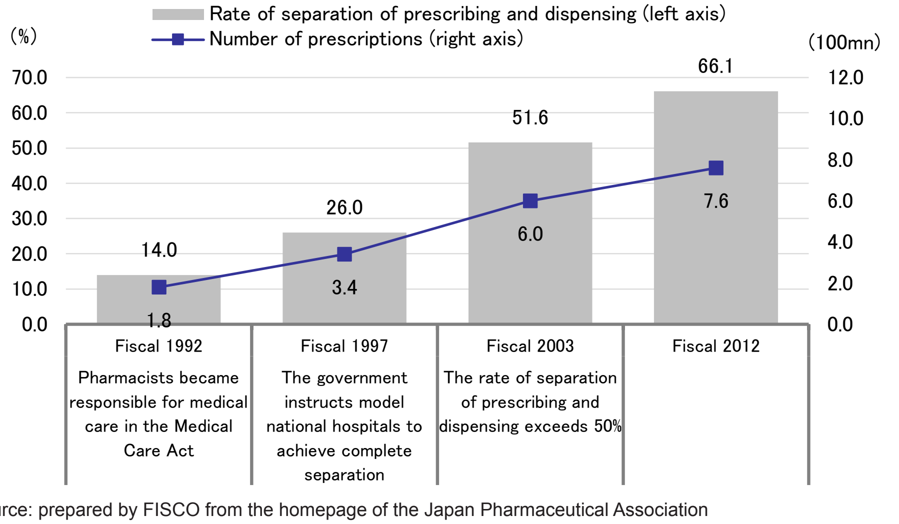
External:net sales internal:operating income (FY3/15 result)
Source: prepared by FISCO from the Company's financial results summary

The percentage of prescriptions dispensed at pharmacies outside of hospitals is rising and the situation of a complete separation of prescribing and dispensing is growing closer

(3) The business environment in the dispensing pharmacies market

The Company's main area of business is dispensing pharmacies and the foundation on which it has established this business is the "separation of prescribing and dispensing." This refers to the separation of the tasks of prescribing and dispensing pharmaceuticals, with these tasks being carried out by doctors and pharmacists respectively. The separation of prescribing and dispensing in Japan began in the Meiji era with the enactment of the Pharmaceuticals Act (1889) and after passing through several laws, has arrived at the current law today, of the Pharmaceutical and Medical Devices Act. The percentage of patients who receive a prescription as outpatients and who are dispensed the pharmaceuticals at a pharmacy outside of a hospital is called the rate of separation of prescribing and dispensing (also the prescription receipt rate) and in 1997, the Ministry of Health, Labour and Welfare instructed the 37 model national hospitals throughout Japan to achieve a rate of 70% or above. This spurred-on the further separation of prescribing and dispensing and by fiscal 2012, the rate had reached 66.1%, and currently the situation is approaching complete separation.

Trends in the number of prescriptions and the rate of separation of prescribing and dispensing



Source: prepared by FISCO from the homepage of the Japan Pharmaceutical Association

In Japan, in principle only those facilities that have received permission to operate a business as a pharmacy based on the Pharmaceutical and Medical Devices Act may use the name “pharmacy.” These facilities will have a pharmacist in resident and be able to dispense pharmaceuticals based on doctors’ prescriptions from their dispensary. Facilities that do not meet the requirements of having a pharmacist and a dispensary cannot use the word “pharmacy” in their name, and generally call themselves “drug stores” or something similar (for example “○○Drugs” or “○○Pharmaceuticals ”). But even a drug store can acquire permission to and call itself and operate as a “pharmacy” if it meets the standards, such as having a pharmacist in residence and a dispensary. The name “dispensing pharmacy” clearly signifies that the facility provides the medical service of dispensing pharmaceuticals and is not just a drug store.

In the dispensing pharmacies industry, those companies that are expanding their business scope while focusing on providing the medical service of dispensing pharmaceuticals are competing for the top positions with those companies that have entered into the dispensing field from the general retail industry. In addition, there are privately run dispensing pharmacies and all together, there are approximately 57,000 pharmacies nationwide. As was previously mentioned, the Company began as a dispensing pharmacy and then expanded its business scope, and currently it is competing for the top position in net sales in the dispensing pharmacy business with Ain Pharmaciez<9627>, while the Group ranks second for the number of pharmacies.

When comparing the Company’s business scale and areas with those of its competitors, we see that those companies that started as specialist dispensing pharmacies, including the Company, Ain Pharmaciez, and Qol<3034>, constitute around 90% of the dispensing pharmacy business. However, companies from the general retail industry that operate drug stores and related facilities are growing their pharmacy networks and expanding their dispensing businesses by opening dispensing pharmacies within their drug stores, and their presence in the industry is gradually increasing. Comparing these companies’ net sales per dispensing pharmacy, Nihon Chouzai’s total of ¥309 million is significantly higher than that any other company, even those of the other dispensing majors, which are around ¥200 million. Moreover, the figure of Welcia Holdings <3141> is only ¥71 million. This difference is grounded in whether or not dispensing is the company’s main businesses, so in this sense these figures can be said to be as expected.

The companies specializing in dispensing pharmacies are also working to enter into businesses other than dispensing and thereby strengthen their business foundations. In the case of the Company, this corresponds to it launching its Pharmaceuticals Manufacturing and Sales business and Medical Practitioners Staffing business. Also, among its industry peers, there are companies that are entering into the drug store business, the medical facilities support and consulting business, and the nursing case business.

