

VALTES CO., LTD.

4442

Tokyo Stock Exchange Growth Market

25-Jul.-2023

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FISCO Ltd.

<https://www.fisco.co.jp>

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Summary

Company specializes in software testing, features a unique education method, and has major potential for growth in expanding market

VALTES CO., LTD. <4442> (hereafter, also “the Company”) was established in 2004 by its current President and Representative Director Shinji Tanaka. Mr. Tanaka had been managing a general software house, but had concerns and misgivings that the test market in Japan for third-party evaluation of software was immature and leading to low quality, high cost software, and his desire to enhance the quality of software in the world inspired him to establish the Company. Since then, the Company has been involved in numerous software testing projects, while also focusing on in-house engineer training and establishing a unique education method. Since most software tests are often done internally by software vendors even now, and software testing by external companies is a developing market, it can be said the Company also has significant future growth potential.

1. FY3/23 consolidated results

In the FY3/23 consolidated results, net sales were ¥9,059mn (+35.1% YoY), operating profit was ¥970mn (+70.1%), ordinary profit was ¥982mn (+69.4%), and profit attributable to owners of parent was ¥651mn (+57.4%). In key performance indicators (hereafter, “KPIs”), the “average unit price” (monthly net sales per engineer) came to ¥740,000 (+¥44,000 YoY), the number of engineers in operation at the end of FY3/23 was 1,157 (+229 YoY), and the number of projects during FY3/23 was 3,868 (+503), all marking record highs. The gross profit margin improved to 29.8% (from 27.8% the previous fiscal year), but this was primarily due to increases in large projects with high profitability and from the enterprise domain. At the same time, SG&A expenses increased 33.8% YoY, though this was within expectations, and it was offset by gross profit increasing on higher sales, so operating profit increased by a large margin.

2. FY3/24 consolidated forecasts

For the FY3/24 consolidated results, the Company is forecasting net sales of ¥11,178mn (+23.4% YoY), operating profit of ¥1,228mn (+26.7%), ordinary profit of ¥1,233mn (+25.5%) and profit attributable to owners of parent of ¥833mn (+28.0%), as it continues working to increase its KPIs. In the mainstay software tests segment, the Company will work to further increase the size of projects and raise the unit price by expanding and deepening enterprise projects. In the web/mobile app development segment, it will expand the security business, activity introduce new technologies and move forward on high-quality development. In the offshore segment, the Company will continue to train engineers and further increase quality. The results of Sinfo Co., Ltd., which became a subsidiary in April 2023, are also expected to contribute.

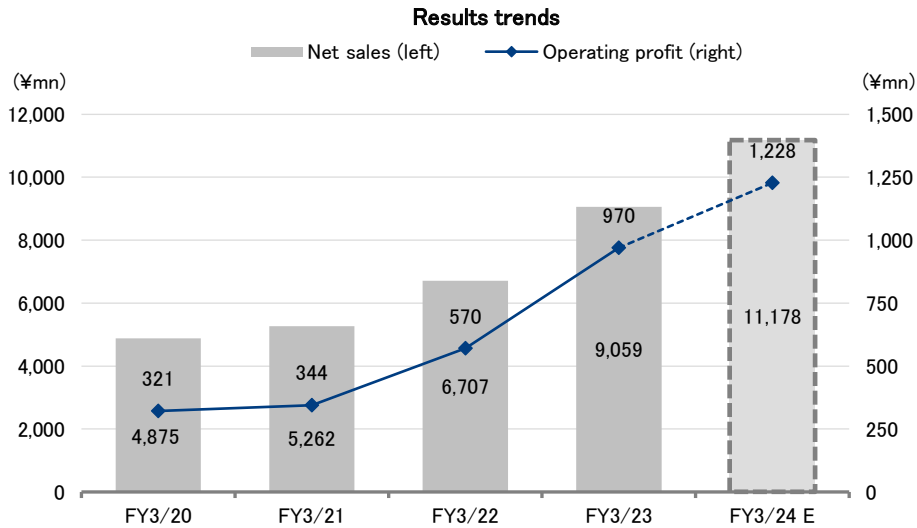
3. Growth strategy

In the Japanese software testing market, software vendors are still conducting a lot of tests in-house, but it is also true that there is a growing need for outsourcing. Therefore, outsourcing to specialized companies like the Company is expected to increase moving ahead. Against this backdrop, the Company plans to achieve both growth in scale and high profitability by controlling investments and implementing four basic strategies ((1) investment in human capital, (2) expansion of enterprise domain, (3) expansion of intellectual property, and (4) M&A and organizational strengthening). The Company has set net sales of ¥10bn in FY3/24 as a quantitative target, which is no doubt already within range, and it plans to announce its new medium-term management plan in FY3/24 2H.

Summary

Key Points

- Mainstay business is software testing services. Targets growth in step with market expansion
- In FY3/23, net sales increased 35.1% and operating profit 70.1% YoY
- Medium-term strategic target of net sales of ¥10bn in FY3/24 is well within range



Source: Prepared by FISCO from the Company's financial results

■ Company overview

Software testing specialist, with unique employee education method among its strengths

The Company was established in 2004 by its current President and Representative Director Shinji Tanaka. Before that, Mr. Tanaka was managing a general software house. At the time, many software houses and IT vendors were conducting software tests in-house. Therefore, assessments inevitably tended to be lenient. As a result, the quality of the deliverables—software—was low, while the cost was high. Mr. Tanaka had concerns and misgivings about such things, and his desire to enhance the quality of software in the world inspired him to establish the Company for the purpose of specializing in software testing. The Company's name, VALTES, comes from "Value Created through Testing."

Company overview

Ever since, the Company has stayed on its path as a software testing specialist, taking part in numerous software testing projects, while also concentrating on in-house engineer education and establishing a unique education method. As a software testing specialist, the Company is currently handling lots of requests for testing from wide array of customers, including users and IT vendors. Although much of software testing is still conducted internally by software vendors and the like, and software testing by external companies is a developing market, there has recently been growing awareness of software testing conducted by external companies. It can therefore be said that the software testing market is developing, and the Company's growth potential is significant.

Regarding the stock, the Company listed on Tokyo Stock Exchange (hereafter, "TSE") Mothers Market in May 2019, and moved to the Growth Market accompanying the TSE's market reorganization in April 2022. The Company currently aims to move to the Prime Market.

