

Summary of Consolidated Financial Results
for the Second Quarter of the Fiscal Year Ending March 31, 2024
(Six Months Ended September 30, 2023)

[Japanese GAAP]

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Listing: Tokyo Stock Exchange
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Scheduled date of filing of Quarterly Report: November 7, 2023
 Scheduled date of payment of dividend: –
 Preparation of supplementary materials for quarterly financial results: Yes
 Holding of quarterly financial results meeting: None

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

1. Consolidated Financial Results for the Second Quarter Ended September 30, 2023

(April 1, 2023 – September 30, 2023)

(1) Consolidated operating results

(Percentages represent year-on-year changes)

	Net sales		Operating profit		Ordinary profit		Profit attributable to owners of parent	
	Million yen	%	Million yen	%	Million yen	%	Million yen	%
Six months ended Sep. 30, 2023	1,117	(16.3)	(342)	–	(345)	–	(595)	–
Six months ended Sep. 30, 2022	1,335	7.6	40	32.8	44	359.1	16	–

Note: Comprehensive income (million yen) Six months ended Sep. 30, 2023: (595) (–%)

Six months ended Sep. 30, 2022: 16 (–%)

	Basic earnings per share	Diluted earnings per share
	Yen	Yen
Six months ended Sep. 30, 2023	(109.70)	–
Six months ended Sep. 30, 2022	3.11	–

(2) Consolidated financial position

	Total assets	Net assets	Equity ratio
	Million yen	Million yen	%
As of Sep. 30, 2023	2,630	888	33.5
As of Mar. 31, 2023	2,559	1,527	59.4

Reference: Shareholders' equity (million yen) As of Sep. 30, 2023: 880 As of Mar. 31, 2023: 1,519

2. Dividends

	Dividend per share				
	1Q-end	2Q-end	3Q-end	Year-end	Total
	Yen	Yen	Yen	Yen	Yen
Fiscal year ended Mar. 31, 2023	–	0.00	–	8.00	8.00
Fiscal year ending Mar. 31, 2024	–	0.00			
Fiscal year ending Mar. 31, 2024 (forecast)			–	4.00	4.00

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

3. Consolidated Earnings Forecasts for the Fiscal Year Ending March 31, 2024 (April 1, 2023 – March 31, 2024)

(Percentages represent year-on-year changes)

	Net sales		Operating profit		Ordinary profit		Profit attributable to owners of parent		Basic earnings per share
	Million yen	%	Million yen	%	Million yen	%	Million yen	%	Yen
Full year	2,624	(8.5)	(180)	–	(181)	–	(441)	–	(81.36)

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

*** Notes**

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

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

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

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

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

3) Changes in accounting-based estimates: None

4) Restatements: None

(4) Number of issued shares (common stock)

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

As of Sep. 30, 2023:	5,428,000 shares	As of Mar. 31, 2023:	5,428,000 shares
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2) Number of treasury shares at the end of period

As of Sep. 30, 2023:	506 shares	As of Mar. 31, 2023:	506 shares
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3) Average number of shares outstanding during the period

Six months ended Sep. 30, 2023:	5,427,494 shares	Six months ended Sep. 30, 2022:	5,427,494 shares
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* This quarterly financial report is not subject to quarterly review by certified public accountants or auditing firms.

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

Forecasts of future performance in this report are based on assumptions judged to be valid and information available to the MKSystem's management at the time the materials were prepared but are not promises by MKSystem regarding future performance. Actual results may differ significantly from these forecasts for a number of reasons. Please refer to "1. Qualitative Information on Quarterly Consolidated Financial Performance, (3) Explanation of Consolidated Earnings Forecasts and Other Forward-looking Statements" on page 4 for forecast assumptions and notes of caution for usage.

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1. Qualitative Information on Quarterly Consolidated Financial Performance

(1) Explanation of Results of Operations

During the first half of the fiscal year ending March 31, 2024 (hereinafter “the period under review”), the Japanese economy was expected to improve the business sentiment, after business activities and private consumption behavior gradually returned to normal by easing of movement restrictions due to COVID-19. However, considering the increased downside risk caused by the global monetary tightening, the prolonged Russia and Ukraine situation, and the continuing price hikes due to yen depreciation, the Japanese economy still remained unpredictable.

