

Financial Supplementary Materials

for the First Quarter of FY2024

Headwaters Co., Ltd.

May 15, 2024

Securities code: 4011

FY2024 1Q Consolidated Financial Results Overview

(Thousand yen)

(Thousand yen)

	FY2023 1Q Results		FY2024 1Q Results			
		Pct. to net sales (%)		Pct. to net sales (%)	YoY change (%)	Vs. annual plan (%)
Net sales	603,662	100.0	708,367	100.0	117.3	24.2
AI	256,055	42.4	378,293	53.4	147.7	25.3
DX	316,661	52.5	290,700	41.0	91.8	22.0
Product	30,946	5.1	39,374	5.6	127.2	34.6
Operating profit	61,275	10.1	132,306	18.6	215.9	58.5
Ordinary profit	61,841	10.2	131,605	18.5	212.8	57.4
Profit attributable to owners of parent	40,380	6.7	89,896	12.6	222.6	57.3
Net income per share	21.57 yen		47.78 yen			

* The OPS Services category was discontinued from FY2024 and the number of service categories were changed from four to three. In line with this change, FY2023 service category sales were reclassified into the three service categories to enable year-on-year comparisons to be made under the same conditions.

FY2024 Key Performance Indicators

Sales, Operating Profit, Recruiting

Net Sales

- **Sales increased 17.3% YoY for the quarter, setting a new record.**
 - ➔ Generative AI projects boosted sales significantly as clients used up their annual budgets toward the end of the fiscal year. Generative AI projects achieved sales of just over 100 million yen in FY2023 overall, but sales reached approximately 130 million yen in the first quarter of FY2024 alone.
 - ➔ Large-scale projects with annual sales of 100 million yen or more are being conducted in parallel.
 - ➔ Client cultivation, securing multiple medium-sized projects from a single client, is also growing into a foundation for stable earnings.

Operating Profit

- **Operating profit margin reached 18.6%**, setting a new record.
 - ➔ Due to an increase in the number of loyal clients, the **gross profit margin reached a record high of 46.7%**.
 - ➔ Efficiency was successfully improved through measures to improve unit sales price through generative AI projects, sharing know-how gained through active investment in generative AI projects in the fourth quarter of FY2023 within the company, and utilizing it for other projects.
 - ➔ HR recruitment expenses were suppressed through inbound measures.

Recruiting

- There was a **net increase of nine employees**, which was slightly lower than the initial plan (1Q of FY2023: net increase of seven employees).
 - ➔ The recruitment target for FY2024 is a net increase of 60 employees.
 - ➔ The employee turnover rate target is 10% or below (16 employees for the year).

Remarks

- The OPS Services category has been discontinued from FY2024.
 - ➔ This is due to a decrease in the number of contracts for the operation and maintenance phase only, and an increase in time-and-materials contracts mainly for agile development.
 - ➔ Projects that were recorded in the OPS Services category have been allocated to the DX (approx. 80%), AI (approx. 15%), and Products (approx. 5%) service categories.

* In each graph on the following pages, figures relating to OPS projects for each quarter of the last two years have been allocated to the three other service categories.



Net Sales by Service Category

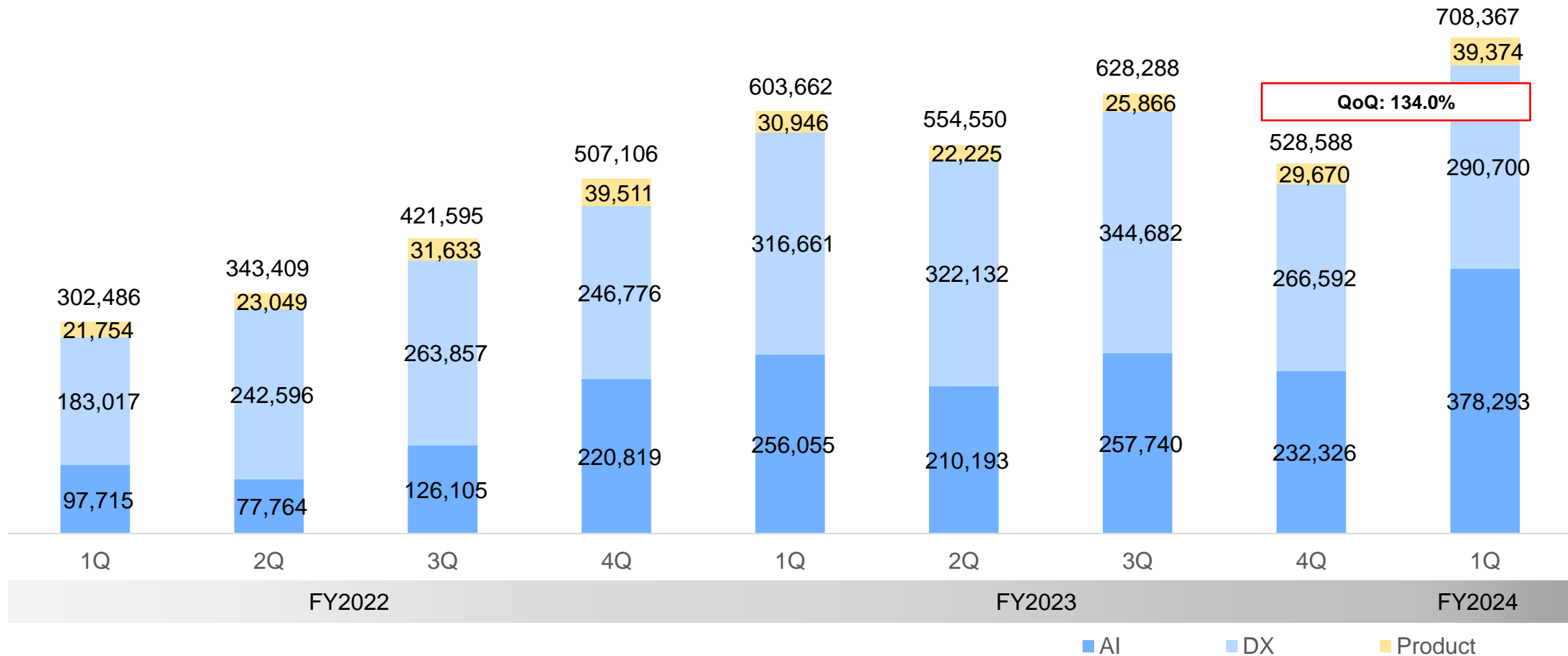
FY2022 Sales: 1,574,596

FY2023 Sales: 2,315,088

(Thousand yen)

YoY for the Quarter: 117.3%

QoQ: 134.0%



* Because the OPS Services category was discontinued from FY2024, FY2022 and FY2023 OPS sales have been allocated to the three other service categories.



