

Polaris Holdings (3010)

Solid execution with strategic growth potential

21 August 2024

Q1 FY3/25 results update

- Establishing a track record of positive change** – Q1 FY3/25 results were in line with guidance, as the company demonstrated solid execution for domestic and overseas hotel operations, supported by continued positive market demand. Occupancy rates remain stable at a high level, and ADR and RevPAR remained on an uptrend YoY. We note that the company has reported three consecutive quarters of high single-digit OPM, reflecting an improvement in the quality of earnings, and management's strategies are delivering a sustained operational turnaround. The balance sheet continues to improve creditworthiness with a 31.6% equity ratio, and the earnings outlook remains positive with the new business collaboration with domestic hotel and restaurant operator Minacia Co., Ltd.

Maintaining our earnings estimates

- Growth remains on the cards** – the company has maintained FY3/25 guidance. We believe the business has de-risked and displays strategic growth potential which should result in strengthening free cash flow generation.
- Minacia opportunity** - Minacia's core business is hotels, with its 'Hotel Wing International' and 'Tenza' brands. According to the company, there are 39 domestic sites with 5,180 rooms making it the 27th largest operator in Japan. Polaris Holdings is ranked 20th, with the combined total resulting in 14,137 domestic rooms and an implied ranking of 10th place.
- Valuations** – we have left our earnings estimates unchanged, and the shares are trading on PER FY3/25 of 15.1x, an FCF yield of 11.2%, and a 1.6% dividend yield.

Year-end	3/23	3/24	3/25E	3/26E	3/26E
Sales (¥bn)	7.02	22.55	20.56	23.75	26.33
OP (¥bn)	0.00	3.38	2.06	2.73	3.16
NI (¥bn)	0.53	2.36	1.53	1.84	1.98
EPS (¥)	4.98	19.21	12.42	15.02	16.15
DPS (¥)	-	-	3.00	4.51	4.84
Sales growth YoY (%)	+89.0	+221.3	-8.8	+15.5	+10.9
OP growth YoY (%)	N/A	N/A	-39.2	+32.8	+15.7
NP growth YoY (%)	N/A	+341.5	-35.3	+20.9	+7.5
EPS growth YoY (%)	N/A	+285.8	-35.3	+20.9	+7.5
PER (x)	37.8	9.8	15.1	12.5	11.6
EV/EBITDA (x)	43.4	7.9	12.1	9.4	8.2
EV/Sales (x)	4.6	1.4	1.6	1.4	1.2
PBR (x)	8.3	3.5	3.5	4.3	5.0
ROE (%)	18.4	34.3	22.3	33.3	41.4
ROCE (%)	0.0	19.4	11.8	17.0	20.6
FCF yield (%)	(0.5)	32.5	11.2	8.2	10.9
Dividend yield (%)	-	-	1.6	2.4	2.6

Source: Company, Astris Advisory (estimates)

*Note: outstanding dilution is 8.4%

Share price: ¥188 Market cap: ¥24.1bn



Source: Bloomberg

Price Performance				
	YTD	1M	3M	12M
Abs (%)	+13.9	-14.9	-16.4	+9.3
Rel (%)	+1.2	-8.7	-13.5	-8.1

Company sector	
Real Estate Management/Services	
Hotels, Restaurants & Leisure (GICS)	

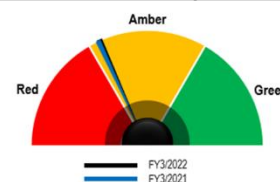
Stock data	
Price (¥)	188
Mkt cap (¥bn)	24.1
Mkt cap (\$m)	164.6
52-week range (¥)	134-285
Shares O/S (m)	127.9
Average daily value (\$m)	0.7
Free float (%)	24.5
Foreign shareholding (%)	77.4
Ticker	3010
Exchange	Tokyo Standard
Net Debt/Equity (x)	4.4
FFO leverage (x)	1.2
BBG BUY HOLD SELL	0 0 0

Source: Bloomberg

Business Overview

Polaris Holdings is a hotel operator with three domestic key franchises - Best Western Japan, KOKO HOTEL, and Value The Hotel. It is shifting its business model towards low-risk management contracts, variable-rent lease contracts, and as an owner/operator.