Comparison of industry peers

Company name	Code	Dispensing pharmacy business					
		Number of pharmacies		Net sales		Sales composition (%)
		Pharmacies	Point in time	(¥mn)	Fiscal period	
Nihon Chouzai	3341	510	End of 3/15	157,999	FY3/15	86.9%
Ain Pharmaciez	9627	754	End of 4/15	169,063	FY4/15	90.0%
Qol	3034	538	End of 3/15	103,259	FY3/15	90.3%
Sogo Medical	4775	538	End of 3/15	80,660	FY3/15	74.7%
Welcia Holdings	3141	687	End of 2/15	48,482	Refer to the remarks	12.7%
Cocokara Fine	3098	234	End of 3/15	45,967	FY3/15	13.2%
Kraft	Unlisted	469	End of 9/15	-	-	-

Company name	Code	Other businesses					Dispensing net sales per pharmacy (¥mn)	Remarks
		Pharmaceutical manufacturing	Staffing	DS	Pharmaceuticals wholesales	Consulting		
Nihon Chouzai	3341	•	•				309	The number of pharmacies is “dispensing pharmacies” only and does not include product-sales drug stores
Ain Pharmaciez	9627			•	•		224	The number of pharmacies is the number of “dispensing pharmacies”
Qol	3034		•				192	The number of pharmacies includes 37 Lawson stores, 4 Bic Camera stores, and 3 West Japan Railway stores
Sogo Medical	4775					•	150	
Welcia Holdings	3141			•			71	Due to changes to the fiscal period, FY2/15 (6 months) and 2H of FY8/14 were used for the total. The number of pharmacies is the number of “pharmacies/stores handling dispensing.”
Cocokara Fine	3098			•			196	The number of pharmacies is the number of “pharmacies/stores handling dispensing.”
Kraft	Unlisted						-	The numbers of pharmacies were researched by FISCO from the companies’ websites

Note: DS is an abbreviation of “drug store”
Source: prepared by FISCO from each company’s financial results summary and briefing materials

Nihon Chouzai's characteristics and strengths

Responding swiftly to the government's requirements for pharmacy operations

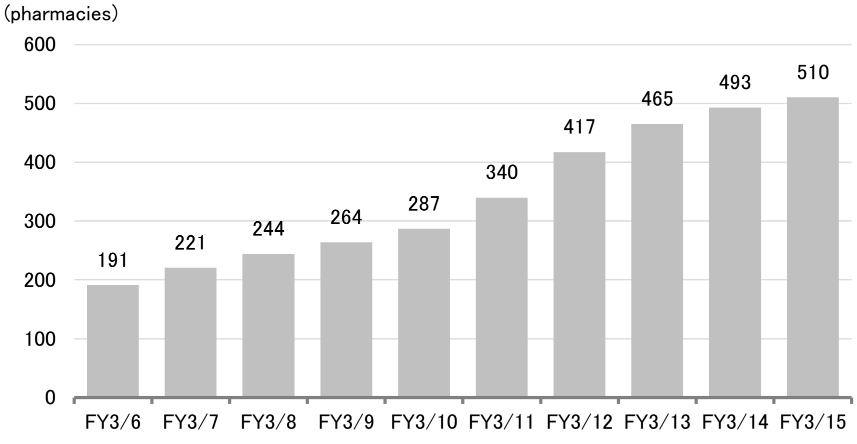
(1) Dispensing Pharmacy business

The most important point in order to understand the dispensing pharmacy business is that basically these pharmacies are national health insurance (NHI) pharmacies incorporated into the health insurance system, and their fees (income) are determined by the number of NHI points stipulated in the health insurance system (which is the basis for calculating income). While to some extent there is room for them to reduce costs through their own efforts, such as by cutting personnel costs or system costs, the measures for increasing sales can broadly be divided into the following two. The first is to increase the number of customers per pharmacy (in many cases this expresses the number of dispensed prescriptions that were brought by individual customers, and a pharmacy-opening strategy from this viewpoint entails opening hospital-adjacent type, medical mall-type, and foot-traffic type. The second method is to increase income per prescription. In the health insurance system, in order to process a prescription the income items are subdivided and the number of points determined for each respective task. But there is also a system for obtaining a range of additional points. Currently, the main ways of acquire additional points in the dispensing pharmacy business are measures for the increased use of generic pharmaceuticals and guidance for management of in-home medical long-term care (hereinafter, "home medical care services").

a) pharmacy strategy

The Company has developed a nationwide network of 523 dispensing pharmacies in 47 prefectures (as of the end of September 2015. It also has 1 product sales specialist store). The first characteristic of the Company's pharmacy strategy is not to rely on M&As, but instead to expand its network by opening pharmacies organically. One reason for this is that the Company is confident that the efficiency and profitability of its own pharmacies is higher than those of its industry peers, so it has not actively tried to acquire the inefficient pharmacies of other companies. Also, one more reason is thought to be that location is very significant for pharmacies and it is difficult to find a potential acquisition in an ideal location.

Trends in the number of Nihon Chouzai dispensing pharmacies



Note: does not include one product sales specialist store.
Source: the Company's FY3/15 financial reports briefing materials

Its strategy for opening pharmacies is a combination of opening hospital-adjacent types (openings next to large-scale hospitals), medical-mall types (openings within buildings with many clinics and others pharmacies), and foot-traffic types (openings focused on customer acquisition in places with a lot of foot traffic, rather than the patients of specific medical facilities). This strategy is adopted not just by the Company, but also by its industry peers. In the Company's case, in recent years the growth rate of the foot-traffic type has been higher than those of the other types of pharmacy. The Company does not disclose data on the percentages of openings according to pharmacy type, but at FISCO, we estimate that going forward it will increase its openings of the foot-traffic type.