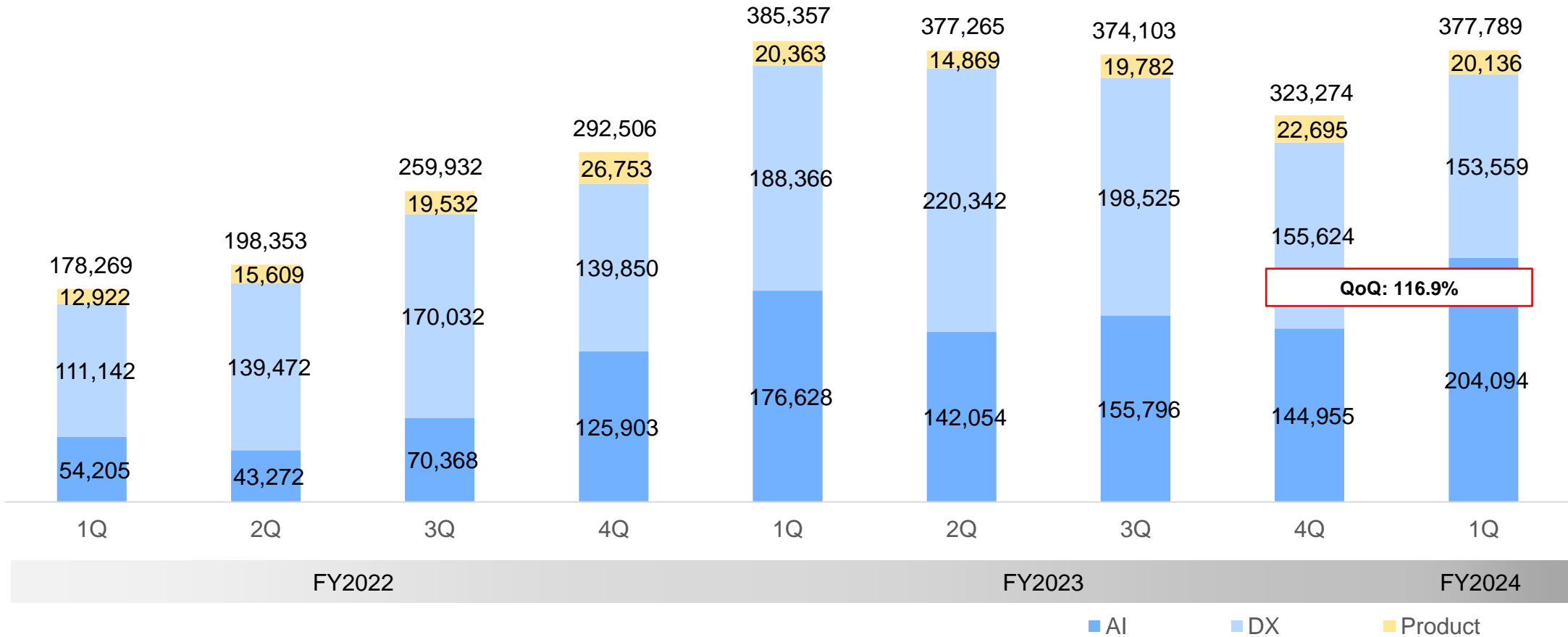
Cost of Sales by Service Category

FY2022 Cost of Sales: 929,060

FY2023 Cost of Sales: 1,459,999

(Thousand yen)

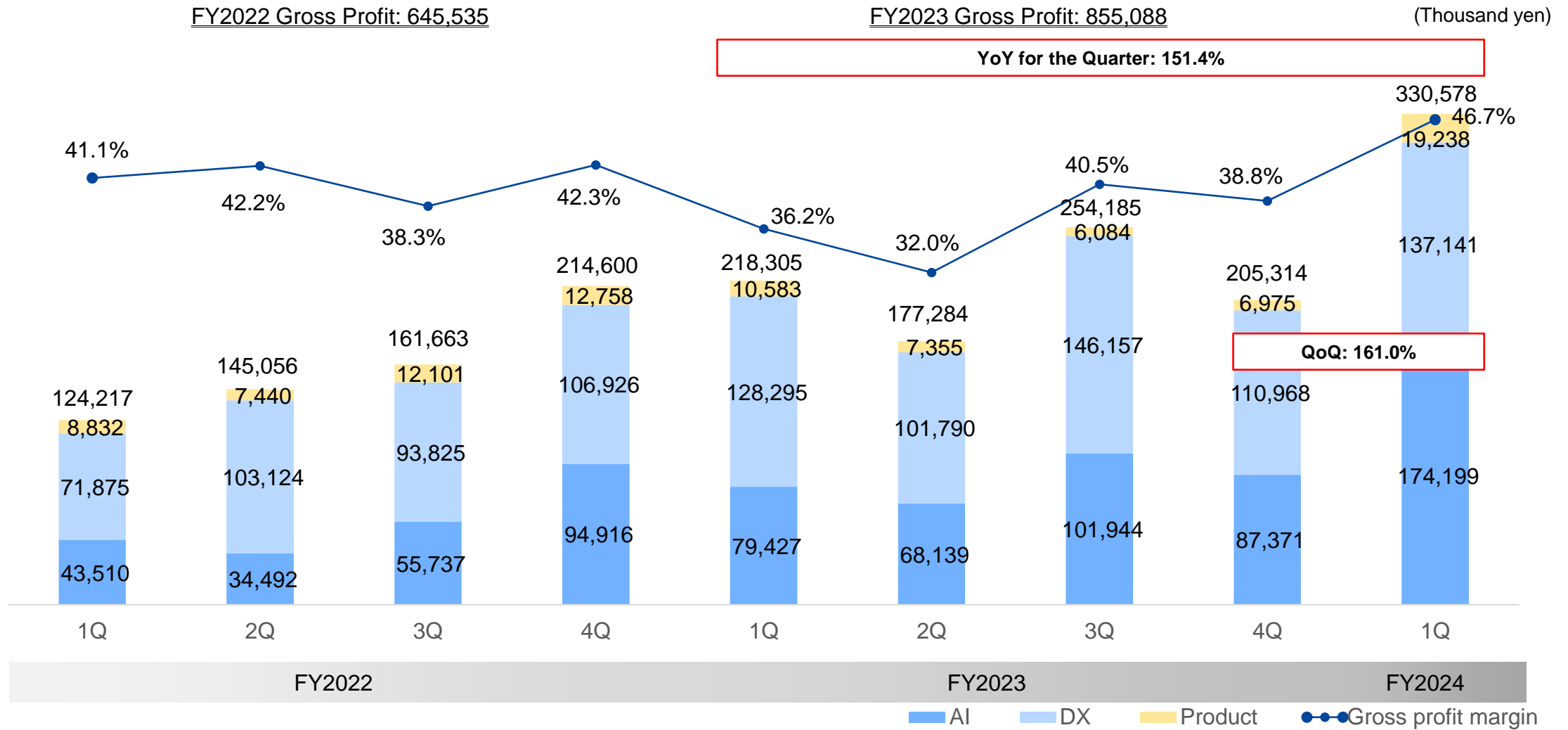
YoY for the Quarter: 98.0%



* Because the OPS Services category was discontinued from FY2024, FY2022 and FY2023 OPS cost of sales have been allocated to the three other service categories.