History

Date	Major event
April 2004	VALTES CO., LTD. established
December 2008	Obtained ISO 27001 information security management system certification
October 2012	Group company VALTES Mobile Technology Co., Ltd. (VMT) established
February 2014	Group company VALTES Advanced Technology, Inc. (Philippines) established
December 2015	Certified as a "Platinum Partner" in the ISTQB Partner Program
December 2017	Certified as a "Global Partner" in the ISTQB Partner Program
May 2019	Listed on the Tokyo Stock Exchange Mothers Market.
August 2020	Made RSR Co., LTD. a subsidiary
November 2021	Released beta version of T-DASH test automation tool
February 2022	Released official version of T-DASH test automation tool
March 2022	Launched Prime WAF, a cloud-based WAF
April 2022	Moved to the Growth Market accompanying the Tokyo Stock Exchange's market reorganization Made Mint CO., LTD. a subsidiary
August 2022	Launched AnyTest capable of remotely controlling actual smartphones via a cloud platform
April 2023	Sinfo made a subsidiary Released the open beta version of QualityTracker, a test management tool that tracks quality

Source: Prepared by FISCO from the Company's website

Business description

Mainly engaged in software testing, but also develops web/mobile apps

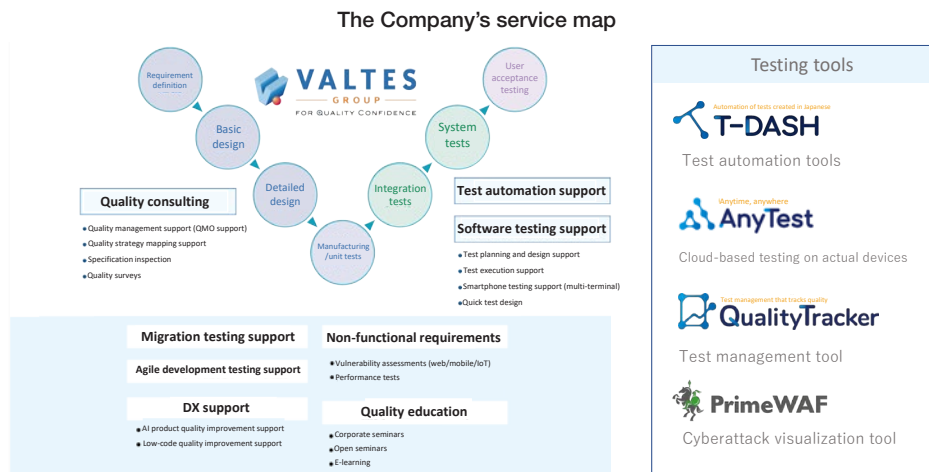
1. Business description and segment overview

The Company's three reporting segments are software tests, web/mobile app development, and offshore.

(1) Software tests segment (90.6% share of FY3/23 net sales)

a) Business domain and workflow

The software tests segment provides a wide range of software testing services from an independent, third-party perspective so user companies, manufacturers, and software vendors can avoid risks by bringing to light any software problems. Its services extend from drafting quality plans in the development process to improving the development process, and discovering software issues. It also handles everything from planning tests, designing tests, preparing test cases, conducting tests, and preparing test summary reports to verify that there are no serious problems with software. A feature of the segment is that it covers extensive ground in software development, from the upstream to downstream.



Source: The Company's results briefing materials

The Company's scope of service provision is extensive, from enterprise (business systems, core systems, etc.) to embedded (AV devices, consumer electronics, industrial equipment, etc.), web/smartphone (websites, mobile applications, etc.), and other domains. Among them, profit margins are relatively high for enterprise-related work, so the Company aims to expand in that field going forward.

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Business description

Comparison matrix of test processes in peripheral markets

		Potential market scale	Market stage	Barriers to entry
Test Process market	Enterprise domain	Huge	Startup	High
	Embedded domain	Big	Startup	High
	Web/smartphone domain	Medium	Growth	Medium
	Entertainment domain	Small	Maturity	Low

VALTES's business domain

Source: The Company's "Business Plan and Growth Potential Explanatory Material"

The Company's testing is also not limited to functionality and determining whether or not planned operations are carried out accurately. Rather, it meets an array of testing needs. For instance, tests of access based on the number of users assuming actual operation, tests concerning the accumulation, continuity, and durability of data from ongoing business activities, and tests to discover potential for things like the leakage of personal information due to software malfunctions and the discovery of software vulnerabilities.

b) Main services, forms of provision, and contract types

The Company's main services are diverse, and include software testing, quality consulting, software quality seminars, digital broadcasting testing, security and vulnerability assessment, reverse engineering, and publishing, information dissemination, and site operation.

Major services provided

Software testing	From single function testing to system testing support, multiple device testing, test automation, and acceptance test support, the Company's engineers with specialist expertise conduct various software tests on behalf of customers, working out the best test patterns according to the objective, and providing testing services supporting the quality of applications, systems, and more to a wide assortment of industries.
Quality consulting	Whereas software testing services entail testing software that has already been developed, quality consulting services involve supporting quality management, such as by establishing and standardizing quality assurance processes for the entire software development process including upstream processes, as a project management office (hereafter, "PMO") for quality or quality management office (QMO).
Software quality seminars	The Company's engineers also provide software quality education seminars for customers' developers, quality managers, project leaders, project managers, and so forth. The Company currently offers 15 educational courses. It has also created English language versions of some content, and training in English is also possible.
Digital broadcasting testing	The Company provides a wide variety of digital broadcasting testing services, not just functional testing for receivers, but also services such as specification testing to determine if systems are in line with broadcasting standards, tests of abnormal conditions not specified in standards, and creation of data for testing.
Security and vulnerability assessment	This includes the provision of SaaS-based WAF services, and diagnostics to check if web systems, mobile applications, or IoT devices are susceptible to external intrusions (hacking). The Company and its subsidiary VALTES Mobile Technology Co., Ltd. both provide these services.
Reverse engineering	For software with no documentation, the Company creates documents from the software and tests the software according to those documents.
Publishing, information dissemination, and site operation	For everyone involved in software development, the Company operates a website conveying information that goes beyond software quality improvement to information on industry trends, management methods, and other valuable information needed by engineers. It also publishes books for engineers, including the new books "Ichiban Yasashii Sofutoea Tesuto No Hon" (rough translation: the easiest software book) and "Sofutoea Tesuto No Kyokasho" (software test textbook).

Source: Prepared by FISCO from the Company's securities report

Business description

The Company provides software testing services in two ways, through “test center testing services” where it sets up a test center in the Group and establishes a test environment according to customer needs, and through “on-site testing services” where it provides (dispatches)* personnel tailored to customer needs.