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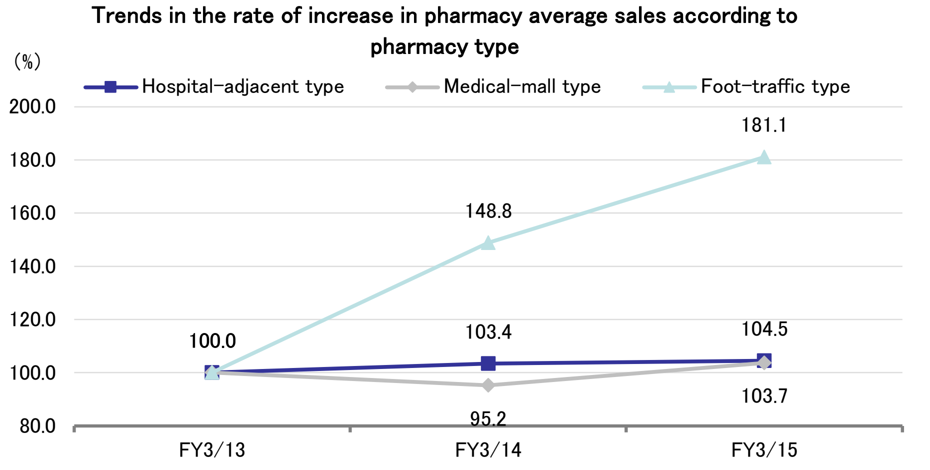
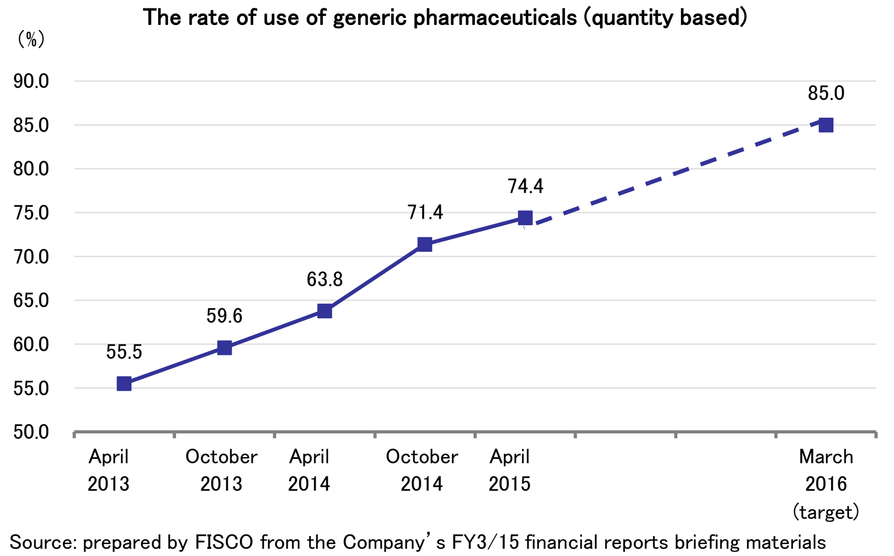


Note: Indexed with FY3/13 set as 100
Source: prepared by FISCO from the Company's FY3/15 financial reports briefing materials

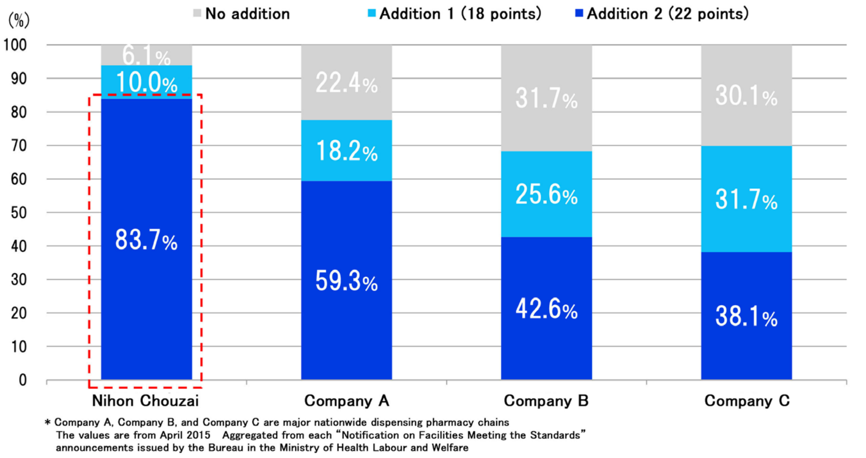
b) Improvement in the rate of use of generic pharmaceuticals
In order to reduce medical expenses within social security expenses, the Japanese government set the target of achieving a rate of prescriptions of generic pharmaceuticals relative to total prescriptions of 80% as quickly as possible in the period up to March 2020 (the denominator is the total of the original pharmaceuticals of the generic pharmaceuticals and the generic pharmaceuticals). In response to this target, by April 2015 the Company had achieved a rate of 74.4% and moreover is targeting 85% by March 2016.



Source: prepared by FISCO from the Company's FY3/15 financial reports briefing materials

As of the end of March, 2015, the Company had developed a network of 510 pharmacies nationwide, and within them, 83.7% had acquired generic pharmaceuticals dispensing addition 2 (22 points), while 10.0% had acquired addition 1(18 points), and only 6.1% had not acquired any additional points. The Company has a higher percentage of pharmacies that have acquired additional points than any of its industry peers.

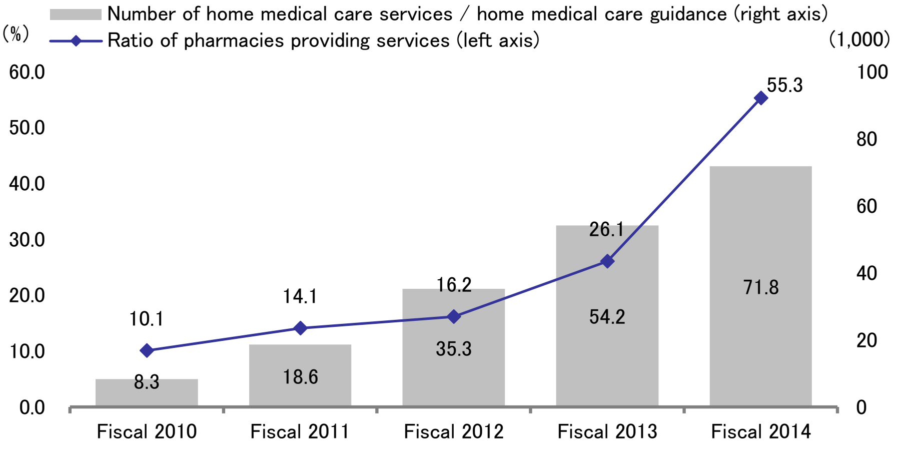
The calculation of additional points in the generic pharmaceuticals dispensing system



Source: the Company's FY3/15 financial reports briefing materials

Just as the Company encourages use of generic pharmaceuticals, it also applied efforts for home medical care services. In each pharmacy, when it has established a 24 hour dispensing system and a system for appropriate pharmaceutical management and compliance guidance for patients at home, the standard dispensing addition is added to the basic dispensing fee at the relevant pharmacy. Moreover, the fees for each home medical care service, of "Guidance for Management of In-Home Medical Long-Term Care fees" can be collected as long-term care insurance fees. While there is a limit to the number of times they can be collected, as the targets of the system are special nursing homes for the elderly and private nursing homes for the elderly, the market is large. Within all of the Company's pharmacies, 95.1% (as of August 2015) provide home medical care services and this has had an effect, with percentage of pharmacies calculated as having the standard dispensing addition 2 increasing to 21.4% of the total.