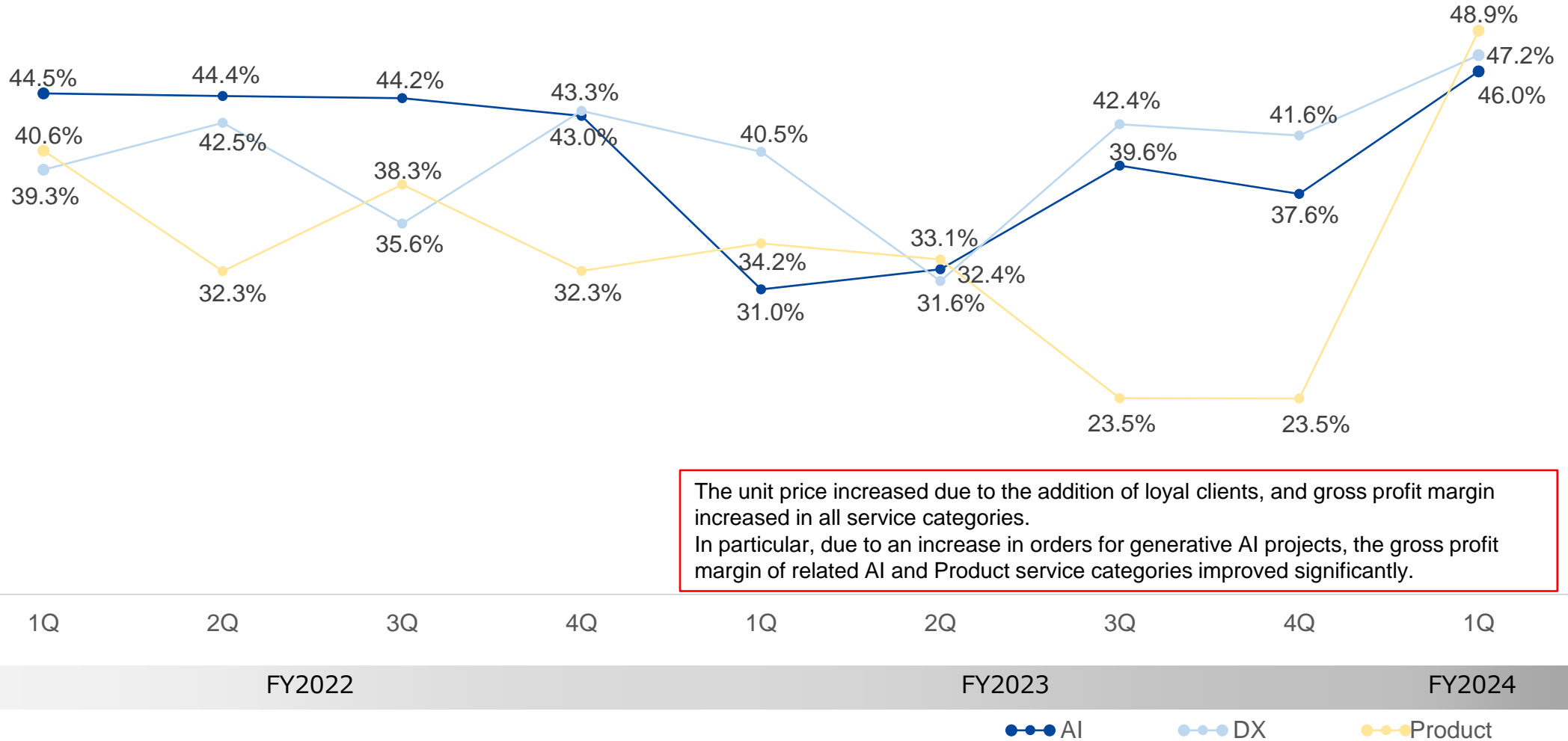
Gross Profit by Service Category



* Because the OPS Services category was discontinued from FY2024, FY2022 and FY2023 gross profit have been allocated to the three other service categories.



Gross Profit Margin by Service Category



The unit price increased due to the addition of loyal clients, and gross profit margin increased in all service categories. In particular, due to an increase in orders for generative AI projects, the gross profit margin of related AI and Product service categories improved significantly.

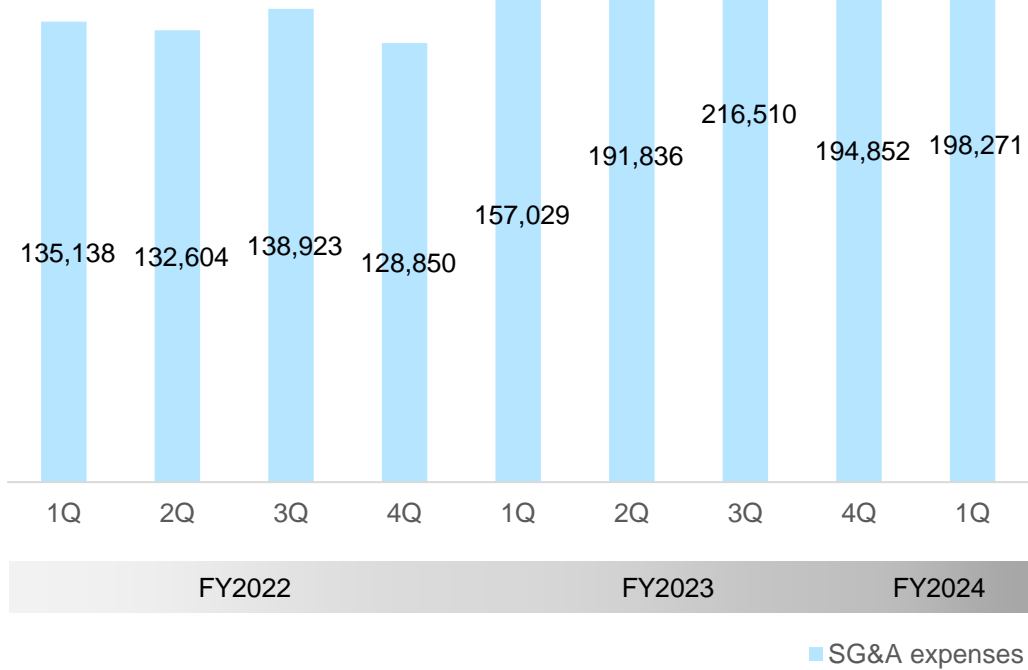
* Because the OPS Services category was discontinued from FY2024, FY2022 and FY2023 gross profit margin have been allocated to the three other service categories.