In the domestic information service industry and the field of personnel and labor management, in which MKSystem Corporation and its group companies (hereinafter collectively “the Group”) are involved, the government has promoted the work-style reform, the rapid transition to teleworking as a measure against the COVID-19 infections, or furtherance of digital transformation (DX) to improve business efficiency. Against these backdrops, corporate demand for investment remained increasing, though companies took a cautious attitude toward investment as demonstrated by the postponement of some new investments because of concern about impacts of the above on the domestic and foreign economies.

Under these circumstances, as announced in “Notice of Ransomware Infection Damages by a Third Party” (available in Japanese only) on June 6, 2023, servers of the data center that provides our services were compromised by a third party using a ransomware, and we had to continue to suspend some of our services for recovery. As a result, we cancelled billing to the affected users for the subscription in June and part of July.

In recovering the system, we removed the infected servers in the data center, as we decided to migrate our services to a cloud computing platform. In addition, unexpected expenses were incurred for investigation by an external specialized agency, reconstruction of system infrastructure, and security enhancement. Accordingly, we recognized 125 million yen of loss on retirement of non-current assets and 125 million yen of system failure response expenses both as extraordinary losses.

As a result, for the period under review, the Group reported net sales of 1,117 million yen (down 16.3% year on year), gross profit of 233 million yen (down 63.3%), operating loss of 342 million yen (compared with operating profit of 40 million yen for the same period of the previous fiscal year), ordinary loss of 345 million yen (compared with ordinary profit of 44 million yen for the same period of the previous fiscal year), and loss attributable to owners of parent of 595 million yen (compared with profit attributable to owners of parent of 16 million yen for the same period of the previous fiscal year). In addition, the return on equity (ROE), one of the KPIs for the Group, came in at minus 49.6% (compared with positive 1.2% for the same period of the previous fiscal year) on a consolidated basis, and minus 40.5% (compared with positive 3.7% for the same period of the previous fiscal year) on a non-consolidated basis.

Results by business segment were as follows.

The Shalom Business

We provide software to support business of labor and social security attorney offices, labor insurance administration associations, and general corporations by facilitating their operations and processes for the social security insurance, labor insurance, and payroll calculation. Our products mainly consist of the following cloud services: Shalom series as our flagship product, MYNABOX series as a My Number management system, and eNEN as a web-based year-end adjustment filing system.

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

In this segment, as mentioned earlier, we were unable to provide proper services to most of roughly 3,400 users due to the unauthorized access to the servers in our data center by a third party using a ransomware. As a result of the incident, net sales decreased due to cancellation of billing to the affected users for the subscription in June and part of July.

Net sales of the segment consist of those from the cloud services of 797 million yen (down 24.7% year on year), of which the ASP services under the subscription model amounted to 763 million yen (down 22.5%) and the system construction services amounted to 33 million yen (down 54.5%); and those from the system products of 40 million yen (down 9.1%).

Gross profit and operating profit significantly decreased year on year due to an increase in cost of sales by higher-than-expected operating cost for the cloud services built as our new system platform, in addition to a decrease in net sales for the above mentioned reason.

As a result, the segment recorded net sales of 845 million yen (down 24.1% year on year), gross profit of 163 million yen (down 72.0%), and operating loss of 318 million yen (compared with operating profit of 73 million yen for the same period of the previous fiscal year). The ratio of operating profit to net sales, one of the KPIs for the Group, came in at minus 37.7% (compared with positive 6.6% for the same period of the previous fiscal year).

The CuBe Business

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

In the contracted development of front-end systems, sales of maintenance business ordered by large companies and local governments have steadily increased. Meanwhile, the number of new development projects that respond to demand for investment in updating systems has piled up at the pace faster than that for the past years. In the cloud service business GooooN, we focused on functional enhancement and cultivation of sales channels.