Home medical care services results



Source: the Company's FY3/15 financial reports briefing materials

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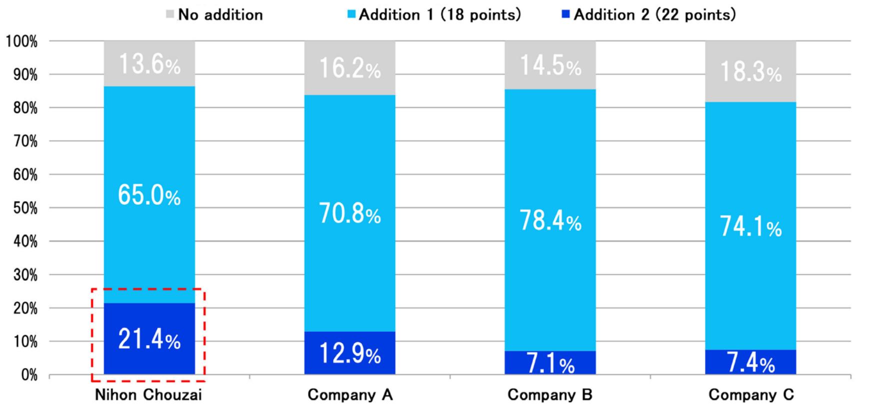
Calculation of the standard dispensing additional points Calculation conditions



* Company A, Company B, and Company C are major nationwide dispensing pharmacy chains
The values are from April 2015 Aggregated from each "Notification on Facilities Meeting the Standards" announcements issued by the Bureau in the Ministry of Health Labour and Welfare

Source: the Company's FY3/15 financial reports briefing materials

The current situation is that the focus is being placed on the two areas of generic pharmaceuticals and home medical care services, but what is important here is the question of how the additional points are obtained. The additional-points framework is that the "government incentivizes the pharmacies to carry out the work it requires." Also, the standards for the additions may change overnight if the system or policy were to change, and the problem is the ability to respond, or of to what extent can a company respond to this sort of institutional change. On these points, at FISCO we consider that the Company, which is led by management who has demonstrated strong leadership, is in a superior position. The Company has the highest sales per dispensing pharmacy in the industry, of ¥309 million, and while a major factor behind this is thought to be that it has developed its pharmacy network by mainly targeting in-patients of highly functional hospitals such as university hospitals, we should also not lose sight of the fact that its pharmacy management has efficiently earned additional points. We consider this to be the Company's biggest strength.

Comparison of sales per dispensing pharmacy

Company name	Code	Dispensing pharmacy business: Number of pharmacies: Pharmacies	Dispensing pharmacy business: Number of pharmacies: Point in time	Dispensing pharmacy business: Net sales: (¥mn)	Dispensing pharmacy business: Net sales: Fiscal period	Dispensing pharmacy business: Sales composition (%)	Dispensing net sales per pharmacy (¥mn)	Remarks
Nihon Chouzai	3341	510	End of 3/15	157,999	FY3/15	86.9%	309	The number of pharmacies is "dispensing pharmacies" only and does not include product-sales drug stores
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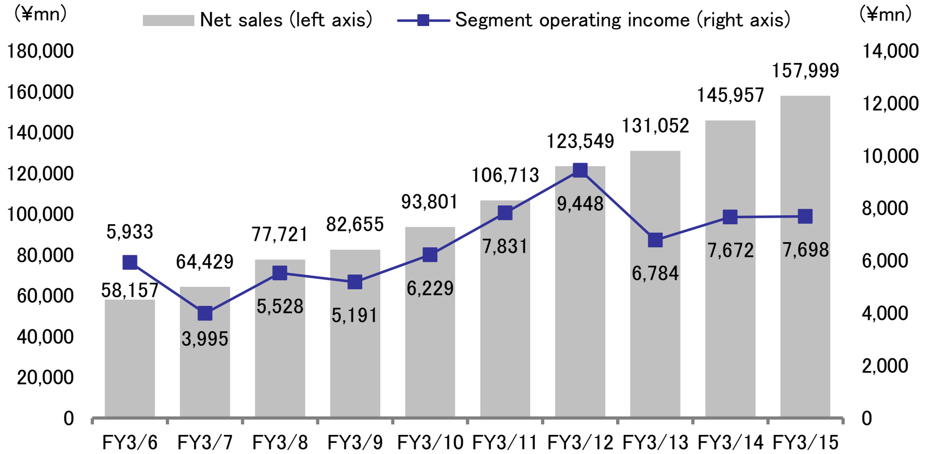
Kraft	Unlisted	464	End of 9/15	-	-	-	-	The numbers of pharmacies were researched by FISCO from the companies' websites

Source: prepared by FISCO from each company's financial results summary and briefing materials

c) Trends in results in the Dispensing Pharmacy business

In the Company's results in its Dispensing Pharmacy business, while net sales have continued to trend upwards, it is not necessarily the case that segment operating income has followed suit. This is due to various factors, including the effects of the NHI price revisions carried out once every two years and the higher costs associated with pharmacy openings. Basically, a newly opened store fully contributes to results from its second year, so at FISCO we consider that as long as the increase in the number of pharmacies continues, the long-term trend will be increases in sales and profits, but that caution is required when forecasting on a single-year basis.

Trends in results in the Dispensing Pharmacy business



Source: the Company's financial results summary

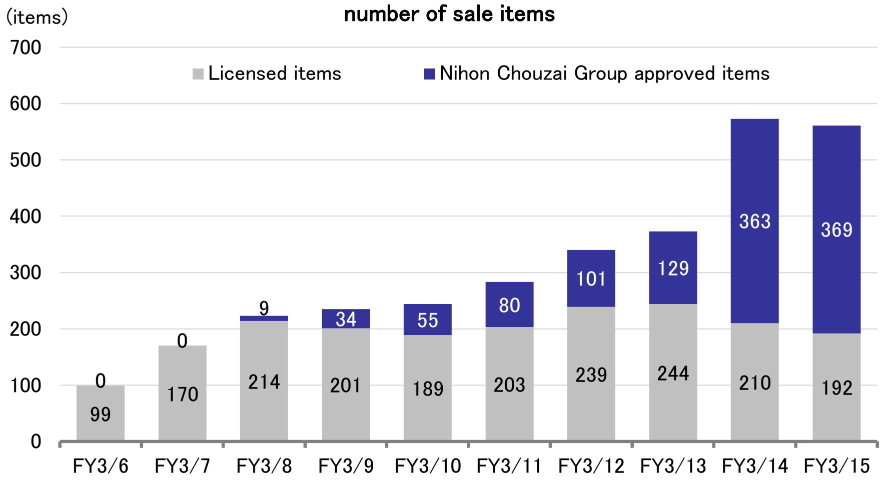
Immediate expansion in the number of approved Nihon Chouzai Group products