Astris-Sustainability ESG rating



Reference Ratings	
MSCI	N/A
Sustainalytics	N/A
Refinitiv	N/A
S&P Global	N/A
Bloomberg	N/A

Next events

Q2 FY3/25 results November 2024

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This report has been commissioned and paid for by the company

Recent results

Q1 FY3/25 results

Results appear in line with guidance

Key financials

(¥bn)	Q1 FY3/24	Q1 FY3/25	YoY (%)
Sales	2.74	4.75	+73.4
Gross profit	2.57	4.55	+76.7
Gross margins (%)	94.0	95.8	
Operating profit/(loss)	0.18	0.44	+142.1
Operating margins (%)	6.7	9.3	
Recurring profit	(0.00)	0.29	N/A
Net income attributable to the parent	(0.03)	0.26	N/A

Source: Company

Hotel operations driving earnings with improving segmental profitability YoY

Per business segment (pre-elimination)

(¥bn)	Q1 FY3/24	Q1 FY3/25	YoY (%)
Sales			
Hotel operations	2.79	4.73	+73.5
Real estate	0.13	0.02	-86.9
Operating profit/(loss)			
Hotel operations	0.27	0.61	+126.4
Real estate	0.06	0.02	-73.4
Operating margins			
Hotel operations	9.8	12.8	
Real estate	47.6	96.3	

Source: Company

Key highlights

Q1 FY3/25 results were in line with guidance in our view, with sustained high occupancy rates both domestically and overseas, rising ReVPAR and stable operating margins. The key takeaways are as follows:

- **Market environment remained positive**, with continued momentum from inbound demand. This has helped to maintain high occupancy rates and room rates.
 - Domestic occupancy rate was 80.3% (Q4 FY3/24 79.3%), overseas occupant rate was 69.3% (Q4 FY3/24 66.3%).
 - Domestic average daily rate at ¥11,463 (+13.7% YoY), and RevPAR at ¥9,544 (+27.6% YoY). Overseas average daily rate at 1,645 Pesos (+20.3% YoY), and RevPAR at 1,139 Pesos (+30.9% YoY).
- **Quarterly OPM of 9.3%** demonstrated stable profitability, with three reported consecutive quarters of high single-digit margins.



- **The balance sheet demonstrates a stable and improving equity ratio**, reaching 31.6%.
- In line with the medium-term management plan, the company made a **joint investment with sponsor Star Asia Group in the unlisted hotel and restaurant operator Minacia**. A business alliance agreement is in place to realize synergies through collaboration.
 - Minacia’s core business is hotels, with its ‘Hotel Wing International’ and ‘Tenza’ brands. There are 39 domestic sites with 5,180 rooms making it the 27th largest operator in Japan (Polaris Holdings is ranked 20th, with the combined total resulting in 14,137 domestic rooms and an implied 10th ranking).
 - It also operates a restaurant business primarily with its ‘Yumezen’ Japanese izakaya dining chain.

Guidance for FY3/25

The company’s **guidance indicates a strong underlying earnings trajectory**, exemplified by the adjusted growth profile YoY when ignoring the one-time impact of the real estate disposals in FY3/24.

The company has also reinstated FY dividends of ¥3 per share, implying a payout ratio of 25.3%. This positive development indicates that the company’s financial health has improved sufficiently, and demonstrates a new commitment to shareholder value creation.