While we are continuing to work on reducing costs, the segment recorded operating loss due to incurrence of upfront costs consisting mainly of outsourcing expenses and promotion expenses.

As a result, the segment recorded net sales of 281 million yen (up 24.1% year on year), gross profit of 70 million yen (up 35.2%), and operating loss of 33 million yen (compared with operating loss of 41 million yen for the same period of the previous fiscal year). Operating loss of the CuBe Business reflects amortization of goodwill of 19 million yen.

(2) Explanation of Financial Position

Cash Flows

The balance of cash and cash equivalents (hereinafter “net cash”) at the end of the period under review increased 117 million yen from the end of the previous fiscal year to 726 million yen. The details of cash flows during the period under review from each activity and the major components of changes are as follows.

Cash flows from operating activities

Net cash used in operating activities was 407 million yen (compared with net cash provided of 245 million yen for the same period of the previous fiscal year). Major positive factors include depreciation of 177 million yen and a 59 million yen increase of accounts payable - other. Major negative factors include loss before income tax of 596 million yen and a 40 million yen decrease of trade payables.

Cash flows from investing activities

Net cash used in investing activities was 146 million yen (compared with cash used of 284 million yen for the same period of the previous fiscal year). Major negative factors include purchase of intangible assets of 119 million yen and purchase of property, plant and equipment of 34 million yen.

Cash flows from financing activities

Net cash provided by financing activities was 671 million yen (compared with cash provided of 176 million yen for the same period of the previous fiscal year). Major positive factors include proceeds from long-term borrowings

of 700 million yen and a net increase in short-term borrowings of 100 million yen. Major negative factors include repayments of long-term borrowings of 85 million yen and dividends paid of 43 million yen.

Financial Resources and Liquidity of Funds

The Group's cash needs, in principle, are met by funds provided by cash flows from operating activities, which are used for capital investment, repayment of borrowings, and other such purposes. The Group's policy is to secure liquidity through its own funds, but the Group plans to borrow from financial institutions to finance working capital and large-scale capital investment where necessary.

Assets, Liabilities and Net Assets

Assets

The balance of current assets at the end of the period under review was 1,381 million yen (up 12.1% from the end of the previous fiscal year), consisting primarily of 726 million yen in cash and deposits and 487 million yen in accounts receivable - trade.

The balance of non-current assets was 1,249 million yen (down 5.9% from the end of the previous fiscal year), consisting primarily of 480 million yen in software, 157 million yen in guarantee deposits, and 116 million yen in goodwill.

As a result, the balance of total assets was 2,630 million yen (up 2.8% from the end of the previous fiscal year).

Liabilities

The balance of current liabilities at the end of the period under review was 989 million yen (up 19.0% from the end of the previous fiscal year), consisting primarily of 300 million yen in short-term borrowings, 282 million yen in accounts payable-other, and 182 million yen in current portion of long-term borrowings.

The balance of non-current liabilities was 752 million yen (up 274.6% from the end of the previous fiscal year), consisting primarily of 742 million yen in long-term borrowings.

As a result, the balance of total liabilities was 1,742 million yen (up 68.8% from the end of the previous fiscal year).

Net assets

The balance of shareholders' equity at the end of the period under review was 880 million yen (down 42.0% from the end of the previous fiscal year), consisting primarily of 219 million yen in share capital, 202 million yen in capital surplus, and 460 million yen in retained earnings.

As a result, the balance of net assets was 888 million yen (down 41.8% from the end of the previous fiscal year).

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

The consolidated financial result of the period under review fell short of the plan, mainly due to the above mentioned higher-than-expected operating costs for the cloud services built as a new system platform. However, the Group plans to revise (increase) some of the product prices in and after the third quarter of the fiscal year ending March 31, 2024; and expects improvement of operating costs for the cloud services. Therefore, the Group has decided to maintain the consolidated earnings forecast for the fiscal year ending March 31, 2024, as announced in Summary of Consolidated Financial Results for the First Quarter of the Fiscal Year Ending March 31, 2024 (Japanese GAAP) on August 8, 2023.