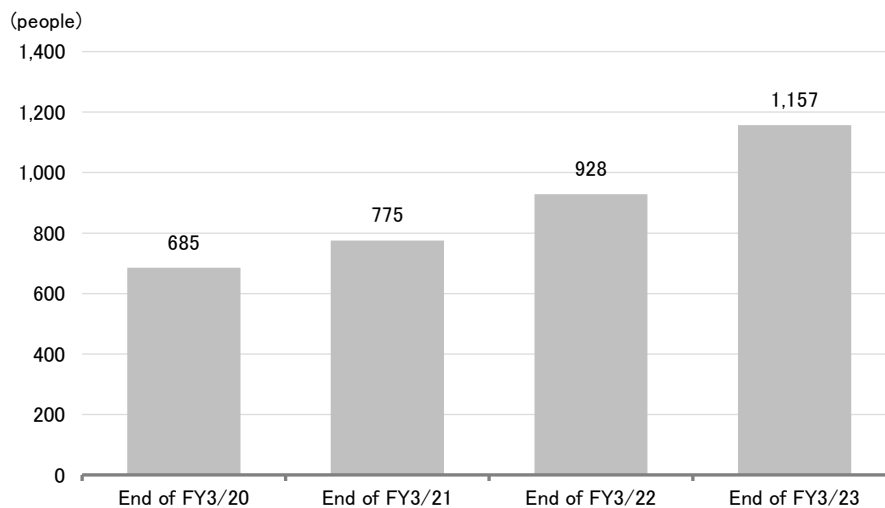
| * The Company has a general worker dispatch business license. |

The Company offers three types of contracts: “dispatch contracts” where the Company’s engineers are dispatched to provide services under the instruction of customers based on dispatch worker contracts, “quasi-consignment contracts” where services are provided under the instruction of the Company according to the content of agreements with customers, and “consignment contracts” where tests are mainly conducted at the Company’s test center and test summary reports and other deliverables are delivered to customers. At present, the majority of contracts are quasi-consignment contracts.

c) KPIs

The Company needs engineers to work on the projects it has acquired, and its engineer numbers are an important factor for its business. The Company’s engineer numbers are equivalent to manufacturers’ production capacity. By increasing its engineers with a certain level of knowledge and experience, the Company increases its production capacity, which, as a result, leads to sales growth. In addition to regular employees and contract employees, the Company’s engineers include what it refers to as business partners. At the end of FY3/23, the number of engineers in operation was 1,157, with a breakdown being 551 regular employees (47.6% of the total), 128 contract employees (11.1%), and 478 business partners (41.3%), and the total number of engineers has steadily grown over the past four years.

Trends in the number of engineers

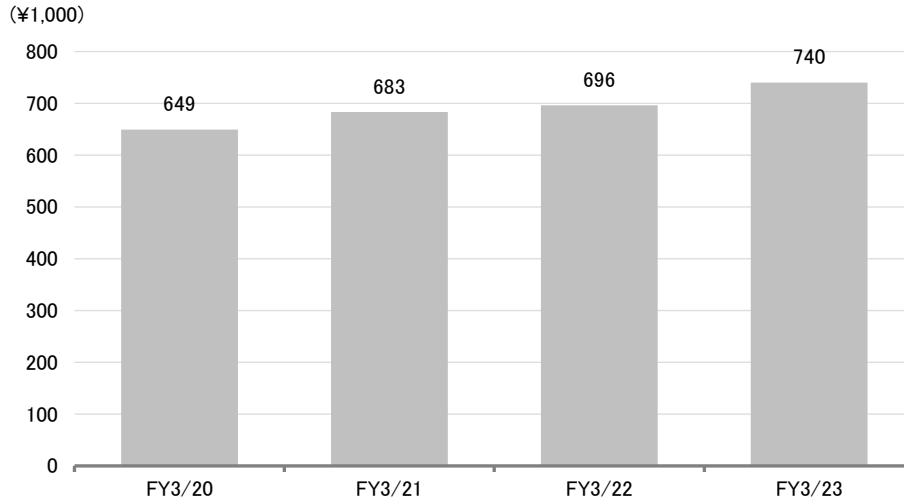


Note: The number of engineers is the total number of regular employees, contract employees, and business partners
 Source: Prepared by FISCO from the Company’s results briefing materials

The second important factor is net sales per engineer. The Company defines that figure as the “unit price (monthly),” which is “net sales in the software tests segment ÷ the number of engineers.” The unit price declined in FY3/20, partly due to impact from the COVID-19 pandemic, but rose steadily thereafter. The unit price in FY3/23 was ¥740,000.

Business description

Trends in the unit price

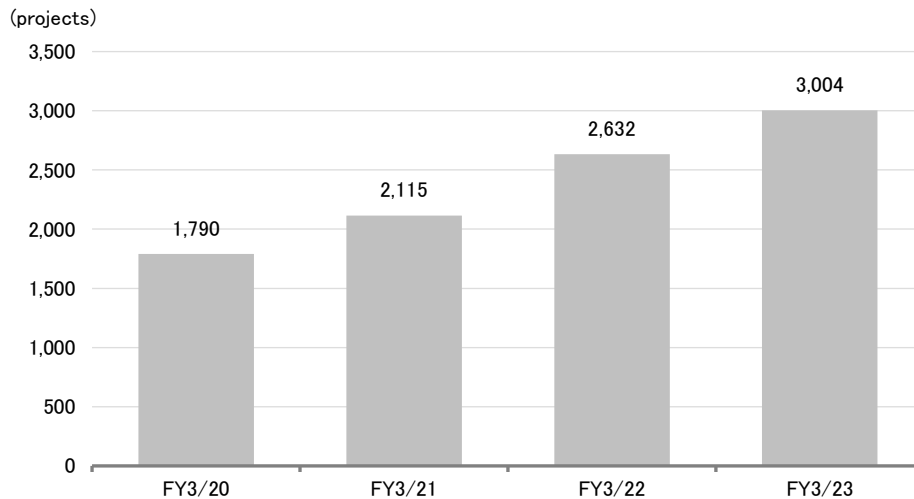


Note: Unit price = net sales in the software tests segment ÷ the number of engineers (regular employees + contract employees + business partners)
 Source: Prepared by FISCO from the Company's results briefing materials

The third factor is the number of projects. The Company handles most work under quasi-consignment contracts, and has few consignment contracts where there is a risk of projects becoming unprofitable. Fundamentally, contracts are concluded for each project. However, there are also lots of cases where requests from customers lead to continuing agreements, such as when there are a succession of development projects or development issues, and when there are updates of systems for which an order was received once. That can also be said to be a significant barrier to entry. The order amount varies by project, and its range is wide from several millions to several tens of millions of yen. When projects are continued, however, they sometimes end up generating sales in the hundreds of millions of yen from the customer. Since cumulative sales from those projects account for the bulk of the segment's net sales, it is fair to say that the number of projects is one KPI for the Company's earnings. There were 3,004 projects (software tests) in FY3/23, and the number of projects has been steadily expanding over the past four years.