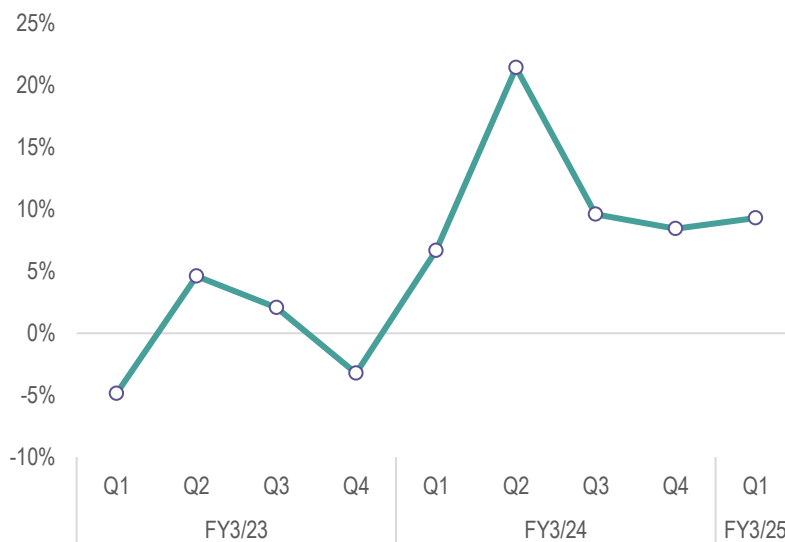
FY3/25 company guidance

(¥bn)	FY3/24 (actual)	FY3/24 (adjusted actual)	FY3/25 guidance	YoY (%)	YoY (adjusted %)
Sales	22.55	14.55	20.08	-10.9	+38.0
Gross profit	15.95	-	-		
Gross profit margin (%)	70.8	-	-		
Operating profit	3.38	1.34	1.89	-44.1	+41.6
Operating profit margin (%)	15.0	9.2	9.4		
Recurring profit	2.61	0.69	1.32	-49.6	+91.2
Net income	3.30	1.38	1.47	-55.3	+7.0
DPS (¥) (FY-basis)	-	-	3.0	-	-
Payout ratio (%)	-	-	25.3	-	-

Source: Company

Q2 FY3/24 benefitted from one-time asset sale, but underlying profitability trend remains on a positive trajectory

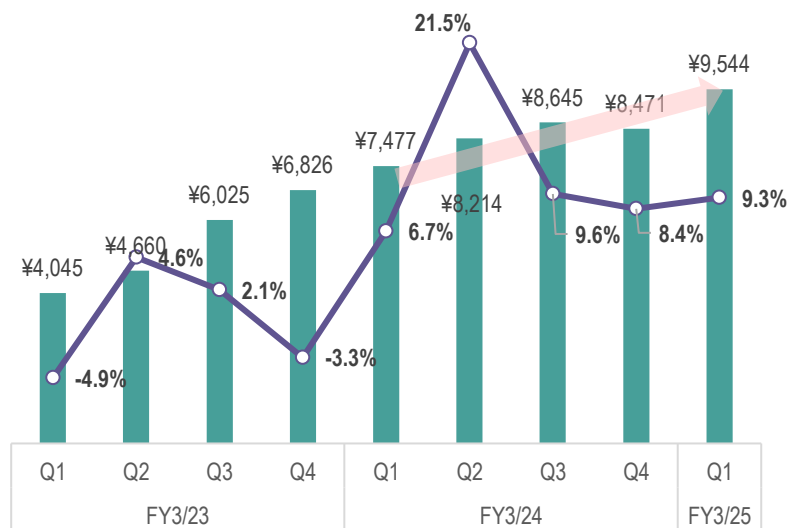
Quarterly operating margin trend (%)



Source: Company

Q1 FY3/25 domestic RevPAR grew 27.6% YoY

Quarterly trend in total OPM (%) and Domestic RevPAR (¥)

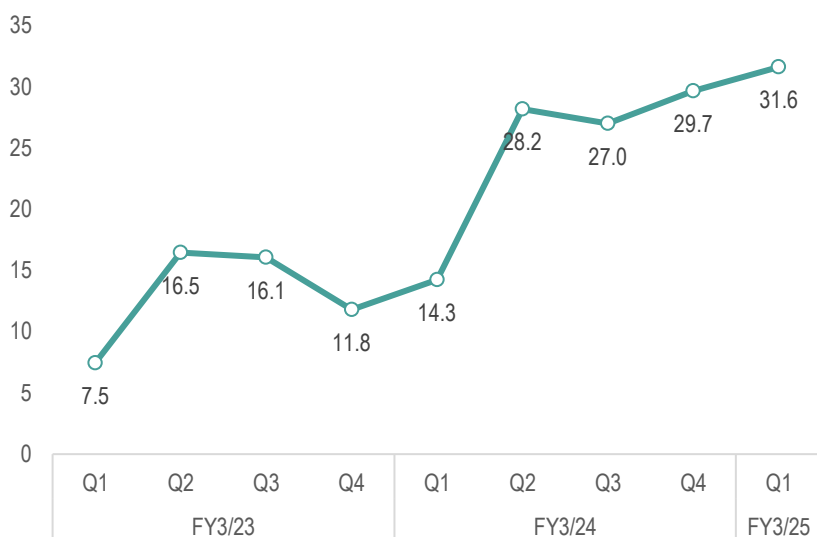


Source: Company



Balance sheet shows a continued trend of reducing reliance on debt financing

Quarterly trend equity ratio (%)



