

Fibergate (9450)

Strong residential WiFi

25th Nov 2022

Share price: ¥1,001

Market cap: ¥20.6bn

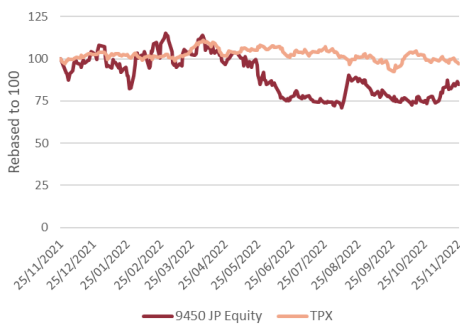
1Q earnings confirmed residential WiFi demand remains strong as Fibergate starts to target growth in new builds & long-stay areas.

Company sector

Diversified Telecommunication

Stock data

Price (¥)	1,001
Mkt cap (¥bn)/(\$m)	20.6 / 147.8
52-week range (¥)	831-1,377
Shares O/S (m)	20.6
Average daily value (\$m)	0.7
Free float (%)	42.9
Foreign shareholding (%)	2.0
Ticker	9450
Exchange	Tokyo Prime
Net Debt/Equity (x)	132.6



Source: Bloomberg

- **Above plan 1Q sales & OP reflected robust existing building WiFi installation demand driving stronger than expected high margin Home-Use sales & was achieved despite charges related to a cyberattack at the end of Sept.**
- **Growth also reflected a market share increase to 10.7% versus 10.2% in FY 6/22 & 6.7% in FY 6/18 as Fibergate starts to challenge competitors such as Tsunagu.net, CYBERHOME & D.U-Net.**
- **Underlying demand in the residential WiFi stock business remains firm, with strong order growth for both existing & new build use. Whilst new build Home-Use sales were only 30% of total 1Q Home-Use sales, we expect the percentage to increase given 1Q orders were split 50:50 between existing & new buildings.**
- **A cyberattack in late Sept that impacted WiFi services in numerous locations resulted in personnel, equipment & outsourcing costs to resolve issues & refund those customers whose service was interrupted. We note Fibergate expects the Y40m cost incurred in the 1Q to be returned through its cyberattack insurance.**
- **1Q Business-Use sales were disappointing, with only 20% of flow business derived from Fibergate's targeted long stay areas & the number of new installations achieving just 10% of the FY target. Whilst we expect a 2H acceleration, initial forecasts may prove challenging.**
- **In aggregate, 1Q results represent a strong start to FY 6/23, underlining continued residential WiFi growth & long-term Business-Use potential. On 16x FY 6/23 company estimates, we encourage investors to book a 1-on-1 with senior MD Takafumi Hamazu on Tues 6th or Thurs 8th Dec: [here](#).**

BUSINESS OVERVIEW

Fibergate is the #2 ranked supplier of domestic wireless telecom services, including free Wi-Fi spot construction, maintenance & operation. It also produces & sells communication equipment.

Next event

1-on-1 meetings, Tues 6th & Thurs 8th Dec

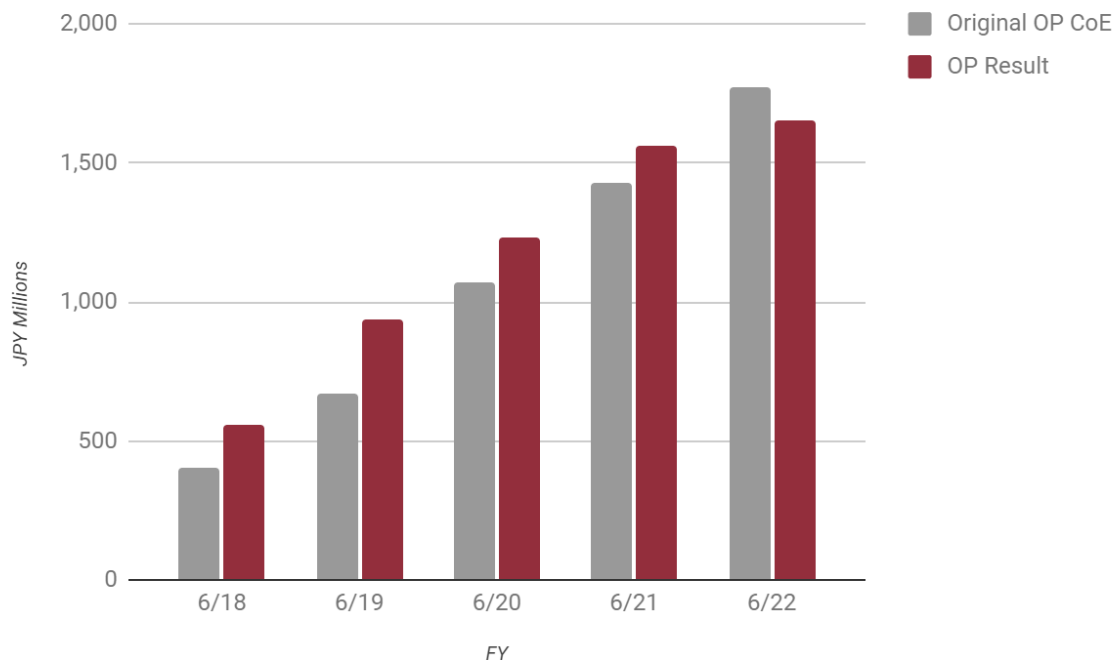
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Fibergate is a research client of Storm Research