SG&A Expenses

(Thousand yen)

YoY for the Quarter: 126.3%

QoQ: 101.8%

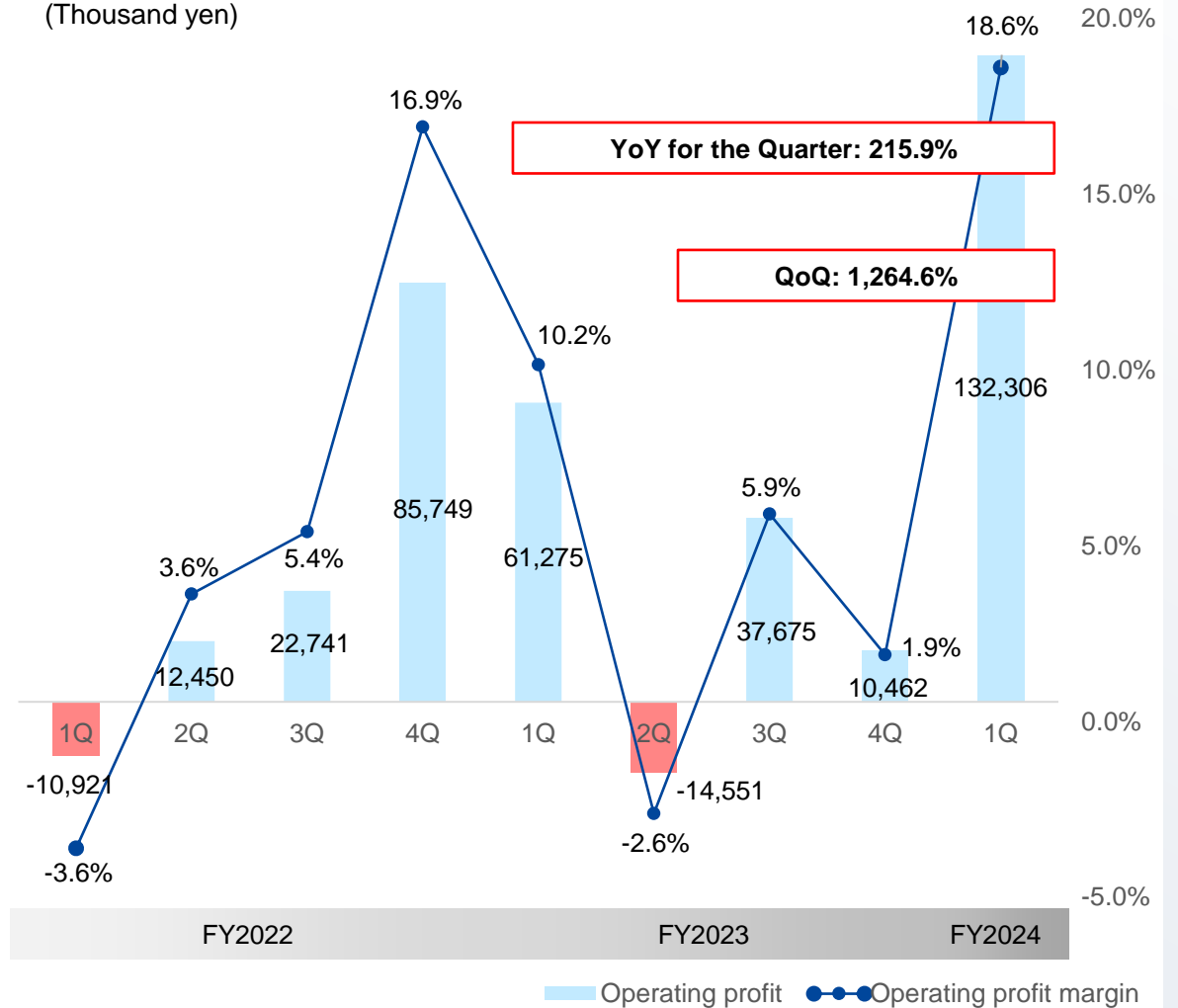


Operating Profit / Operating Profit Margin

(Thousand yen)