Source: Company

National occupancy rates for business (Polaris' area of focus), city hotels continue to outperform the overall market

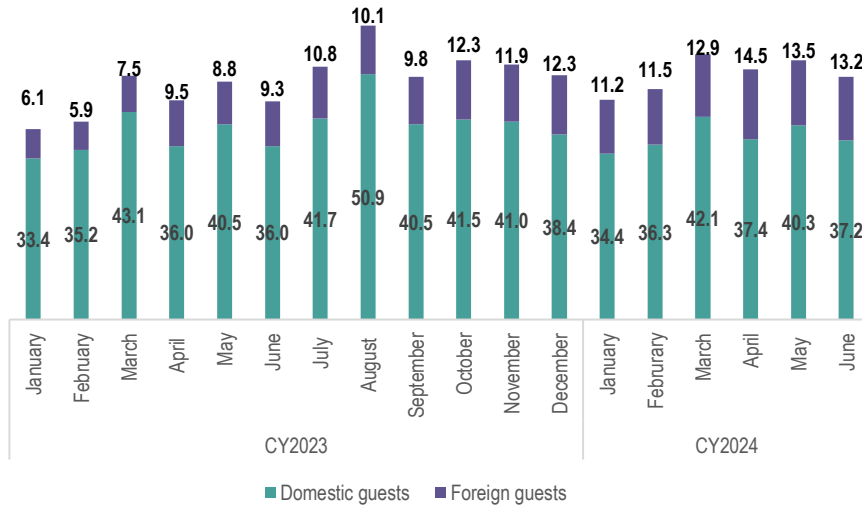
National occupancy rate trend



Source: Japan Tourism Agency



Continued momentum of foreign guest overnight stays into CY24
 The national trend in the number of guests (per million overnight stays per month)



Source: Japan Tourism Agency



Astris earnings estimates and key assumptions

We have maintained our earnings estimates for FY3/25 and beyond.

Astris Advisory earnings estimates

Year-end	FY3/25 guidance	FY3/25E	FY3/26E	FY3/27E
Sales (¥bn)	20.08	20.56	23.75	26.33
<i>Growth YoY (%)</i>	-10.9	-8.8	+15.5	+10.9
Operating profit (¥bn)	1.89	2.06	2.73	3.16
OPM (%)	9.4	10.0	11.5	12.0
EBITDA (¥bn)	N/A	2.67	3.44	3.95
EBITDA margin (%)	-	13.0	14.5	15.0
Recurring profit (¥bn)	1.32	1.37	2.05	2.48
<i>Growth YoY (%)</i>	-49.6	-47.3	+49.1	+20.9
*Implied effective tax rate (%)	-11.4	-11.0	10.0	20.0
Net income (¥bn)	1.47	1.53	1.84	1.98
<i>Growth YoY (%)</i>	-55.3	-35.4	+34.2	+7.5
DPS (¥)	3.0	3.0	4.5	4.8
Payout ratio (%)	25.3	26.8	30.0%	30.0%
Dividend yield (%)	1.2	1.2	1.7	1.8
FCF (¥bn)	N/A	2.58	1.88	2.52
FCF margin (%)	-	2.4	3.4	4.4
FCF conversion (%)	-	39.2	47.3	48.3
FCF yield (%)	-	11.2	8.2	10.9
Diluted FCF yield (%)	-	10.3	7.5	10.1