If the future development of business performance causes us to decide to revise the consolidated earnings forecasts for the full year of the fiscal year ending March 31, 2024, we will disclose them promptly.

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

	(Thousands of yen)	
	FY3/23 (As of Mar. 31, 2023)	Second quarter of FY3/24 (As of Sep. 30, 2023)
Assets		
Current assets		
Cash and deposits	609,336	726,608
Accounts receivable-trade	507,988	487,924
Merchandise	29,154	25,080
Work in process	29,966	29,003
Supplies	440	415
Prepaid expenses	47,293	43,080
Other	8,350	69,481
Total current assets	1,232,530	1,381,594
Non-current assets		
Property, plant and equipment		
Buildings, net	112,613	106,851
Vehicles, net	0	0
Tools, furniture and fixtures, net	144,907	32,618
Total property, plant and equipment	257,520	139,469
Intangible assets		
Software	485,234	480,817
Software in progress	249,092	317,265
Trademark right	855	740
Telephone subscription right	1,218	1,218
Goodwill	136,016	116,467
Total intangible assets	872,417	916,509
Investments and other assets		
Investments in capital	60	60
Guarantee deposits	163,022	157,298
Deferred tax assets	33,216	34,874
Other	1,176	1,176
Total investments and other assets	197,475	193,409
Total non-current assets	1,327,414	1,249,388
Total assets	2,559,945	2,630,983

(Thousands of yen)

	FY3/23 (As of Mar. 31, 2023)	Second quarter of FY3/24 (As of Sep. 30, 2023)
Liabilities		
Current liabilities		
Accounts payable-trade	78,633	38,002
Short-term borrowings	200,000	300,000
Current portion of long-term borrowings	115,592	182,214
Accounts payable-other	125,321	282,339
Accrued expenses	17,838	29,947
Income taxes payable	77,519	2,267
Accrued consumption taxes	25,688	4,690
Advances received	111,909	53,358
Provision for system failure response expenses	-	2,420
Provision for bonuses	71,228	83,951
Other	8,001	10,722
Total current liabilities	831,733	989,915
Non-current liabilities		
Long-term borrowings	195,000	742,786
Retirement benefit liability	6,010	10,192
Total non-current liabilities	201,010	752,978
Total liabilities	1,032,743	1,742,893
Net assets		
Shareholders' equity		
Share capital	219,110	219,110
Capital surplus	202,122	202,122
Retained earnings	1,098,920	460,087
Treasury shares	(499)	(499)
Total shareholders' equity	1,519,653	880,820
Non-controlling interests	7,548	7,269
Total net assets	1,527,201	888,089
Total liabilities and net assets	2,559,945	2,630,983

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

	(Thousands of yen)	
	First six months of FY3/23 (Apr. 1, 2022 – Sep. 30, 2022)	First six months of FY3/24 (Apr. 1, 2023 – Sep. 30, 2023)
Net sales	1,335,613	1,117,759
Cost of sales	701,275	884,675
Gross profit	634,337	233,083
Selling, general and administrative expenses	594,274	575,119
Operating profit (loss)	40,063	(342,035)
Non-operating income		
Interest income	2	2
Dividend income	1	1
Rental income	21,402	20,272
Outsourcing service income	3,000	3,000
Other	74	22
Total non-operating income	24,479	23,297
Non-operating expenses		
Interest expenses	1,300	2,043
Rental costs	19,014	18,269
Commission expenses	–	6,000
Total non-operating expenses	20,314	26,312
Ordinary profit (loss)	44,228	(345,050)
Extraordinary losses		
Loss on retirement of non-current assets	–	125,934
System failure response expenses	–	125,275
Total extraordinary losses	–	251,209
Profit (loss) before income taxes	44,228	(596,260)
Income taxes-current	28,811	1,194
Income taxes-deferred	(904)	(1,657)
Total income taxes	27,906	(463)
Profit (loss)	16,321	(595,796)
Loss attributable to non-controlling interests	(556)	(383)
Profit (loss) attributable to owners of parent	16,877	(595,413)