(2) Pharmaceuticals Manufacturing and Sales business

The Company established Nihon Generic in 2005 and thereby entered into the generic Pharmaceuticals Manufacturing and Sales business. The important point here is that this business department does not exist only for vertical integration within the Company. In other words, the subsidiaries in the group responsible for pharmaceutical manufacturing, of Nihon Generic and Choseido Pharmaceutical, have business models of selling the products they produce (and some purchased products) to third party groups via pharmaceutical wholesalers. In the FY3/15 results, approximately 66.6% of the net sales of the Pharmaceuticals Manufacturing and Sales business segment were external net sales and 33.4% were internal (in-Group) transactions.

Initially, Nihon Generic handled products purchased from other companies, but as it established its own production system, sequentially from FY3/08 it increased the number of products approved and manufactured in-company. In addition to Nihon Generic, Choseido Pharmaceutical was made into a subsidiary by the Company in April 2013, which immediately expanded the approved items in the Nihon Chouzai Group. As of June 2015, it has 576 such items.

Pharmaceuticals Manufacturing and Sales business: trends in the number of sale items



Source: prepared by FISCO from the FY3/15 financial reports briefing materials

The Company is also accelerating the expansion of its manufacturing bases. Previously, Nihon Generic had one base, the N building at the Tsukuba plant, but in FY3/15 it completed the S building at the same plant and moreover purchased the Kasukabe plant from Teva Pharma Japan to establish a 3 plant structure, in doing so expanding its production capacity from 1 billion tablets to 3.2 billion tablets per year. Choseido Pharmaceutical has also completed its second plant at its headquarters and has increased its production capacity from 900 million tablets to 1.1 billion tablets.

Moreover, in September 2015 Nihon Generic announced that it would construct a second plant at Tsukuba. By March 2018, this newly constructed plant will have an annual production capacity of 10 billion tablets, and the investment amount for the first phase is expected to be approximately 17.2 billion yen in total for the land, buildings, and machinery and equipment. In parallel with this, the production capacity of the current Tsukuba plant (the total for the N and S buildings) is being bolstered and the plan is to increase the total production capacity, including Choseido Pharmaceutical's portion, to 15.6 billion tablets per year.

In the background to this sort of strengthening of production capacity is that the government has set the target of increasing to above 80% generic pharmaceuticals' share of all prescribed pharmaceuticals by the end of fiscal 2020. The Company considers that the growth of the generic pharmaceuticals market will further accelerate in the next five years compared to its development in the past five years and intends to firmly capture this rapid market expansion for its corporate earnings.

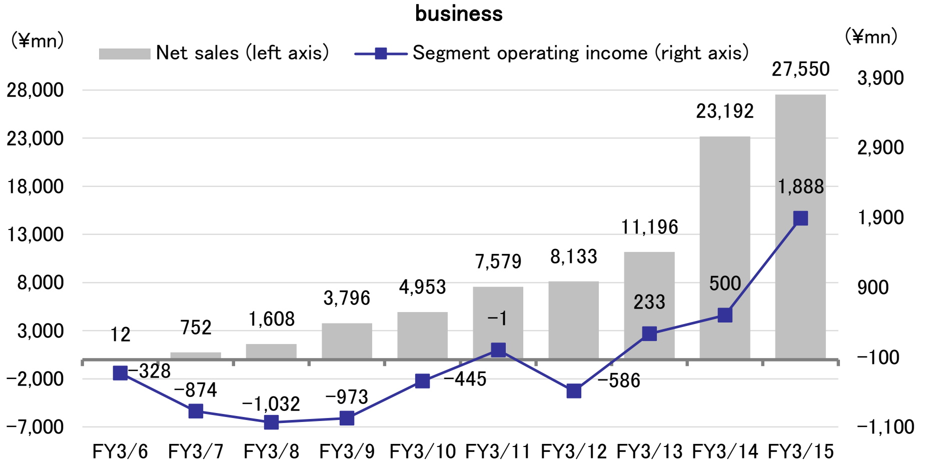
List of the generic pharmaceuticals manufacturing bases

Company name	Plant name	Production capacity (100mn tablets/year)		
		End of FY3/14	End of FY3/15	End of FY3/18 (forecast)
Nihon Generic	Tsukuba plant N building	10	10	36
	Tsukuba plant S building	-	13	
	Tsukuba second plant	-	-	100
	Kasukabe plant	-	9	9
	Sub-total	10	32	145
Choseido Pharmaceutical	Headquarters first plant	7	7	7
	Headquarters second plant	-	2	2
	Kawauchi plant	2	2	2
	Sub-total	9	11	11
Total		19	43	156

Source: prepared by FISCO from the Company's FY3/15 financial reports briefing materials

Thanks to the increase in the number of sales items, the enhancement of its manufacturing bases, and the expansion of external sales, the Company's Pharmaceuticals Manufacturing and Sales business segment recorded a segment operating income for the first time in FY3/13 and subsequently has maintained profitability. Due to factors including the increase in depreciation costs in conjunction with the completion of building S at the Tsukuba plant and the amortization of goodwill following the acquisition of the Kasukabe plant, there were concerns that segment operating income would come under pressure from FY3/16 onwards. But in the financial statements of Q1 FY3/16, segment operating income increased 78.7% year on year (y-o-y) to ¥589 million, and at FISCO we consider it highly likely that these concerns about shrinking profit margins will prove unfounded.