Source: Astris Advisory

Note: FCF conversion is FCF/Pre-tax Profit

Note*: Implied effective tax rate assumes no extraordinary gains or losses



Current domestic hotel portfolio – 33 hotels

Name	Location	Rooms	Contract type
BW Osaka Tsukamoto	Osaka	105	Fixed + variable rent
BW Plus Hotel Fino Chitose	Chitose	154	Fixed + variable rent
BW Plus Hotel Fino Osaka Kitahama	Osaka	129	Fixed rent lease
NEW BW Plus Nagoya Sakae	Nagoya	143	Fixed + variable rent
BW Hotel Fino Tokyo Akasaka	Tokyo	87	Fixed + variable rent
BW Hotel Fino Shin Yokohama	Yokohama	108	Fixed + variable rent
BW Plus Fukuoka Tenjin Minami	Fukuoka	236	Fixed + variable rent
VTH Ishinomaki	Miyagi	82	Fixed rent lease
VTH Narahakidoekimae	Fukushima	107	Fixed rent lease
Sure Stay Plus Hotel Shin-Osaka	Osaka	108	Fixed + variable rent
KOKO HOTEL Osaka Namba	Osaka	100	Variable rent lease
BW Hotel Fino Osaka Shinsaibashi	Osaka	179	Management contract
KOKO HOTEL Ginza Itchome	Tokyo	305	Fixed + variable rent
KOKO HOTEL Sapporo Ekimae	Sapporo	224	Fixed + variable rent
KOKO HOTEL Fukuoka Tenjin	Fukuoka	159	Fixed + variable rent
KOKO HOTEL Hiroshima Ekimae	Hiroshima	250	Fixed + variable rent
KOKO HOTEL Kagoshima Tenmonkan	Kagoshima	295	Fixed + variable rent
KOKO HOTEL Premier Kanazawa Korinbou	Kanazawa	207	Management contract
KOKO HOTEL Premier Tokyo Nihonbashi Hamacho	Tokyo	223	Fixed rent lease
KOKO HOTEL Nagoya Sakae	Nagoya	204	Management contract
KOKO HOTEL Osaka, Shinsaibashi	Osaka	211	Management contract
KOKO HOTEL Kobe, Sannomiya	Kobe	141	Fixed rent lease
KOKO HOTEL Premier Kumamoto	Kumamoto	205	Management contract
KOKO HOTEL Residence Tokyo, Asakusa Kappabashi	Tokyo	47	Management contract
KOKO HOTEL Residence Tokyo, Asakusa Tawaramachi	Tokyo	42	Management contract
KAYA Kyoto Nijo Castle, BW Signature Collection by BW	Kyoto	57	Management contract
KOKO HOTEL Sendai Kotodai Park	Sendai	230	Management contract
KOKO HOTEL Sendai Station West	Sendai	170	Management contract
KOKO HOTEL Sendai Station South	Sendai	190	Management contract
VTH Higashi Matsushima Yamoto	Miyagi	407	Owner-and-operator
VTH Sendai Naton	Miyagi	314	Owner-and-operator
KOKO HOTEL Tsukiji Ginza	Tokyo	188	Management contract
*Fino Hotel Sapporo Odori	Sapporo	145	Fixed + variable rent
Domestic total		5,752	

Source: Company

*Note: rebranded as KOKO HOTEL Sapporo Odori in April 2024



The Philippine overseas platform is to operate the “Red Planet” brand hotels as an owner-operator. Furthermore, Red Planet BGC The Fort had a soft opening in December 2023, with the formal opening in May 2024, and is expected to grow earnings.

Hotel Portfolio in the Philippines – 14 hotels

Name	Location	Rooms	Contract type
Red Planet Davao	Davao	155	Owner-and-operator
Red Planet Manila Ortigas	Pasig	182	Owner-and-operator
Red Planet Aurora Boulevard	Quezon	167	Owner-and-operator
Red Planet Manila Aseana City	Paranaque	200	Owner-and-operator
Red Planet Manila Amorsolo	Makati	189	Owner-and-operator
Red Planet Angeles City	Angeles	165	Owner-and-operator
Red Planet Cebu	Cebu	150	Owner-and-operator
Red Planet Manila Mabini	Manila	167	Owner-and-operator
Red Planet Manila Bay	Manila	150	Owner-and-operator
Red Planet Manila Binondo	Manila	171	Owner-and-operator
Red Planet Manila Makati	Makati	213	Owner-and-operator
Red Planet Cagayan de Oro	Cagayan de Oro	159	Owner-and-operator
Red Planet Quezon Timog	Davao	140	Owner-and-operator
NEW Red Planet BGC The Fort	Bonifacio Global City	245	Owner-and-operator
Total		2,453	

Source: Company



Summary

Polaris Holdings is a hotel operator with four core brands (three domestic, and one overseas) with the acquisition of Red Planet's business in the Philippines. During the pandemic, it underwent significant capital raising and is positioned to capitalize on the recovering hotel demand in a post-pandemic environment.

With the support of the Star Asia Group and with the key focus on stable earnings growth, the company is implementing strategic investments into substantial reforms and demonstrating growth in the hotel market, and recovery and growth since the COVID-19 pandemic has been remarkable.