Year end	6/2021	6/2022	1Q 6/2022	6/2023E
Sales (¥bn)	8.5	10.6	2.6	12.9
OP (¥bn)	1.6	1.7	0.5	2.0
NP (¥bn)	1.0	1.1	0.3	1.3
EPS (¥)	50.1	52.6	16.5	63.7
DPS (¥)	4.0	4.5	n/a	7.0
Sales growth YoY (%)	+14.4	+25.1	+14.8	+21.4
OP growth YoY (%)	+26.3	+6.0	+66.7	+22.3
NP growth YoY (%)	+41.1	+ 5.3	+85.2	+21.2
EPS growth YoY (%)	+38.4	+5.0	+85.1	+21.1
PER (x)	30.7	18.1	n/a	15.7
EV/EBITDA (x)	13.2	8.3	n/a	8.7
PBR (x)	8.5	5.9	6.2	6.2
ROE (%)	31.9	30.9	30.8	n/a
ROIC (%)	15.0	12.6	12.1	n/a
FCF yield (%)	n/a	0.5	n/a	n/a
Dividend yield (%)	0.4	0.5	n/a	0.7

RESULTS VS FORECAST HISTORY



EARNINGS

1Q sales & OP were above the CoE driven by **above plan new contracts for existing buildings** versus a conservative forecast in the Home-Use division. Earnings were strong despite charges for a cyberattack-related communication failure that occurred between 20th - 28th Sept & caused WiFi outages across many of its properties (number of properties not disclosed).

The total cyberattack 1Q impact to sales & OP is estimated at approx. Y40m, mainly but not exclusively in the Home-Use division. Excluding cyberattack charges, 1Q OP would have been comfortably over Y500m & **highlights the ongoing growth potential in the high margin Home-Use division.**

- *Cyberattack:* The cyberattack caused huge internet traffic flow & resulted in WiFi services going down at many of its customers, although there was no data leakage. The attack resulted in Fibergate having to replace equipment, with personnel (including salespeople) required to work overtime & some outsourcing required.

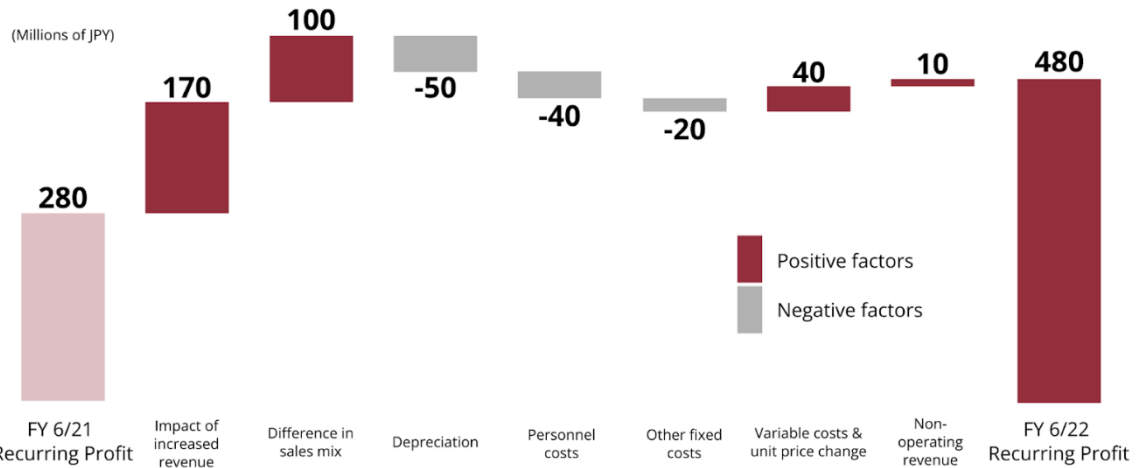
The total 1Q cost related to the restoration of WiFi & reimbursement to customers for lack of service was approx. Y40m. Fibergate has insurance to cover such failures but there is a time lag between claiming & reimbursement & the company **expects full reimbursement of related expenses in the 2H.**