Trends in results in the Pharmaceuticals Manufacturing and Sales business



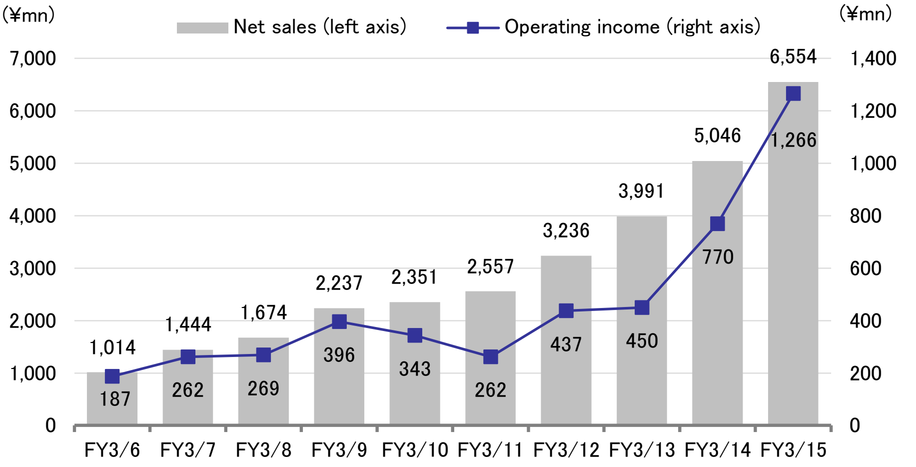
Source: Prepared by FISCO from the FY3/15 financial reports briefing materials

Continuing the keynote of increases in sales and profits

(3) Medical Practitioners Staffing business

The Company operates its staffing business for medical practitioners, including doctors, nurses, and pharmacists, through its consolidated subsidiary Medical Resources. While the percentage of net sales provided by this business segment is low at 4% (the FY3/15 result), its operating income margin is very high compared to the other businesses at 19.3% (FY3/15) while its percentage of operating income is 12%, and it is growing as a businesses with a sense of presence. Its results over the last few years have also trended upwards each fiscal year and it has continued a keynote of increases in sales and profits.

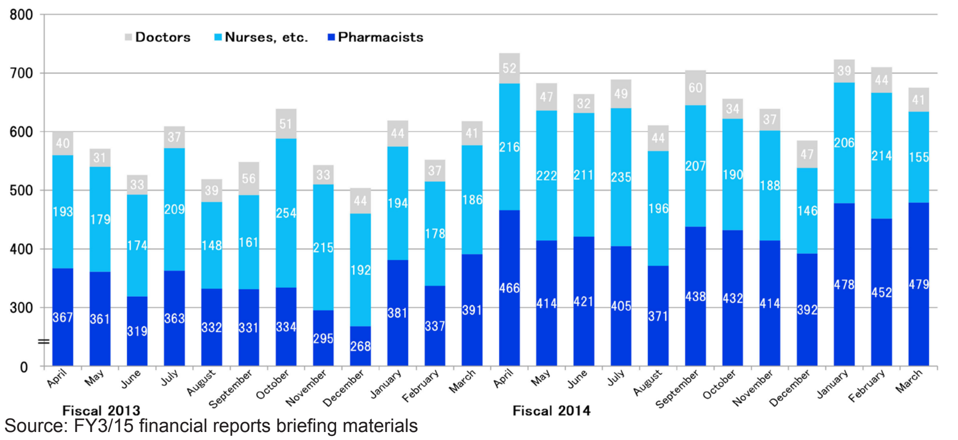
Trends in the results of the Medical Practitioners Staffing business



Source: the Company's financial results summary

There are many companies operating a medical-practitioners staffing business, including those who specialize in it and those for which it is an additional business. Among them, the positioning of the Company for the "dispatch of pharmacists" is that it is the industry leader in terms of the number of registered pharmacists and the results for dispatches and placements. It has also been steadily improving its results for the number of registered staff and placements of doctors, nurses, and co-medical practitioners in its staffing business. The percentages of women in the medical-related industries are high and the tendency is for them to leave work for a while after getting married or having children and then to return to work later. As an industry leading dispensing pharmacy group, the Company is in a position to more easily ascertain the recruitment demand for medical practitioners and at FISCO we consider that it is highly possible that the trend of increases in sales and profits in its staffing business will continue in the future.

Trends in the number of placements by job category



Source: FY3/15 financial reports briefing materials

Medium-term management plan

The main targets in the new medium-term management plan are to increase net sales by 50% and double operating income

(1) Outline of the medium-term management plan

In April 2015, the Company announced its new three year medium term management plan for the period FY3/16 to FY3/18. In this plan, based on the corporate philosophy, of “Realizing the true separation of prescribing and dispensing”, the Company has set the main targets of increasing net sales by 50% and doubling operating income.

The main targets in the new medium-term management plan

Corporate philosophy		Realizing the “true separation of prescribing and dispensing”	
Main targets	Net sales	Achieve a 50% increase	FY3/15: ¥181.8 billion →FY3/18: ¥273.8 billion
	Operating income	Doubled	FY3/15: ¥6.6 billion→FY3/18: ¥12.2 billion
	Operating income margin	Raise to 4.5%	FY3/15: 3.7%→FY3/18: 4.5%
	Corporate governance	Improve corporate value by the appropriate practice of the corporate governance code	

Source: prepared by FISCO from the Company’s FY3/15 financial reports briefing materials and press releases

(2) Priority measures for each business

In the current medium-term plan in the section “Nihon Chouzai’s characteristics and strengths,” the content of the descriptions of the priority measures for each business overlap in terms of their main points. In other words, in its Dispensing Pharmacy business, the Company is aiming to promote the use of generic pharmaceuticals and home medical care services and open pharmacies flexibly and proactively; in the Pharmaceuticals Manufacturing and Sales business, it is targeting expanding sales items and establishing a system for stable supply; and in its Medical Practitioners Staffing business, it is aiming to increase the total number of placements per month. By implementing these priority measures, the plan is to expand these 3 business department and achieve net sales ¥273,800 million and operating income of ¥12,200 million in FY3/18.