Business description

Trends in the number of projects



Source: Prepared by FISCO from the Company's results briefing materials

d) Reasons for outsourcing test process

One reason that customers ask (place orders with) outside companies like the Company to perform software tests is that general system engineers do not receive systematic education about testing and are not test professionals, so it is inefficient for them to do the work. In particular, subcontracted small-scale Sler tend to have the engineers that developed the software conduct testing. However, it is said to generally be difficult to objectively conduct tests on programs that you created yourself. It is like how magazine writers and reporters overlook more issues when editing and proofreading their own work. Furthermore, few developers know systematic and exhaustive testing methods, and developers don't like testing work itself, so having developers handle the testing process often ends up prolonging the testing process and reducing quality (launches with undiscovered bugs). To resolve those issues, outsourcing to external companies has been advancing in recent years.

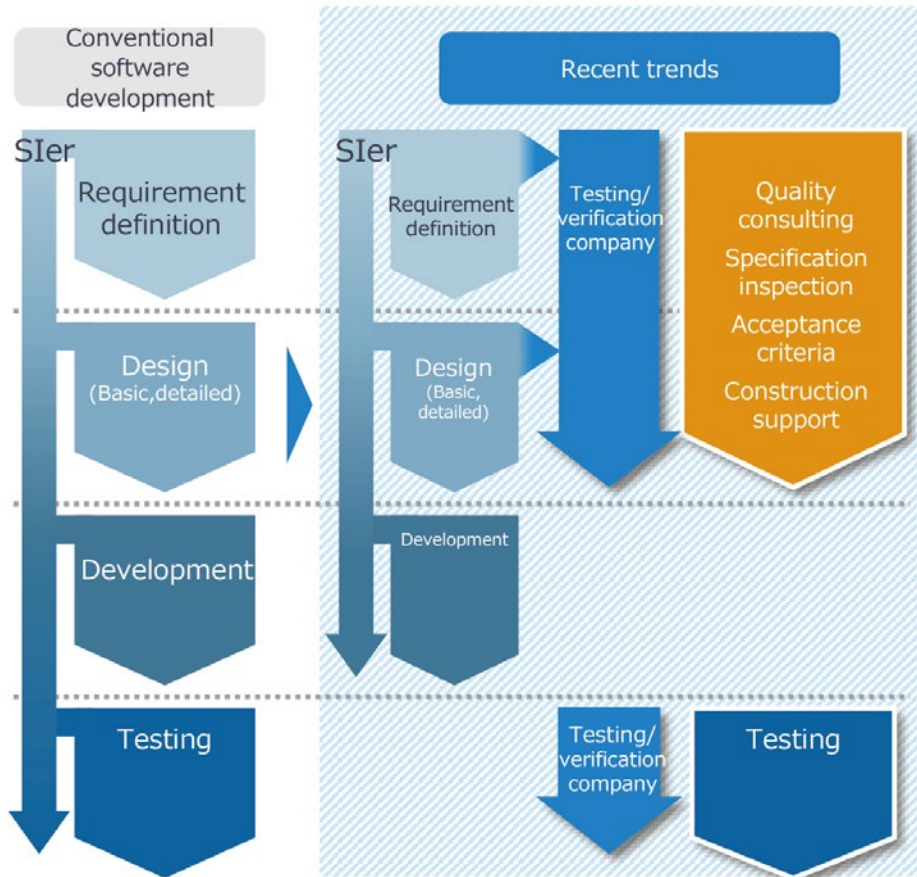
The second reason for outsourcing is that there is currently a shortage of engineers in Japanese IT industry. The Japanese IT market is expected to continue to grow in the future, driven by digital transformation (DX) initiatives. On the other hand, it is also true that there is a shortage of engineers, and many Sler are often receiving inquiries but having difficulty accepting orders due to insufficient staffing. In this situation, if they were to outsource the testing process, which accounts for over 37% of the entire development process, the freed-up resources would enable them to accept orders for new development projects. Also, it is true that major Sler, users, and others are increasingly outsourcing the testing process since in addition to things like shortening the process timeline and assuring quality, it enhances productivity by optimizing human resources.

The third reason is that promoting DX puts added burden on user companies. When the redevelopment of company systems or introduction of new package systems are consigned to a systems integrator or package vendor, acceptance testing needs to be conducted at the user company. Acceptance testing has to be appropriately conducted by users with the limited number of IT personnel they have on staff, and with DX investment heating up in recent years, this has put a very large burden on companies. To lessen this burden, there are increasing cases of user companies outsourcing acceptance testing processes and comprehensive testing support covering each process and quality management to an independent dedicated testing provider.

Business description

It can be said that the shift to outsourcing software testing due to this situation is likely to increase further going forward.

Changes in software development workflow



Source: The Company's results briefing materials

(2) Web/mobile app development segment (9.0% share of FY3/23 net sales)

The consolidated subsidiary VALTES Mobile Technology Co., Ltd. develops web/mobile apps, and provides security diagnostics (vulnerability assessments). In web/mobile app development, it can provide one-stop services from planning to requirement definition, design, release, and operation. Also, the Group's management policy is to raise the quality of software, and secure coding based on education from the Company's security service team is practiced in providing software development services. In security diagnostics services, it provides safety investigations. Skilled engineers' diagnostics expertise is used to create procedures that can discover latent vulnerabilities. Additionally, the consolidated subsidiary Real System Research Co., LTD. undertakes operations such as developing computer software, developing systems on a consignment basis, and dispatching development personnel.

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Business description

(3) Offshore segment (0.4% share of FY3/23 net sales)

The consolidated subsidiary VALTES Advanced Technology, Inc., which mainly operates in the Philippines, shares know-how with Group companies to provide software testing and software development services to customers, including software vendors and manufacturers. With an inexpensive, ample local labor force, local engineers that have undergone training with the Company’s educational content provide services to customers such as Japanese companies and Japanese companies in the Philippines with VALTES Advanced Technology as the point of contact.

The Company actively conducts M&A as well, and it made Mint CO., LTD. a subsidiary in April 2022 and Sinfo a subsidiary in April 2023.