Growth strategy in the medium-term management plan

Shifting hotel
operator model to
higher return
formats

- In the medium-term management plan, the growth drivers are to 'increase the number of hotel locations and the number of rooms in operation' and 'improve the profitability of operated hotels.' The target is to reach 60 operated hotels and 10,000 operational hotel rooms by FY3/27.
- Actively transitioning from the domestic legacy model involving long-term fixed rent leases towards low-risk **"Fee-For-Service"** management and variable rent lease contracts, and constructing a portfolio that balances growth and stability by incorporating a well-balanced mix of fixed-rent and ownership-type assets where more upside potential can be realized.
- As a member of the Star Asia Group ecosystem, it is possible to implement flexible strategies such as expanding opportunities to manage new hotels, achieving long-term operational revenue, and executing selective investments or joint investments as an owner-operator.
- In addition to hotel operation contracts from Star Asia Group, to continue expanding the business portfolio by accepting operations from new third-party owners.

We estimate that Polaris Holdings will experience major growth in FY3/25 and beyond driven by the following factors:

- The business environment will return to similar levels seen in CY2019 or above.
- Consequent improving demand and sales mix will drive additional TRevPAR growth.
- The shift in the hotel operating model is expected to improve operational leverage by reducing fixed costs and increasing earnings, while concurrently the outlook is for achieving higher growth through more profitable operational models.

The shares are trading on an estimated PER FY3/25 of 15.1x, an FCF yield of 11.2%, and a 1.6% dividend yield.



JGAAP Financial Summary

(¥bn)	FY 3/23	FY 3/24	FY 3/25E	FY 3/26E	FY 3/27E
Sales	7.02	22.55	20.56	23.75	26.33
COGS	0.51	6.59	2.06	2.37	2.63
Gross profit	6.51	15.95	18.51	21.37	23.70
Gross profit margin (%)	92.7	70.8	90.0	90.0	90.0
Operating profit	0.00	3.38	2.06	2.73	3.16
OP margin (%)	0.0	15.0	10.0	11.5	12.0
Non-operating income	0.03	0.05	0.05	0.05	0.05
Non-operating expense	(0.25)	(0.82)	(0.73)	(0.73)	(0.73)
Recurring profit	(0.22)	2.61	1.37	2.05	2.48
Extraordinary gains	1.46	1.46	-	-	-
Extraordinary losses	(0.69)	(0.69)	-	-	-
Pre-tax profit	0.55	3.38	1.37	2.05	2.48
Tax	0.02	1.02	(0.15)	0.20	0.50
Effective tax rate (%)	(5.4)	(3.6)	(11.0)	10.0	20.0
Net income	0.53	2.36	1.53	1.84	1.98
Non-controlling NI	-	-	-	-	-
Parent attributable NI	0.53	2.36	1.53	1.84	1.98
Sales growth YoY (%)	+89.0	+221.3	-8.8	+15.5	+10.9
OP growth YoY (%)	N/A	N/A	-39.2	+32.8	+15.7
NI growth YoY (%)	N/A	+341.5	-35.3	+20.9	+7.5

Balance sheet (¥bn)	FY 3/23	FY 3/24	FY 3/25E	FY 3/26E	FY 3/27E
Cash & equivalents	4.28	3.38	11.96	11.25	11.10
Trade debtors	1.84	1.76	0.23	0.23	0.23
Real estate for sales and stock	5.86	-	-	-	-
Other	0.88	2.81	0.37	0.37	0.37
Current assets	12.86	7.96	12.56	11.85	11.70
Tangible assets	9.87	12.81	5.50	5.12	4.68
Intangible assets	0.03	0.03	0.03	0.03	0.03
Investment & others	1.89	2.41	2.41	2.41	2.41
Fixed assets	11.79	15.25	7.95	7.57	7.12
Total assets	24.65	23.21	20.51	19.41	18.82
Short term borrowing	1.74	1.83	1.83	1.83	1.83
Trade creditors	0.39	0.36	0.14	0.17	0.18
Other	2.62	3.58	1.16	1.33	1.48
Current liabilities	4.75	5.78	3.13	3.33	3.50
Long term borrowing	15.50	9.89	9.89	9.89	9.89
Other LT liabilities	1.49	0.65	0.65	0.65	0.65
Long term liabilities	16.99	10.54	10.54	10.54	10.54
Shareholder's equity	2.91	6.88	6.84	5.54	4.78
Non-controlling interests	-	-	-	-	-
Total net assets	2.91	6.88	6.84	5.54	4.78
Total liabilities & net assets	24.65	23.21	20.51	19.41	18.82