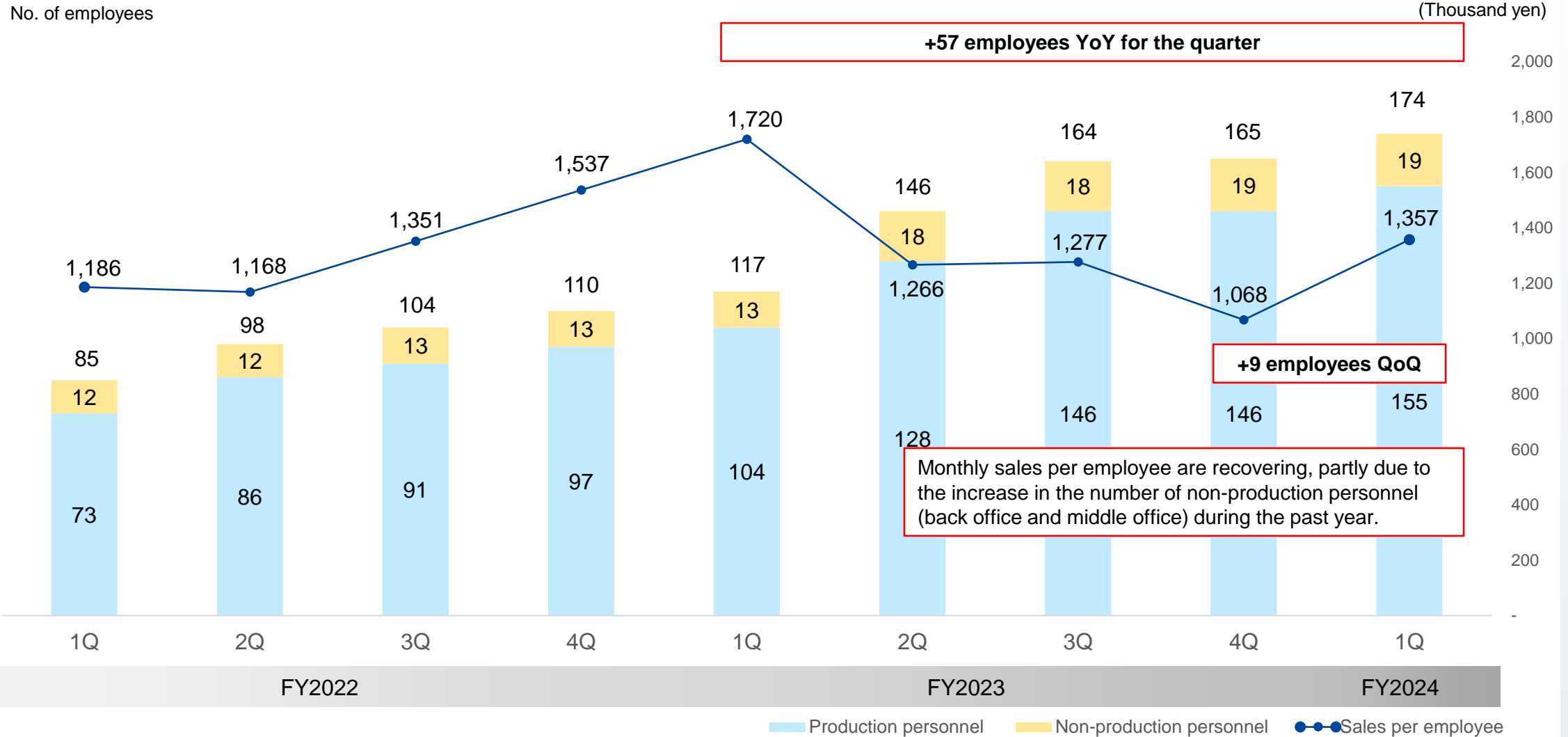
YoY for the Quarter: 215.9%

QoQ: 1,264.6%





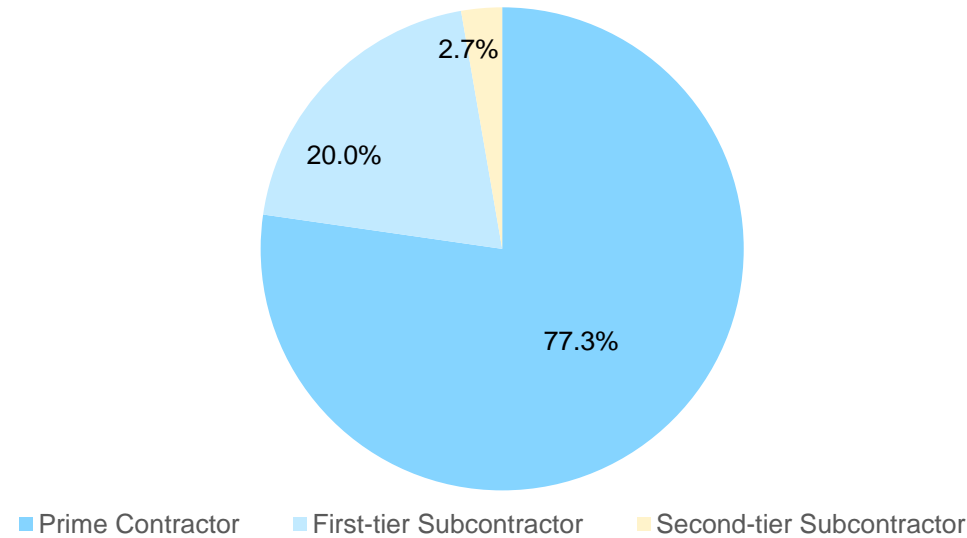
Employees, Monthly Sales Per Employee



* Contract and part-time employees are not included beginning from FY2024 for the consistency with other disclosed materials.

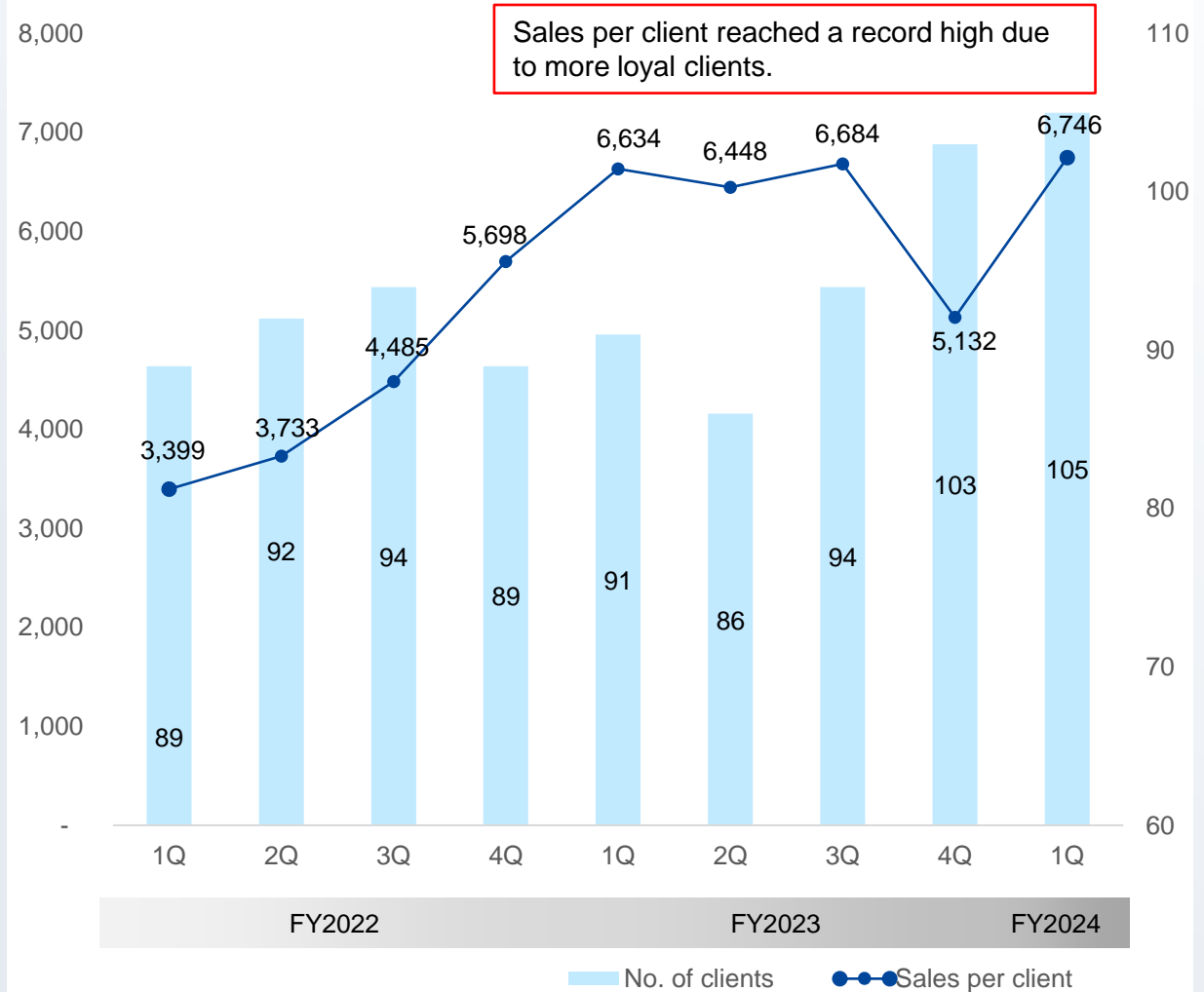
Unit Sales Price, Number of Projects and Contractual Chain Status by Service Category

Pct. of the Contractual Chain (FY2024 cumulative)



- Direct contracts with clients account for most of contracts.
- Even for the projects referred through alliance strategies, contracts are signed directly with the referred client.
- For enterprise companies, there may be a contract through a system subsidiary or a contract with a group company, in which case it is categorized as the first-tier subcontractor.