The priority measures in each business

Dispensing Pharmacy business department	• Promote home medical care service • Thoroughly promote the use of generic pharmaceuticals • Continue to actively open various types of pharmacies • Establish an attitude of complete acceptance toward the various institutional reforms
Pharmaceuticals Manufacturing and Sales business department	• Realize an expansion in business scope exceeding the market growth rate • Secure the number of sales items at an industry-leading level • Establish a system for the stable supply of high-quality products
Medical Practitioners Staffing business department	• Rapidly achieve annual net sales of ¥10 billion • Increase the total number of placements per month
Information Provision and Consulting business department * The net sales and other values for the relevant business department are included in the Dispensing Pharmacy business	• The development of new products in the data provision business

Source: prepared by FISCO from the Company’s FY3/15 financial reports briefing materials and press releases

Numerical targets in the medium-term management plan

(¥mn)	FY3/15 Results	FY3/18 Target	FY3/18 Sales increase	FY3/18 Rate of increase
Dispensing Pharmacy business	157,999	217,600	59,601	37.7%
Pharmaceuticals Manufacturing and Sales business	27,550	55,700	28,150	102.4%
Medical Practitioners Staffing business	6,554	14,000	7,446	113.6%
Elimination of transactions between segments	-10,259	-13,500	-	-
Net sales total	181,844	273,800	91,956	50.6%
Operating income	6,647	12,200	5,553	83.5%

Source: prepared by FISCO from the Company's FY3/15 financial reports briefing materials and press releases

Results trends

All three segments achieved increases in sales and profits in Q1 FY3/16

(1) Q1 FY3/16 financial results

In its financial results for Q1 FY3/16 (April to June 2015) the Company recorded major increases in both sales and profits and high values in terms of its progress toward achieving the plan targets, of net sales of ¥48,895 million (up 13.4% y-o-y), operating income of ¥2,052 million (up 133.6%), recurring income of ¥1,896 million (up150.8%), and net income of ¥1,221 million (up 316.9%).

All three segments achieved year-on-year increases in sales and profits. In the mainstay Dispensing Pharmacy business, in addition to the steady performance of the existing pharmacies, the increase in the number of prescriptions for a drug to treat Hepatitis C that was released in the second half of last year also contributed to the improved results. In the Pharmaceuticals Manufacturing and Sales business, sales grew following the increase in demand for generic pharmaceuticals and operating income also increased significantly despite the rise in depreciation costs. In the Medical Practitioners Staffing business, the Company has been steadily increasing profits by finding new facilities for the placement of pharmacists and securing registrations of new staff.

Summary of Q1 FY3/16

(unit: ¥mn)

		FY3/15		FY3/16				
				Q1		Q2 cumulative total (E)	Rate of progress	Full year (E)
		Q1	FY3/15	Results	y-o-y		Q1/Q2 cumulative total (E)	
Net sales	Dispensing Pharmacy business	37,546	157,999	42,322	12.7%	-	-	-
	Pharmaceuticals Manufacturing and Sales business	6,506	27,550	7,702	18.4%	-	-	-
	Medical Practitioners Staffing business	1,499	6,554	2,087	39.2%	-	-	-
	Before adjustment	45,552	192,104	52,112	14.4%	-	-	-
	Adjusted amount	-2,419	-10,259	-3,216	-	-	-	-
	Net sales total	43,133	181,844	48,895	13.4%	99,739	49.0%	207,523
Operating income	Dispensing Pharmacy business	1,190	7,698	2,015	69.3%	-	-	-
	Pharmaceuticals Manufacturing and Sales business	330	1,888	589	78.5%	-	-	-
	Medical Practitioners Staffing business	327	1,266	441	34.9%	-	-	-
	Before adjustment	1,847	10,853	3,046	64.9%	-	-	-
	Adjusted amount	-968	-4,205	-994	-	-	-	-
	Operating income total	878	6,647	2,052	133.6%	3,650	56.2%	8,200
SG&A expenses		6,248	25,281	6,706	7.3%	-	-	-
	Ratio of SG&A expenses to net sales	14.5%	13.9%	13.7%	-	-	-	-
Recurring income		756	6,003	1,896	150.8%	3,386	56.0%	7,434
Net income		293	2,778	1,221	316.9%	1,849	66.0%	3,583

Source: the Company's financial results summary

(2) Outlook for 1H and the full year of FY3/16

Reflecting its strong financial results in Q1, the Company has upwardly revised its forecasts for 1H FY3/16 (cumulative total for Q1 and Q2). The new forecast for 1H is net sales of ¥99,739 million (up 14.1% y-o-y), operating income of ¥3,650 million (up 39.2%), recurring income of ¥3,386 million (up 46.1%), and net income of ¥1,849 million (up 59.8%).

In the Q1 results, each business performed strongly from organic growth rather than due to any special factors, and when considering that no major changes to the business environment have been seen on entering Q2, the impression at FISCO is that even the upwardly revised forecasts are conservative and it is highly possible that the 1H results will exceed these revised forecasts.

Details of the revised Q2 forecast and outlook for the full-year results

(unit: ¥mn)

	FY3/16			
	Q2			Full year (E)
	Previous forecast	New forecast	Extent of revision (%)	
Net sales	97,980	99,739	1.8%	207,523
Operating income	2,926	3,650	24.7%	8,200
Recurring income	2,553	3,386	32.6%	7,434
Net income	1,195	1,849	54.7%	3,583

Source: prepared by FISCO from the Company's press releases

As was previously explained, the Company's rate of prescriptions of generic pharmaceuticals is high compared to its industry peers, but there is still room for it to go even higher and also plenty of room for further improvements in home medical care. Also, as the effects of the new pharmacy openings will increase in 2H, at FISCO we think that the keynote of increasing profits in the Dispensing Pharmacy business will continue until at least the end of the fiscal year. In the Pharmaceuticals Manufacturing and Sales business and the Medical Practitioners Staffing business also, it seems highly like that the trends in 1H will continue on in 2H. The Company has maintained its initial forecasts for its full-year results, of net sales of ¥207,523 million (up 14.1% y-o-y), operating income of ¥8,200 million (up 23.4%), recurring income of ¥7,434 million (up 23.8%), and net income of ¥3,583 million (up 29.0%). But at FISCO, we believe it is highly likely that it will upwardly revise these forecasts in the near future.