The Company has announced that it will be changing to a holding company structure in October 2023. The change was approved at the Company’s annual general meeting of shareholders held in June 2023. The purpose of the change is to 1) strengthen business that provides the value of raising software quality, 2) strengthen Group governance, and 3) train and develop personnel for executive management.



Source: The Company's results briefing materials

(4) Main intellectual property investments

In addition to services for each project, the Company also offers subscription-based services. While the amount of those sales is not disclosed because it is yet small in scale, growth looks promising and conditions going forward will be under focus.

a) Qbook testing information platform

This platform is for improving software quality. The Company provides the testing and quality enhancement expertise it has amassed free of charge, with the aim of increasing its recognition, educating personnel contributing to ICT society, and so on.

b) T-DASH test automation software

This test automation tool enables even non-engineers to easily check and verify the operation of web applications

c) PrimeWAF pay-as-you-go cloud-based WAF

This simple, low-cost cloud-based web application firewall (WAF) service protects websites from an array of cyberattacks.

d) AnyTest for testing actual equipment anytime, anywhere

This tool enables actual equipment to be operated remotely via a cloud platform. With an extensive model and OS lineup, it features remote yet lag-free operation.

Business description

2. Features, strengths, and competition

The Company's core business is software testing services, and its features and strengths are described below.

(1) Robust experience, knowledge, and insight as a specialized company

As previously mentioned, the Company has continued to engage in software testing business as a specialized company since it was established in 2004 for the purpose of providing software testing services. It has therefore accumulated a wealth of experience and specialist knowledge and insight during this time. Regarding its expertise, it is fair to say the Company has leading technological capabilities in Japan, including having been the first in Japan to obtain Global Partner status for the international certification ISTQB*. This high level of expertise as well as experience and knowledge are creating strong relationships of trust with customers, and that is no doubt one of the Company's strengths.

* Abbreviation for International Software Testing Qualifications Board, an organization for certifying software testing professionals in 130 countries around the world. Only 7 companies in the world are a Global Partner, and the Company is the first in Japan.

(2) Offers testing services for all software development processes

The Company provides testing services covering the entire software development process, from the upstream tasks of requirement definition, basic design, detailed design, manufacturing and unit tests, combined tests, and system tests to the downstream task of user acceptance tests. It can therefore provide one-stop solutions for customers, which is also no doubt one of its strengths.

(3) Unique education method

It goes without saying that number and quality of engineers are an important factor for the Company's business. The Company has established a unique, systematic education method (training curriculum) leveraging the experience and insight gained since its founding to secure high-quality engineers. New graduates without experience undergo 320 hours of training per month and mid-career hires with experience 160 hours per month after joining the Company, concentrating only on training for the first two months after entering the Company and not conducting any regular business during that time. This unique education method aims to quickly turn engineers into competitive forces, while maintaining high skills. As a result, 92% of engineers that have been with the Company for two years or longer have JSTQB* certification. This kind of education method cannot be established in a short period of time, and is one of the Company's strengths as well as a barrier to entry.

* Abbreviation for Japan Software Testing Qualifications Board, a certification organization for software testing professionals in Japan.

(4) Competition

Competitors in the software testing market include SHIFT Inc. <3697> and VeriServe Corporation (SCSK Corporation's <9719> subsidiary). While their respective market shares are unclear due to the lack of accurate data, the market itself is growing, so the Company apparently faces little direct competition from them. Rather, it can be said that the Company's biggest competition is from the in-house market (Sler, users conducting tests internally, etc.). Since the outsourcing ratio in the software testing market is still low, it appears that the market itself is expanding more than those companies are competing with each other.

Business performance

In FY3/23, main KPIs performed well and operating profit increased sharply to a new record high

1. Overview of FY3/23 results

(1) Profit and loss conditions

In the FY3/23 consolidated results, net sales were ¥9,059mn (+35.1% YoY), operating profit was ¥970mn (+70.1%), ordinary profit was ¥982mn (+69.4%) and profit attributable to owners of parent was ¥651mn (+57.4%), with profits setting new record highs.

In the main KPIs, the “average unit price” (software testing) was ¥740,000 (¥696,000 the previous fiscal year), the number of engineers in operation as of the end of FY3/23 was 1,157 (928 the previous fiscal year), and the number of projects during FY3/23 was 3,868 (3365 the previous fiscal year), all of which were record highs.

The gross profit margin improved 29.8% (27.8% the previous fiscal year), and this was mainly attributable to an increase in large projects and an increase in the enterprise domain. At the same time, SG&A expenses increased 33.8% YoY (+437mn), but this was in line with expectations and less than the growth rate in gross profit, so operating profit increased by a large margin.

The main factors behind the increase in SG&A expenses were an increase in personnel expenses of ¥105mn, an increase in recruiting expenses of ¥130mn, and an increase in other expenses of ¥246mn. Other expenses included an increase in M&A-related expenses of ¥99mn and an increase in site expansion expenses of ¥24mn.

Analyzing the factors contributing to the change in operating profit shows higher sales boosted profit by ¥654mn (with boosts of ¥613mn in the software tests segment, ¥36mn in the web/mobile app development segment and ¥4mn in the offshore segment), improvement in the gross profit margin buoyed profit by ¥183mn (with boosts of ¥115mn in the software tests segment, ¥72mn in the web/mobile app development segment and a decrease of ¥4mn in the offshore segment), and a rise in SG&A expenses (with personnel expenses up ¥105mn, recruiting expenses up ¥130mn, R&D expenses down ¥44mn, and other expenses up ¥246mn) depressed profit by ¥437mn.

FY3/23 consolidated results

(Unit: ¥mn)

	FY3/22		FY3/23		YoY
	Result	% of net sales	Result	% of net sales	
Net sales	6,707	100.0%	9,059	100.0%	35.1%
Gross profit	1,865	27.8%	2,703	29.8%	44.9%
SG&A expenses	1,295	19.3%	1,733	19.1%	33.8%
Operating profit	570	8.5%	970	10.7%	70.1%
Ordinary profit	580	8.6%	982	10.9%	69.4%
Profit attributable to owners of parent	413	6.2%	651	7.2%	57.4%

Source: Prepared by FISCO from the Company's financial results

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Business performance

Equity ratio of 58.9%, cash on hand of ¥1.5bn

(2) Financial condition

As for the Company's financial condition at the end of FY3/23, current assets totaled ¥2,894mn (+¥548mn from the end of FY3/22). This mainly reflected an increase in cash and deposits of ¥178mn and an increase in accounts receivable – trade and contract assets (including electronically recorded monetary claims) of ¥299mn. Non-current assets were ¥1,194mn (+¥609mn). Key factors were an increase in property, plant and equipment of ¥95mn, an increase in intangible assets of ¥254mn, which was primarily from an increase in goodwill, and an increase in investments and other assets of ¥259mn. As a result, total assets came to ¥4,089mn (+¥1,158mn).