Whilst the cyberattack did not result in any customer cancellations, it meant salespeople were unable to do their job for the duration of the attack as all employees were involved in solving issues & communicating with clients.

Fibergate **continues to invest in the ability to handle heavy data loads** & to review & strengthen recovery processes in the event of future issues. The majority of cyberattack related costs were accounted for in the 1Q, but reparation works continued into Oct & we anticipate a further approx. Y10m charge impacting 2Q earnings.

- OPM: The 1Q OPM improved +5.7ppt YoY to 18.5%. Home-Use profitability increased YoY, albeit versus easy hurdles as 1Q FY 6/22 new contract profitability was poor as sales included low margin equipment. In contrast, new contract profitability improved from 2Q FY 6/22 onwards.

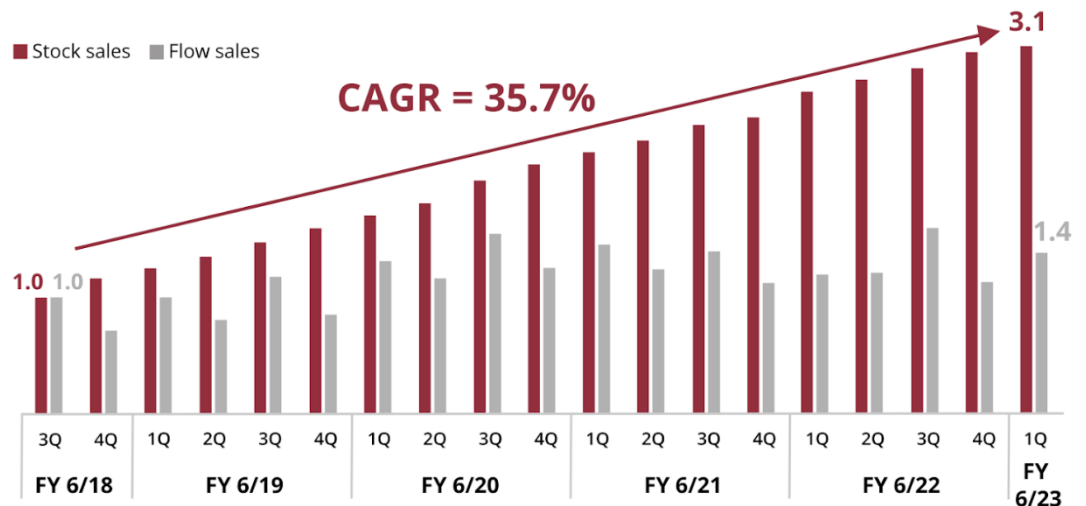
- FY 6/21 RP versus FY 6/22 RP:



Source: Company

Personnel & depreciation cost increases were largely offset by the reduction in the variable cost unit price as a result of efficient use of internet lines.

- Stock versus & flow business growth:



Note: Adjusted for FY 6/18=1. The apparent height of bars may differ even if the figures appear the same due to rounding differences. This revenue breakdown is a continuous comparative figure based on the company's definition and is strictly different from period-proportioned sales under revenue recognition standards.

Source: Company

1Q Stock business growth remained strong & has grown consistently since listing. The pace of growth has slowed a little since 3Q FY 6/18, as the company shifts towards new builds in its Home-Use division, but **it remains above +35% per year.**

HOME-USE
BUSINESS

(JPY Millions)	6/22 Results	YoY	1Q 6/23 Results	YoY	6/23 CoE	YoY
Sales	8,141	15.2%	2,256	16.9%	9,320	14.5%
OP	2,318	23.9%	671	48.8%	2,530	9.1%
OPM	28.5%	2.0%	29.7%	6.4%	27.1%	-1.3%

1Q Home-Use sales & OP were significantly above plan, driven by existing building WiFi installation demand. As of 1Q FY 6/23, Fibergate had a total of 474,200 units +5%QoQ, +21.6%YoY in service, with a **10.7% domestic market share versus 10.2% in FY 6/22 & 6.7% in FY 6/18**.