Source: Company, Astris Advisory (estimates)

Cash flow statement (¥bn)	FY 3/23	FY 3/24	FY 3/25E	FY 3/26E	FY 3/27E
Profit before tax	0.55	3.38	1.37	2.05	2.48
Depreciation/amortization	0.74	0.70	0.62	0.71	0.79
Other non-cash items	(1.37)	(1.19)	(0.50)	(0.84)	(0.67)
Changes in working capital	(0.04)	4.85	1.32	0.20	0.16
Cash from Operating Activities	(0.11)	7.74	2.81	2.12	2.76
Capex	(0.00)	(0.24)	(0.24)	(0.24)	(0.24)
Acquisitions/increase stakes	(0.27)	(0.02)	-	-	-
Other investing cash flow	(0.46)	(1.40)	(0.93)	(1.17)	(1.05)
Cash from Investing Activities	(0.73)	(1.66)	(1.17)	(1.40)	(1.28)
Total cash dividends paid	-	-	-	(0.37)	(0.55)
Debt issuance/(retirement)	0.04	(6.48)	-	-	-
Equity financing	2.18	0.61	-	-	-
Other	(0.04)	(1.08)	(1.08)	(1.08)	(1.08)
Cash from Financing Activities	2.19	(6.94)	(1.08)	(1.44)	(1.63)
FX impact	-	0.01	0.01	0.01	0.01
Net cash flow	1.35	(0.85)	0.58	(0.72)	(0.15)
Free cash flow	(0.11)	7.50	2.58	1.88	2.52
EBITDA	0.75	4.09	2.67	3.44	3.95
Free cash flow margin (%)	-3.2	2.3	2.4	3.4	4.4
Free cash flow conversion (%)	N/A	40.1	39.2	47.3	48.3
EBITDA margin (%)	10.6	18.1	13.0	14.5	15.0
Capex/sales (%)	0.2	0.2	0.1	0.1	1.1
Capex/depreciation (%)	30.4	26.3	23.3	21	22
CFO margin (%)	-3.1	2.4	2.6	3.5	4.5

Key metrics	FY 3/23	FY 3/24	FY 3/25E	FY 3/26E	FY 3/27E
Profitability					
Gross margin (%)	92.7	70.8	90.0	90.0	90.0
Operating margin (%)	0.0	15.0	10.0	11.5	12.0
Net margin (%)	7.6	10.5	7.4	7.8	7.5
ROA (%)	2.2	10.2	7.4	9.5	10.5
ROE (%)	18.4	34.3	22.3	33.3	41.4
ROCE (%)	0.0	19.4	11.8	17.0	20.6
ROIC (%)	0.0	18.1	12.3	13.7	15.0
Liquidity					
Current ratio (x)	2.7	1.4	4.0	3.6	3.3
Quick ratio (x)	1.5	1.4	4.0	3.6	3.3
Leverage					
Debt/Equity ratio (x)	5.9	1.7	1.7	2.1	2.5
Net Debt/Equity ratio (x)	4.4	1.2	N/A	0.1	0.1
Equity ratio (x)	0.1	0.3	0.3	0.3	0.3
Interest cover (x)	0.0	4.6	2.8	3.8	4.3
Net Debt/EBITDA (x)	17.4	2.0	N/A	0.1	0.2
Valuation					
EPS reported (¥)	4.98	19.21	12.42	15.02	16.15
PER (x)	37.8	9.8	15.1	12.5	11.6
Diluted PER (x)	40.9	10.6	16.4	13.6	12.6
DPS (¥)	-	-	3.0	4.5	4.8
Dividend payout ratio (%)	-	-	24.1	30.0	30.0
Dividend yield (%)	-	-	1.6	2.4	2.6
Free cash flow yield (%)	(0.5)	32.5	11.2	8.2	10.9
Diluted FCF yield (%)	(0.5)	30.0	10.3	7.5	10.1
PBR (x)	8.3	3.5	3.5	4.3	5.0
EV/sales (x)	4.6	1.4	1.6	1.4	1.2
EV/EBITDA (x)	43.4	7.9	12.1	9.4	8.2
EV/EBIT (x)	10,517	9.6	15.8	11.9	10.3
EV/FCF (x)	N/A	4.3	12.6	17.2	12.8



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