(Thousand yen) No. of Clients and Sales Per Client (Companies)

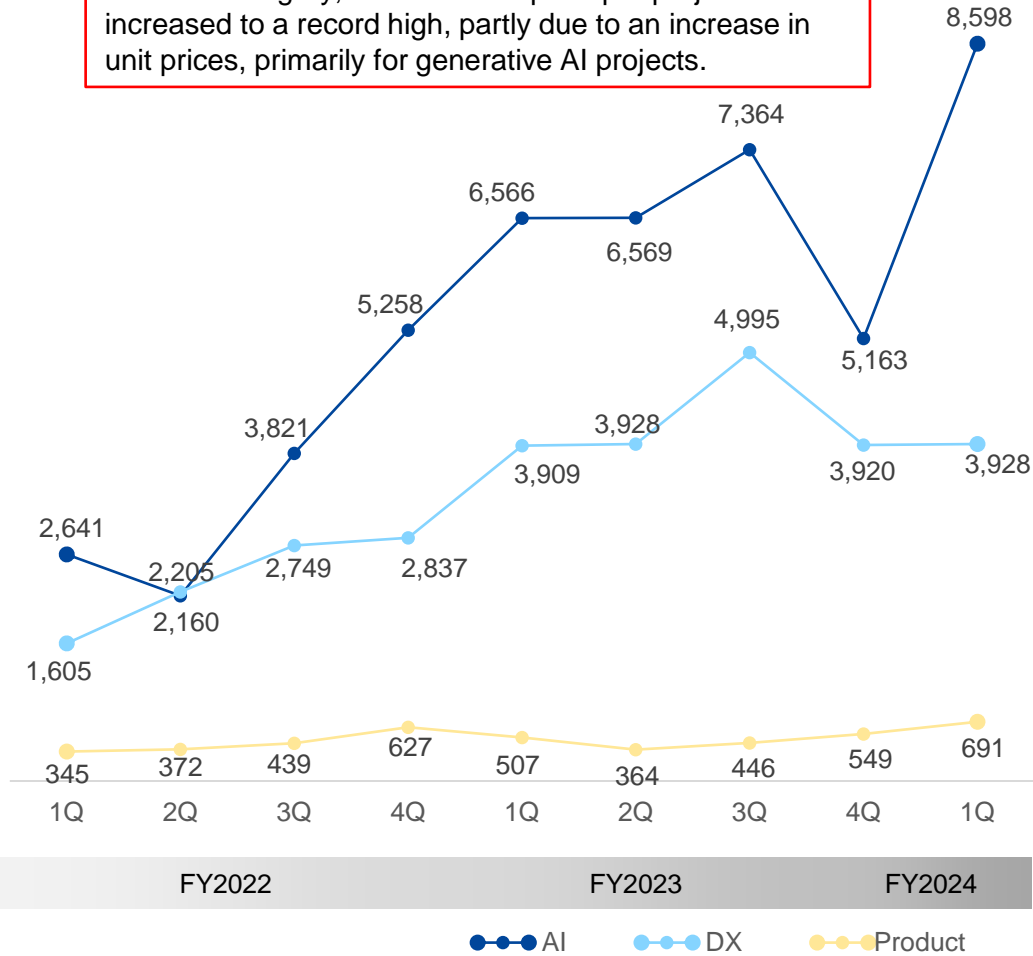


Unit Sales Price, Number of Projects and Contractual Chain Status by Service Category

Unit Sales Price by Service Category

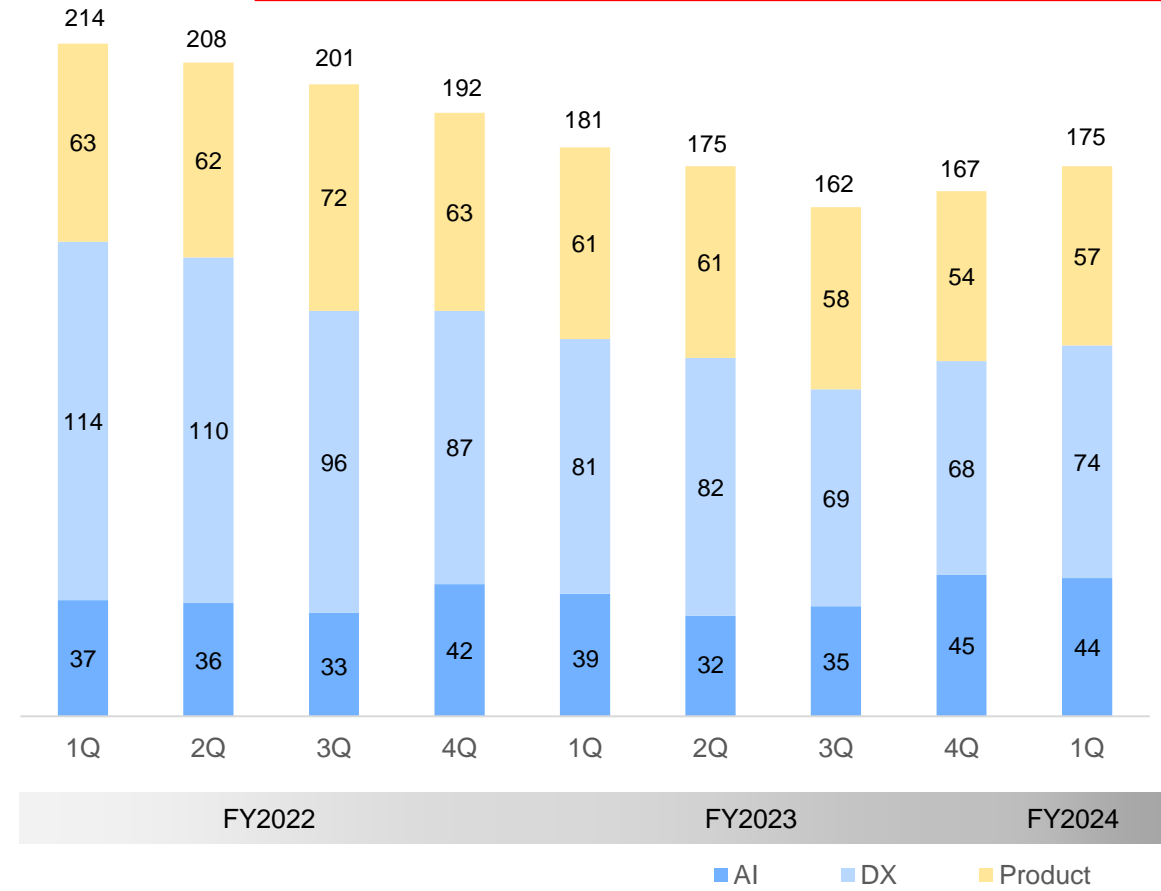
(Thousand yen)

In the AI category, the unit sales price per project increased to a record high, partly due to an increase in unit prices, primarily for generative AI projects.