Total liabilities were ¥1,682mn (+¥464mn from the end of FY3/22). This chiefly owes to an ¥134mn increase in accounts payable – trade, and a ¥26mn decrease in long-term and short-term borrowings. Total net assets were ¥2,406mn (+¥693mn), mainly due to a ¥651mn increase in retained earnings from the recording of profit attributable to owners of parent. As a result, the equity ratio was 58.9% (compared to 58.4% at the end of FY3/22).

Consolidated balance sheets

	(Unit: ¥mn)		
	End of FY3/22	End of FY3/23	Change
Cash and deposits	1,356	1,535	178
Notes and accounts receivable - trade, and contract assets (including electronically recorded monetary claims)	919	1,215	299
Total current assets	2,345	2,894	548
Property, plant and equipment	89	185	95
Intangible assets	197	451	254
Goodwill	64	350	286
Investments and other assets	298	558	259
Total non-current assets	585	1,194	609
Total assets	2,930	4,089	1,158
Accounts payable – trade	175	310	134
Short-term borrowings	141	136	-5
Accounts payable – other	387	556	169
Total current liabilities	1,159	1,648	489
Long-term borrowings	54	32	-21
Total non-current liabilities	58	33	-24
Total liabilities	1,217	1,682	464
Retained earnings	1,067	1,719	651
Total net assets	1,712	2,406	693

Source: Prepared by FISCO from the Company's financial results

(3) Status of cash flows

In FY3/23, net cash provided by operating activities was ¥846mn. The main inflows included ¥981mn in profit before income taxes, ¥72mn in depreciation, and a ¥135mn increase in trade payables. The main outflows included a ¥279mn increase in trade receivables and contract assets.

Net cash used in investing activities was ¥639mn. The main outflows included ¥130mn for the purchase of investment securities, ¥108mn in payments of leasehold and guarantee deposits and ¥296mn for the purchase of shares of subsidiaries resulting in change in the scope of consolidation. Net cash used in financing activities was ¥29mn. This was mainly from ¥21mn for repayments of long-term borrowings. As a result, cash and cash equivalents increased ¥178mn to ¥1,515mn at the end of FY3/23.

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Business performance

Consolidated statements of cash flows

	FY3/22	FY3/23
	(Unit: ¥mn)	
Cash flows from operating activities	505	846
Profit before income taxes	580	981
Depreciation	52	72
Decrease (increase) in trade receivables and contract assets	-176	-279
Decrease (increase) in works in process	28	-
Increase (decrease) in trade payables	59	135
Cash flows from investing activities	-104	-639
Purchase of property, plant and equipment	-10	-98
Purchase of investment securities	-62	-130
Payments of leasehold and guarantee deposits	-	108
Purchase of shares of subsidiaries resulting in change in scope of consolidation	-	-296
Cash flows from financing activities	-235	-29
Repayments of long-term borrowings	26	26
Net increase (decrease) in cash and cash equivalents	166	178
Cash and cash equivalents at end of period	1,336	1,515

Source: Prepared by FISCO from the Company's financial results

2. FY3/23 performance by segment

FY3/23 earnings by segment

	FY3/22		FY3/23		
	Result	% of net sales	Result	% of net sales	% change
Net sales	6,707	100.0%	9,059	100.0%	35.1%
Software testing services	5,998	89.4%	8,205	90.6%	36.8%
Web/mobile app development	683	10.2%	813	9.0%	19.0%
Offshore	24	0.4%	40	0.4%	62.9%
Operating profit	570	8.5%	970	10.7%	70.1%
Software testing services	568	-	977	-	72.0%
Web/mobile app development	70	-	71	-	1.6%
Offshore	10	-	0	-	-99.2%
Adjustment amount	-78	-	-78	-	-

Note: Net sales do not include internal sales or transfer amounts
 Source: Prepared by FISCO from the Company's financial results

(1) Software tests segment

In the software tests segment, net sales increased 36.8% YoY to ¥8,205mn, and operating profit rose 72.1% to ¥977mn.

The number of projects steadily expanded to 3,004 (+14.1% YoY), with the acquisition of many large projects (¥100mn or more annually) in particular leading to sales growth. Net sales from large projects were ¥4,117mn (+66.1%), accounting for 50.1% of the total. Projects are becoming larger primarily due to increased participation in the upstream processes of new large reconstruction projects as the PMO*1 and QMO*2 and in migration projects*3.

*1 Abbreviation for project management office, a department or structural system that supports management of individual projects across the organization.

*2 Abbreviation for quality management office, a department or structural system that supports management of individual aspects of quality across the organization.

*3 Migration means moving software, systems, data, and so forth to a different environment or switching to a new environment.

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Business performance

The “unit price” was ¥740,000 (+¥44,000). Key factors were growth in the share of sales accounted for by the enterprise domain, active hiring of PMO personnel, aggressive proposal of test automation installation support, and existing customers’ ongoing strong performance. Also, the number of active personnel increased steadily by 204 people to 998 people, owing to an increase in the number of applicants, strengthening of relationships with business partners, and steady collaboration with joining companies.

(2) Web/mobile app development

In the web/mobile app development segment, net sales rose 19.0% YoY to ¥813mn, and operating profit edged up 1.6% to ¥71mn, so profit was nearly the same as the previous year. In addition to growth in sales of app development and reverse engineering services*, sales related to security and vulnerability assessment were also brisk. On the profit front as well, operating profit was secured since an unprofitable project in the previous fiscal year dropped out.

* Services entailing creating development documents (all kinds of design documents) by deciphering source code, system operations, and so forth.

(3) Offshore segment

In the offshore segment, net sales increased 62.9% YoY to ¥40mn, and operating profit declined 99.2% to ¥0mn. Despite an uptrend in inquiries from local Japanese companies in the Philippines, the scope of transactions contracted and profit declined from the lingering impact of the COVID-19 pandemic.