The 1Q OPM improved +6.4ppt YoY to 29.7%, partly due to sales growth but mainly due to the weak 1Q FY 6/22 OPM on account of low margin equipment sales.

- *New build vs existing buildings:* As of the 1Q, **30% of sales were for new builds versus 70% for existing** & we expect new build exposure to increase from the 2H. The order to sales lead time for new builds of 6-12 months is longer than for existing buildings of a few weeks & we note the breakdown of 1Q orders was 50% new build vs 50% existing.

- *IoT:* IoT remains a small percentage of total divisional sales but is forecast to increase over the medium term. FY 6/22 IoT sales growth was slower than expected & Fibergate's IoT related FY 6/23 sales estimate has therefore been pitched conservatively & is expected to remain a small percentage of the total.

Whilst solar panels are forecast to boost sales in the medium term, & Fibergate is working on new solar panel development, zero earnings contribution has been included in FY 6/23.

- *FY 6/23 outlook:* Fibergate anticipates existing business installation growth to beat its conservative forecasts with an acceleration in the 2H as the contribution from new build sales increases. FY 6/23 sales & OP are therefore likely to be above plan.

BUSINESS-USE
BUSINESS

(JPY Millions)	6/22 Results	YoY	1Q 6/23 Results	YoY	6/23 CoE	YoY
Sales	1,244	-8.1%	329	28.0%	1,830	47.1%
OP	235	-46.7%	46	-13.2%	570	142.6%
OPM	18.9%	-13.7%	14.0%	-6.6%	31.1%	12.3%

1Q sales increased +28%YoY but were a little disappointing versus the company's expectations due to **slower than expected growth at targeted long stay customers**. 1Q flow & stock sales were approx. 50/50 with an increase in flow business YoY (amount not disclosed), but only approx. 20% of the flow business was from the strategically targeted long-term areas.

Weak 1Q OP mainly related to additional unforeseen costs from a loss-making hotel related project completed in the 1Q. Increased personnel costs, higher parts costs (for example, semiconductors) & the weaker Yen also pushed up costs. As sales grow, both OP & the OPM are set to increase YoY.

Fibergate has 3 strategic target areas of long stay usage for Business-Use growth: care homes & hospitals, resort hotels & government facilities. The number of new installations in the 1Q for these 3 areas was lower than expected at +30 versus the FY 6/23 target of +357. Fibergate

assumes installations accelerate in the 2H but, having achieved less than 10% of the FY target FYTD, the target risks proving optimistic.

Whilst it has had some success in acquiring nursing facilities & resort hotels as customers, hospitals have proved more challenging due to their complicated networks. It is tying up with more sales channels to grow its presence in hospitals, for example medical equipment dealers, but the order lead time is longer versus at other facilities. Fibergate has not assumed any significant growth from government facilities.

Due to the relaxation of movement restrictions post-COVID, **demand for outdoor use WiFi, such as buses, taxis & events, has been stronger than expected** & Fibergate recently announced a business tie-up with taxi company Nihon Kohtsu. It is also benefiting from the gradual recovery in tourism & is focusing on strengthening sales of WiFi services for tourist facilities. To a certain extent, these areas can offset slower than expected growth in targeted long stay areas.

- *FY 6/23 outlook*: Demand for outdoor use WiFi is expected to continue expanding in FY 6/23 as consumer activity returns to pre-COVID levels, but growth in Fibergate's 3 target long stay areas may prove challenging versus the CoE, likely leaving Business-Use division sales & OP a little below plan.

REAL ESTATE BUSINESS

(JPY Millions)	6/22 Results	YoY	1Q 6/23 Results	YoY	6/23 CoE	YoY
Sales	1,238	1668.6%	5	-92.9%	1,740	40.5%
OP	59	883.3%	-6	n/a	100	69.5%
OPM	4.8%	-3.8%	n/a	n/a	5.7%	1.0%

1Q sales were minimal, in line with the CoE, as although there was rental income from Reunir Gracias Kawaguchi (a new-generation SDG ecological condominium owned by subsidiary FG Smart Asset), there were no real estate sales. Real estate sales of 2 owned properties are expected in FY 6/23 with the smaller in the 2Q or 3Q & the larger in the 4Q.

Fibergate contends its FY 6/23 estimates are conservative.