No. of Projects by Service Category

The number of projects increased in 1Q due to an increase in projects to use up annual budgets, while large-scale projects increased in line with the progress with the addition of loyal clients.

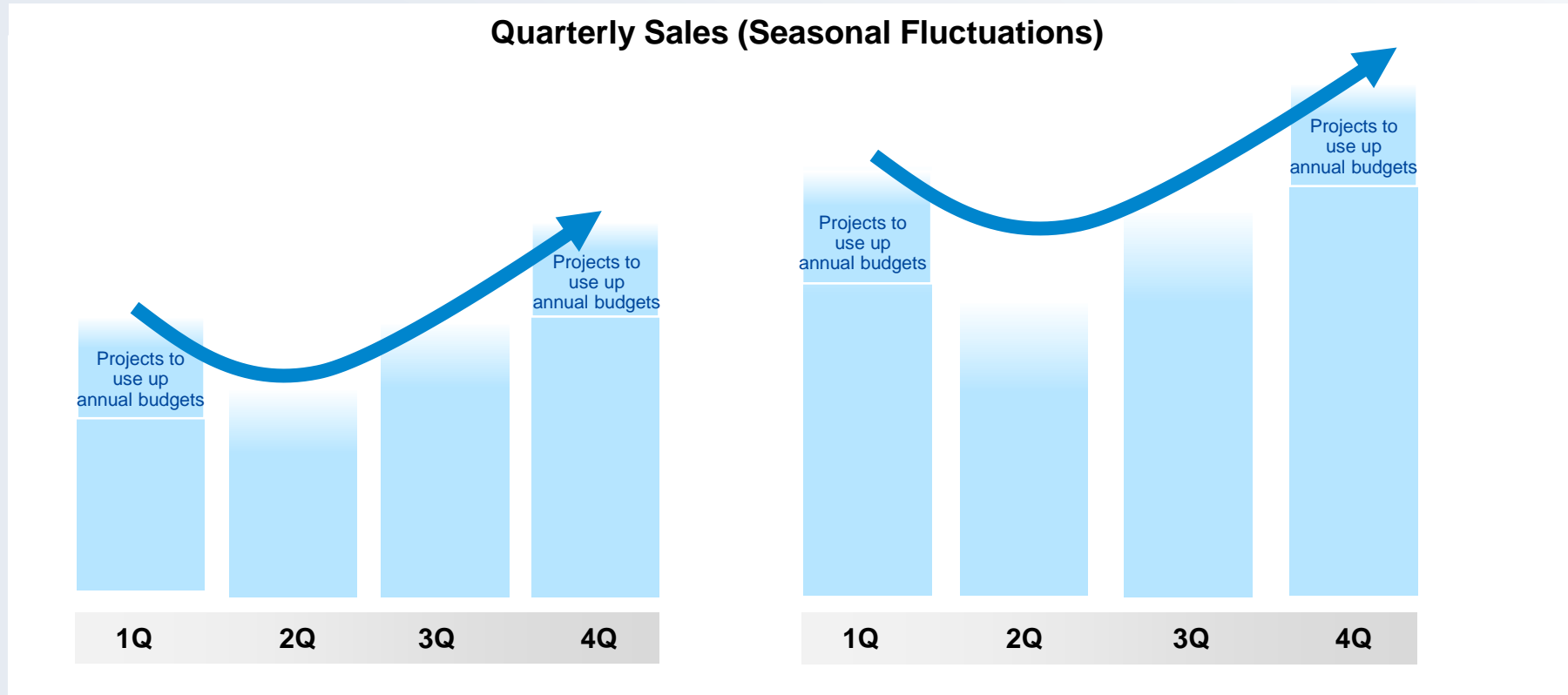


* Because the OPS Services category was discontinued from FY2024, the number of OPS projects in FY2022 and FY2023 has been allocated to the three other service categories.

▶ Seasonal Fluctuations in Net Sales

Headwaters' sales are budgeted in a quarterly budget plan that incorporates the following seasonal fluctuations.

- **In the first quarter and fourth quarter, sales are in an upward trend:** This is due to major client companies implementing projects to use up their annual budgets toward the end of the fiscal year.
- **In the second quarter, sales settle down:** This is because clients tend to start working slower entering a new fiscal year, and there are more sales proposal phases.
- In the majority of cases, the business model is also a human resource-intensive business model, and **progress in the number of new employees and sales activities will affect net sales in the second half of the year.**
 - ➔ As a medium- to long-term measure, net sales are expected to be leveled out by increasing net sales of recurring revenue businesses (Products).