3. Topics for FY3/23
(1) Release of open beta version of QualityTracker

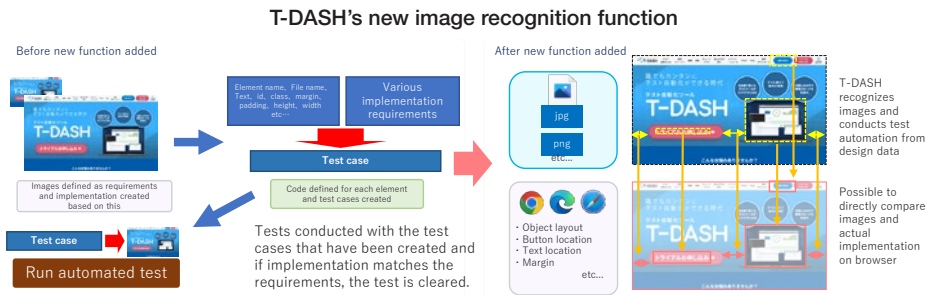
The Company released the open beta version of QualityTracker (QT), a test management tool that tracks quality, on April 3, 2023. QT makes it possible to manage progress and test cases when tests are conducted on a cloud basis. The progress of each test is displayed in real time, allowing progress to be managed accurately. The tool is also expected to greatly reduce administrator costs.

In terms of features, QT enables 1) more accurate progress management, 2) test cases to be shared (reused) as assets within project teams, 3) more efficient testing, and 4) real time calculations. Based on the Company’s project track record, a 30% reduction in administrator manhours can be expected. The tool is provided on a cloud basis, so a monthly fee is charged per license. The beta version has been provided free of charge until June 30, after which, starting in July, the Company plans to officially begin collecting fees, though this has not been included in results forecasts for the year.

(2) Industry-academia partnership with the Kyoto Institute of Technology

Through an industry-academia partnership with the Kyoto Institute of Technology, the Company succeeded in developing a new image recognition function for T-DASH. With development methods and processes diversifying, test automation is one means of creating development worksites that contribute to business more efficiently, but there are many companies for which this has not been effective because of over-reliance on individual abilities. The Company therefore conducted joint research on test automation using the T-DASH test automation tool in order to free companies from over-reliance on individual abilities in test automation.

Business performance



Source: Prepared by FISCO from the Company's results briefing materials

(3) Relocation and expansion of Tokyo Head Office and expansion of Osaka Head Office

The Group relocated and expanded its Tokyo Head Office in February 2023 and expanded its Osaka Head Office in March in order to enhance the work environment, increase employee well-being and improve its recruiting ability. At the Tokyo Head Office in particular, workspaces, break rooms, meeting rooms and other areas were developed with an emphasis on enhancing communication among employees with the overarching intention of creating an appealing office.

(4) Partnerships with other companies

The Company made minority investments in the following startup companies with a view to jointly increasing corporate value through sharing knowledge with corporations that possess intellectual property.

- FUNDINNO, Inc. (equity investment-based crowdfunding)

The Company provides knowledge related to quality and security. The aim is to further increase registered users and contracted projects by improving system quality.

- eXmotion Co., Ltd. (software development consulting)

Collaboration on an in-vehicle project. Jointly provide quality improvement services in upstream processes by defining improved processes with the addition of USDM*2 and the Company's as well as the W-model*1.

*1 A test model by which the development phase and test phase are simultaneously conducted from the initial stage of development.

*2 Abbreviation for universal specification describing manner, a specification technique for defining accurate requirements.

- between the arts, Inc. (collection item management platform)

Creation of new added value, app development, stronger synergies with security services.

■ Outlook

Forecasts FY3/24 operating profit growth of 26.7% YoY, advancing up-front investments looking to future growth

1. FY3/24 forecasts

For the FY3/24 consolidated results, the Company forecasts net sales of ¥11,178mn (+23.4% YoY), operating profit of ¥1,228mn (+26.7%), ordinary profit of ¥1,233mn (+25.5%), and profit attributable to owner of parent of ¥833mn (+28.0%). The Company has said that it will continue active investment in its advanced phase as well in order to achieve sustainable growth. It intends to prioritize investment for the future over short-term profit and will achieve its targets by conducting measures in each segment as described below.

FY3/24 consolidated forecasts

(Unit: ¥mn)

	FY3/23		FY3/24		
	Result	% of net sales	Forecast	% of net sales	YoY
Net sales	9,059	100.0%	11,178	100.0%	23.4%
Operating profit	970	10.7%	1,228	11.0%	26.7%
Ordinary profit	982	10.9%	1,233	11.0%	25.5%
Profit attributable to owners of parent	651	7.2%	833	7.5%	28.0%

Source: Prepared by FISCO from the Company's financial results

2. Key initiatives for FY3/24

(1) Software tests segment

The Company will conduct the following measures to expand and deepen enterprise projects, further increase project size and raise the unit price.

- Increase participation as the PMO/QMO from the upstream process of large projects and raise the unit price
- Increase orders from target sectors, including the financial industry
- Acquire orders for migration projects
- Increase orders of web service projects
- Strengthen coordination between in-house development tools. Raise business added value through in-house utilization.
- Strengthen M&A
- Strengthen the functions of divisions that hire regular employees
- Strengthen activities to acquire business partners

(2) Web/mobile app development segment

The Company plans to expand its security business and conduct high-quality development by actively deploying the latest technologies.

- Accelerate the capture of security demand
- Work to raise the unit price through high-quality development
- Develop new services using the metaverse
- Train personnel for business expansion

Outlook

(3) Offshore segment

The Company aims to increase quality by continuing to train engineers and deliver “Japan Quality” to the world.

- Work to increase transactions with local Japanese companies
- Continue active hiring and integrated Group training

Medium- to long-term growth strategy

Aiming for net sales of ¥11.1bn in FY3/24

1. Business environment

In terms of the Company’s future business climate (market expansion, etc.), it can be said that the following will be tailwinds.

(1) Target industry’s growth potential

Naturally, the Company will target markets including various kinds of software and the IT industry going forward, and the global software testing market’s compound annual growth rate (CAGR) is forecast at 12.4%, so the industry itself is likely to achieve strong growth.