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

	(Thousands of yen)	
	First six months of FY3/23 (Apr. 1, 2022 – Sep. 30, 2022)	First six months of FY3/24 (Apr. 1, 2023 – Sep. 30, 2023)
Profit (loss)	16,321	(595,796)
Comprehensive income	16,321	(595,796)
Comprehensive income attributable to		
Comprehensive income attributable to owners of parent	16,877	(595,413)
Comprehensive income attributable to non-controlling interests	(556)	(383)

(3) Quarterly Consolidated Statement of Cash Flows

(Thousands of yen)

	First six months of FY3/23 (Apr. 1, 2022 – Sep. 30, 2022)	First six months of FY3/24 (Apr. 1, 2023 – Sep. 30, 2023)
Cash flows from operating activities		
Profit (loss) before income taxes	44,228	(596,260)
Depreciation	165,269	177,620
Amortization of goodwill	19,430	19,654
Increase (decrease) in provision for retirement benefits for directors (and other officers)	(5,000)	–
Increase (decrease) in retirement benefit liability	3,042	4,182
Increase (decrease) in provision for bonuses	3,720	12,723
Interest and dividend income	(3)	(3)
Interest expenses	1,300	2,043
Loss on retirement of non-current assets	–	125,934
Decrease (increase) in trade receivables	36,503	20,064
Decrease (increase) in inventories	(20,708)	5,062
Increase (decrease) in trade payables	(14,249)	(40,630)
Increase (decrease) in accrued consumption taxes	(2,194)	(19,266)
Increase (decrease) in accounts payable-other	2,206	59,779
Other, net	11,242	(107,309)
Subtotal	244,789	(336,404)
Interest and dividends received	3	3
Interest paid	(1,300)	(2,043)
Income taxes refund (paid)	1,801	(69,265)
Net cash provided by (used in) operating activities	245,293	(407,710)
Cash flows from investing activities		
Purchase of property, plant and equipment	(65,193)	(34,015)
Purchase of intangible assets	(219,372)	(119,243)
Proceeds from refund of leasehold and guarantee deposits	145	7,076
Net cash provided by (used in) investing activities	(284,420)	(146,183)
Cash flows from financing activities		
Net increase (decrease) in short-term borrowings	46,000	100,000
Proceeds from long-term borrowings	300,000	700,000
Repayments of long-term borrowings	(126,126)	(85,592)
Dividends paid	(43,223)	(43,241)
Net cash provided by (used in) financing activities	176,650	671,166
Net increase (decrease) in cash and cash equivalents	137,523	117,272
Cash and cash equivalents at beginning of period	461,052	609,336
Cash and cash equivalents at end of period	598,575	726,608

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

Not applicable.

Significant Changes in Shareholders' Equity

Not applicable.

Segment Information

First six months of FY3/23 (Apr. 1, 2022 – Sep. 30, 2022)

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

(Thousands of yen)

	Shalom Business	CuBe Business	Total	Adjustment (Note)	Amounts recorded in quarterly consolidated statement of income
Net sales					
External sales	1,110,856	224,756	1,335,613	–	1,335,613
Inter-segment sales and transfers	3,303	2,003	5,306	(5,306)	–
Total	1,114,159	226,760	1,340,919	(5,306)	1,335,613
Segment profit (loss)	73,911	(41,873)	32,038	8,024	40,063

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

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

First six months of FY3/24 (Apr. 1, 2023 – Sep. 30, 2023)

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

(Thousands of yen)

	Shalom Business	CuBe Business	Total	Adjustment (Note)	Amounts recorded in quarterly consolidated statement of income
Net sales					
External sales	843,424	274,335	1,117,759	–	1,117,759
Inter-segment sales and transfers	1,752	7,062	8,814	(8,814)	–
Total	845,176	281,397	1,126,573	(8,814)	1,117,759
Segment loss	(318,600)	(33,384)	(351,985)	9,949	(342,035)

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

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

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