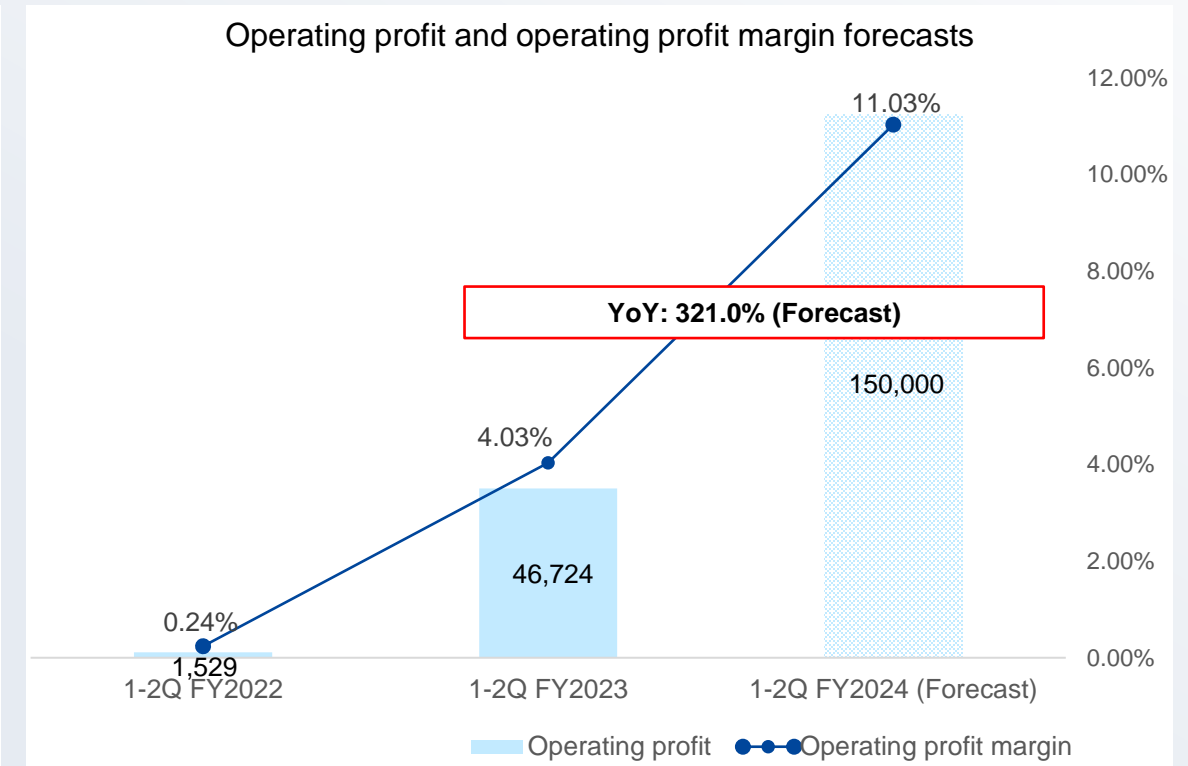
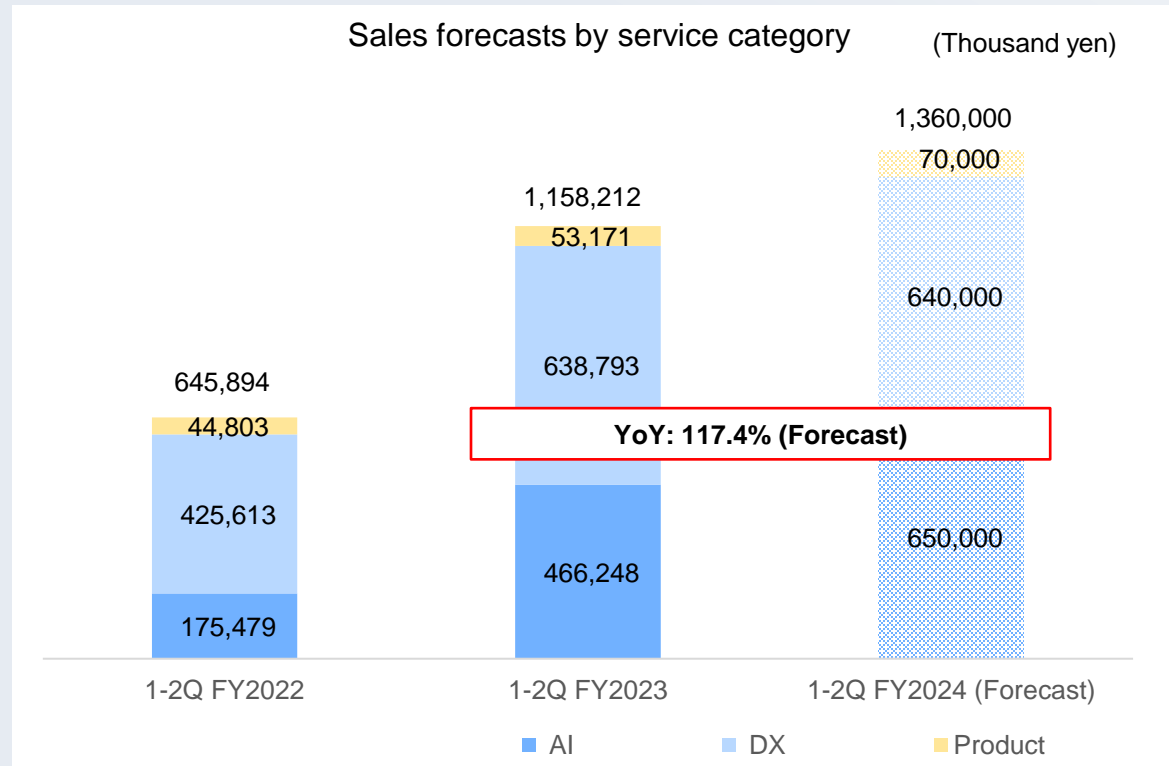
▶ 2Q Revenue Forecast

In terms of future earnings forecasts, the second quarter of FY2024 is also the weakest quarter for both sales and operating profit. Headwaters is focusing on three short-term points of focus for the third and fourth quarters: sales activities, human resources development, and recruitment activities.

QoQ sales and operating profit in comparison with the first quarter is expected to be lower as planned.

With 10 new graduates joining the company in April and mid-career recruitment progressing, it is expected that personnel expenses and recruitment expenses will rise, and the disparity in operating profit will be larger than that in sales.

On a YoY basis, steady growth is expected, as shown in the following graphs.



* Forecast figures may change as they are as of the time of disclosure of these materials.



IR News: <https://www.headwaters.co.jp/ir/news/>

■ Collaborations/Services

- ✓ Supported “Introduction of architecture using Azure PaaS” and “Microsoft Teams UX development” in the Asahi Kasei’s conference DX project
- ✓ Launched “Multimodal AI Lab Service” that provides AI support for complex generation of texts, voices, images and videos for companies using the Azure OpenAI Service
- ✓ Collaborated with Human Resocia for supporting the use of generative AI
- ✓ Launched “Multimodal AI Mobile App Copilot” service to support the development of unique mobile applications equipped with generative AI.
- ✓ Started verification of small-scale language model SLM and image language model VLM running on “NVIDIA Jetson Orin Nano” for achieving combination of generative AI and edge AI.

■ Collaborations/Services

- ✓ Selected as an outsourcing operator for implementing Shibuya City data linkage platform
- ✓ Certified as a Databricks SI consulting partner

■ Others

- ✓ Notice regarding changes of Executive Officers



- This document contains outlooks, future plans and management goals related to Headwaters. Descriptions regarding these forward-looking statements are based on assumptions made at the current moment about future events and trends, and there is no guarantee that these assumptions are accurate. Various factors may cause actual performance to significantly differ from what is described in this document.
- The figures in this document represent consolidated figures for the entire group, including Headwaters Consulting, Headwaters Professionals and DATA IMPACT JOINT STOCK COMPANY.
- In this document, numerical comparisons are presented in the following three categories.
 - **QoQ:** A comparison between the figures of the previous quarter and the current quarter
 - Comparison between figures of 4Q FY2023 and 1Q FY2024
 - **YoY:** A comparison between the cumulative figures of the previous fiscal year and the current fiscal year
 - Comparison between figures of 1H FY2023 and 1H FY2024
 - **YoY for the Quarter:** A comparison between the figures of the corresponding quarter for the previous fiscal year and the current fiscal year
 - Comparison between figures of 1Q FY2023 and 1Q FY2024
- Unless otherwise specified, the financial information in this document is based on generally accepted accounting principles in Japan.
- Information regarding companies other than Headwaters is based on generally known information.