Income statement and the major indicators

(unit: ¥mn)

	FY3/13	FY3/14	FY3/15	FY3/16		
	Full year	Full year	Full year	Q1	Q2 cumulative total (E)	Full year (E)
Net sales	139,466	165,347	181,844	48,895	99,739	207,523
y-o-y	7.2%	18.6%	10.0%	13.4%	14.1%	14.1%
Gross profit	21,494	25,623	31,929	8,759	-	-
Gross margin	15.4%	15.5%	17.6%	17.9%	-	-
SG&A expenses	18,248	20,878	25,281	6,706	-	-
Ratio of SG&A expenses to net sales	13.1%	12.6%	13.9%	13.7%	-	-
Operating income	3,245	4,744	6,647	2,052	3,650	8,200
y-o-y	-40.6%	46.2%	40.1%	133.6%	39.2%	23.4%
Operating income margin	2.3%	2.9%	3.7%	4.2%	3.7%	4.0%
Recurring income	2,855	4,188	6,003	1,896	3,386	7,434
y-o-y	-42.2%	46.7%	43.3%	150.8%	46.1%	23.8%
Net income	184	1,901	2,778	1,221	1,849	3,583
y-o-y	-91.1%	928.4%	46.1%	316.9%	59.8%	29.0%
EPS (¥)	25.67	262.48	388.96	174.21	131.93	255.55
Dividend per share (¥)	70.00	70.00	70.00	-	40.00	62.00
BPS (¥)	2,034.09	2,181.26	2,515.19	-	-	-
EPS after adjustment for stock-split (¥)	12.84	131.24	194.48	87.11	-	-
Dividend per share after adjustment for stock-split (¥)	35.00	35.00	35.00	-	20.00	42.00
BPS after adjustment for stock-split (¥)	1,017.05	1,090.63	1,257.60	-	-	-

Source: the Company's financial results summary

Consolidated balance sheet

(unit: ¥mn)

	FY3/11	FY3/12	FY3/13	FY3/14	FY3/15
Current assets	28,920	36,543	43,037	53,373	60,096
Cash and deposits	7,275	12,622	14,583	15,429	13,952
Accounts receivable	10,893	12,868	13,645	17,395	20,001
Inventories	8,831	8,879	12,405	16,396	21,066
Other	1,921	2,174	2,404	4,153	5,077
Fixed assets	43,781	50,071	52,102	63,921	70,044
Tangible fixed assets	25,465	30,796	32,459	42,123	48,819
Intangible fixed assets	9,947	9,845	9,423	11,103	10,376
Investments, etc.	8,368	9,429	10,219	10,694	10,848
Total assets	72,701	86,615	95,140	117,295	130,141
Current liabilities	38,399	36,757	44,702	55,666	53,474
Accounts payable	20,091	21,884	24,542	28,963	33,392
Short-term debt, etc.	13,484	8,373	14,065	18,639	11,169
Other	4,824	6,500	6,095	8,064	8,913
Fixed liabilities	21,522	35,141	35,735	45,779	59,031
Long-term debt	20,183	33,610	33,845	42,165	53,184
Other	1,339	1,531	1,890	3,614	5,847
Total liabilities	59,921	71,899	80,437	101,446	112,505
Shareholders' equity	12,856	14,562	14,353	15,845	17,515
Capital	3,953	3,953	3,953	3,953	3,953
Capital surplus	4,754	4,754	4,754	4,754	4,754
Retained earnings	6,614	8,233	7,915	9,310	11,868
Treasury stock	-2,464	-2,378	-2,269	-2,171	-3,059
Total accumulated other comprehensive income	-76	153	349	3	119
Net assets, total	12,780	14,716	14,702	15,849	17,635
Total liabilities and net assets	72,701	86,615	95,140	117,295	130,141

Source: the Company’s financial results summary

Consolidated cash flow statement

(unit: ¥mn)

	FY3/11	FY3/12	FY3/13	FY3/14	FY3/15
Cash flow from operating activities	6,723	7,127	2,885	6,243	5,831
Cash flow from investing activities	-8,269	-9,694	-6,422	-14,510	-8,437
Cash flow from financing activities	1,109	7,920	5,496	8,782	1,422
Cash and deposits balance at start of fiscal year	7,636	7,200	12,554	14,513	15,027
Cash and deposits balance at end of fiscal year	7,200	12,554	14,513	15,027	13,844

Source: the Company’s financial results summary

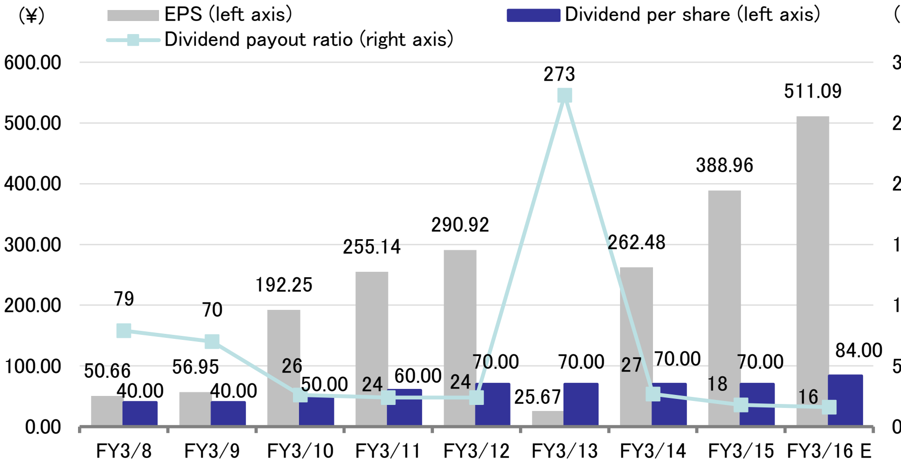
Returns to shareholders

Increased the dividend by a further ¥4 based on the Q1 results

The Company's basic approach to shareholder returns is to pay dividends linked to business performance while ensuring it maintains the internal reserves necessary for growth.

In FY3/15, the Company paid a dividend per share of ¥70 (interim dividend of ¥35 and year-end dividend of ¥35). In FY3/16, it has announced that it plans to pay an interim dividend of ¥40 and then subsequently a dividend of ¥22 at the end of the fiscal year following the two-for-one stock split carried out on October 1, 2015. This represent an annual divided of ¥84 when adjusted for the stock split and returned to the same level as the previous fiscal year, so in actuality it constitutes a dividend increase of ¥14. The Company initially announced that it would provide an annual dividend of ¥80 for a ¥10 increase, but it decided to increase the dividend by an additional ¥4 based on the Q1 results. So it is matching its actions to its words and is implementing its basic policy of providing returns to shareholders according to profits. So as a company that is highly aware of returns to shareholders, further returns can be expected from it in the future.

Trends in EPS, dividend per share, and the dividend payout ratio



Note: the Company implemented a two-for-one stock split on October 1, 2015, but the EPS and dividend per share in the graph do not take into account this stock split.

Source: the Company's financial results summary

Disclaimer