- 11th Nov 2022: Initiating coverage: 'Residential & business WiFi'

PREVIOUS REPORTS

COMPANY INFORMATION

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Major shareholders	Stake %
Masanori Inomata	25.85
MI Corp KK	23.06
Bank of New York Mellon	10.84
GPIF	5.49
Taizou Matsumoto	5.30
Norges Bank	1.21
Nomura Hdgs	1.05
Fibergate	0.93
Vanguard	0.91
Sumitomo Mitsui Trust Hdgs	0.77

Source: Bloomberg

J GAAP Financial statements

Income statement (¥bn)	FY 6/20	FY 6/21	FY 6/22
Sales	7.42	8.49	10.62
COGS	3.6	4.1	5.8
Gross profit	3.9	4.4	4.8
Gross profit margin (%)	52.1	51.2	45.5
Operating expense	2.6	2.8	3.2
Total OP	1.23	1.56	1.65
OP margin (%)	16.6	18.4	15.5
Non-Op Income (Loss)	0.1	0.1	0.1
Pretax Income	1.2	1.5	1.6
Tax	0.5	0.5	0.5
Effective tax rate (%)	38.9	31.0	32.2
Net income	0.72	1.02	1.07

Cash flow statement (¥bn)	FY 6/20	FY 6/21	FY 6/22
Net income/pre-tax profit	0.7	1.0	1.1
Depreciation/amortization	0.8	1.0	1.2
Other non-cash items	0.1	0.3	(0.2)
Changes in working capital	0.1	-0.2	-0.1
Net cash from discontinued operations	0.0	0.0	0.0
Cash from Operating Activities	1.7	1.7	2.3
Change in fixed & intangible assets	-2.1	-2.2	-2.3
Net change in long-term investments	0.0	0.0	0.0
Net cash from acquisitions & divestitures	0.0	0.0	-0.3
Other investing activities	0.0	0.0	0.0
Net cash from discontinued operations	0.0	0.0	0.0
Cash from Investing Activities	-2.1	-2.3	-2.6
Dividends paid	0.0	-0.1	-0.1
Cash from (repayment) debt	0.7	1.4	0.6
Cash from (repurchase) of equity	0.0	0.0	-0.1
Other financing activities	0.0	0.0	-0.1
Net cash from discontinued operations	0.0	0.0	0.0
Cash from Financing Activities	0.7	1.3	0.4
FX impact	0.0	0.0	0.0
Net cash flow	0.4	0.8	0.1
Free cash flow	-0.3	-0.5	0.1
EBITDA	2.0	2.6	2.9

Balance sheet (¥bn)	FY 6/20	FY 6/21	FY 6/22
Cash & equivalents	1.4	2.2	2.3
Accounts & notes receivable	1.1	1.2	1.4
Inventories	0.3	0.4	2.1
Other short-term assets	0.0	0.1	0.1
Current assets	2.8	3.9	6.0
Property, plant & equipment (net of depreciation)	4.0	5.2	6.2
Long term investments & receivables	0.0	0.0	0.1
Other long-term assets	0.2	0.2	0.8
Total non-current assets	4.2	5.5	7.1
Total assets	7.0	9.4	13.1
Payables & accruals	1.0	1.0	0.9
Short-term debt	1.1	1.2	2.6
Other short-term liabilities	0.1	0.2	2.2
Total current liabilities	2.2	2.4	5.6
Long term debt	2.0	3.3	4.1
Other long-term liabilities	0.0	0.1	0.1
Total non-current liabilities	2.0	3.3	4.2
Total liabilities	4.3	5.7	9.8
Share capital & APIC	0.9	0.9	0.9
Treasury stock	0.1	0.1	0.2
Retained earnings	1.9	2.9	2.6
Other equity	0.0	0.0	0.0
Equity before minority interest	2.7	3.7	3.3
Total equity	2.7	3.7	3.3
Total liabilities & equity	7.0	9.4	13.1

Key metrics	FY 6/20	FY 6/21	FY 6/22
Profitability			
Gross margin (%)	52.1	51.2	45.5
Operating margin (%)	16.6	18.4	15.5
Net margin (%)	9.7	12.0	10.1
ROIC (%)	14.4	15.0	12.6
Liquidity			
Current ratio (x)	1.2	1.6	1.1
Quick ratio (x)	1.1	1.4	0.7
Leverage			
Debt/Equity ratio	113.4	121.1	202.9
Net Debt/Equity ratio	61.2	61.4	132.6

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