Software testing market potential

	Scale of market			CAGR	Source
	Region	Year	Market Size		
Enterprise IT	Japan	2024	12.8 trillion yen	3.4%	IDC Japan Japanese enterprise IT market forecast
AI	Japan	2025	491.0 billion yen	25.5%	IDC Japan Japanese AI system market forecast
Metaverse	Global	2024	783.3 billion US dollars	13.1%	Bloomberg http://www.Bloomberg.com/professional/blog/metaverses-e-may-be-800-billion-market-next-tech-platform/
Web/e-commerce	Global	2024	4.9 trillion US dollars	20.7%	eMarketer, Dec2016 Infrastructure Development for a Data-Driven Society in Japan in FY2017 (Market Research on E-Commerce), Ministry of Economy, Trade and Industry
IoT	Japan	2025	10.2 trillion yen	10.1%	IDC Japan Yano Research Institute Ltd.
In-vehicle software	Japan	2025	1.1 trillion yen	4.5%	Yano Research Institute Ltd. Survey of the in-vehicle software market
Other Japanese and international software test related industries market scale combined with the overall global potential					
Software testing	Global	2025	34.49 billion US dollars	12.4%	Technavio Software Testing Services Market by Product, Geography, and End-user - Forecast and Analysis 2021-2025

Source: The Company’s results briefing materials

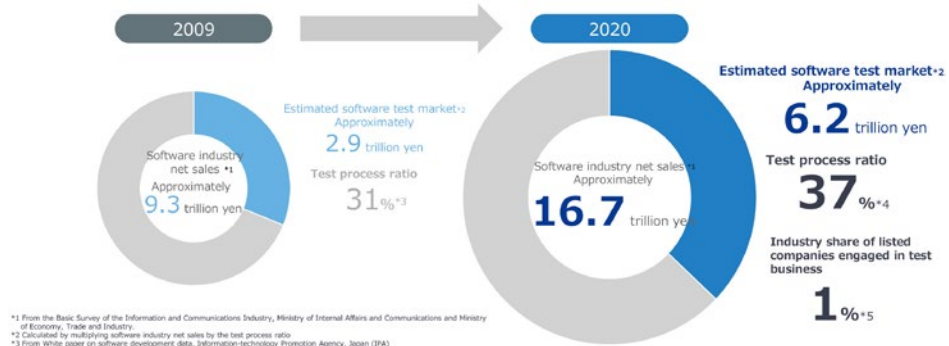
(2) Rise in outsourcing ratio for software tests

According to the Company’s research, the Japanese software industry’s net sales were ¥16.7tn in 2020, with an estimated roughly 37% (about ¥6.2tn) from testing processes. Moreover, listed companies including the Company only have a mere 1% share in the software test market, and, while some unlisted companies are performing tests, the majority are being handled in-house by Sler.

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Medium- to long-term growth strategy

Trends in the ratio of testing processes to software industry net sales and estimated market scale



*1 From the Basic Survey of the Information and Communications Industry, Ministry of Internal Affairs and Communications and Ministry of Economy, Trade and Industry.
 *2 Calculated by multiplying software industry net sales by the test process ratio.
 *3 From White Paper on Software Development Data, Information-technology Promotion Agency, Japan (IPA).
 *4 From Software Development Data Collection 2020, Information-technology Promotion Agency, Japan (IPA).
 *5 From the total sales of listed companies mainly engaged in the testing and debugging business.

Source: The Company's results briefing materials

For Sler, outsourcing these testing processes, which account for 37% of total development, frees up resources that can be diverted to new development projects, in addition to shortening the process timeline, ensuring quality, and leading to higher productivity via human resource optimization. Meanwhile, benefits for users include a reduction in personnel assigned to testing processes, quality maintenance, and a reduction in rework man-hours for Sler and development companies placing the orders. Given these points, the outsourcing ratio in the software testing market is expected to continue to rise moving forward, and is bound to be a tailwind for the Company.

2. Basic strategies

The Company plans on achieving both growth in scale and high profitability, mainly by implementing the four basic strategies of (1) investment in human capital, (2) expansion of enterprise domain, (3) expansion of intellectual property, and (4) M&A and organizational strengthening, as well as controlling investments.

(1) Investment in human capital

The Company will sustain growth by promoting proactive, systematic recruitment of human resources, quick turning of inexperienced human resources into competitive forces, advancement of seasoned personnel's skills, and effective use of external human resources.

(2) Expansion of enterprise domain

The Company aims to improve profit margins and build barriers to entry by advancing the establishment of specialized departments, hiring of high-level personnel, collaboration with external parties, and accumulation of knowledge.

(3) Expansion of intellectual property

The Company will build barriers to entry and create new value by promoting the accumulation of testing and training know-how, accumulation of knowledge, development of new technology, and investment in and collaboration with new technology companies.

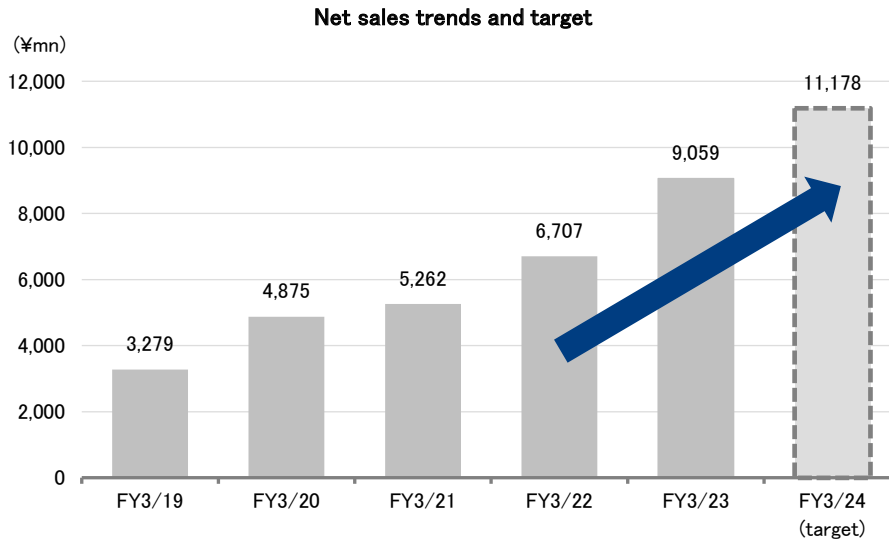
(4) Strengthening M&A and organizational structure

The Company aims to increase its sales, corporate value, and ability to respond to changes in the environment by advancing M&A in existing domains, portfolio diversification, optimization of M&A organizational structure, and improvement of Group governance.

Medium- to long-term growth strategy

3. Numerical targets

The Company has set net sales of ¥10.0bn in FY3/24 as a quantitative target. It achieved net sales of ¥9.05bn in FY3/23, and its forecast for net sales in FY3/24 is ¥11.1bn, so the target is already well within reach. The Company has said it plans to announce a new medium-term management plan in the second half of FY3/24, and we look forward to learning what the company plans for its next step.



Source: Prepared by FISCO from the Company's results briefing materials

Shareholder return policy

Announced an annual dividend of ¥12

Up to FY3/23, the Company had prioritized internal reserves for future growth and had not paid a dividend, but for FY3/24 it announced a policy of paying an annual dividend of ¥12. Going forward, we would expect the Company to continue a dividend policy that strikes a balance between internal reserves for growth and shareholder returns.



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