SRE Holdings (2980 JP)

Transformation into an AI cloud company

Executive Summary

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SRE Holdings（2980 JP）

Share Price (13 March, 2025) JPY 2,840

Market Cap US$ 311 million

FY (Mar-end)	F25E	F26E	F27E	F28E
EPS	121	162	214	291
P/E	19.0x	17.6x	13.3x	9.8x
EV/EBITDA	14.1x	11.4x	8.9x	6.7x
P/B	3.5x	3.4x	2.9x	2.6x
Dividend Yield	0.5%	0.5%	0.5%	0.5%
ROE	15.5%	19.6%	23.5%	27.7%
FCF Conversion	55%	52%	60%	67%
ROIC ex-cash	11.6%	14.1%	17.4%	21.9%
Incremental ROI*	43%	29%	31%	43%

*FCF Conversion = FCF ÷ Net Profit

**Incremental ROI = Incremental Change in OpCF ÷ Incremental Change in Invested Capital

SRE is in the midst of a business transformation from a Real Estate Service company to a high margin AI solutions business where it is becoming an increasing presence due to its unique value proposition. The growth and margins for AI Cloud & Consulting (AICC) buiness, specifically in the healthcare field, is set to contribute significantly to the group earnings in the coming years. With wider acceptance of AI solutions as well as the strong need for Digital Transformation in medical and welfare facilities, we believe this backdrop is set to become a multi-year tailwind for SRE.

The key point to the Equity Story is the following:

① Significant opportunity for acceleration and business transformation through Life & Healthcare (LH: Healthcare, Finance, IT) cloud solutions

CGS believes SRE to be at an inflection point with sustainable high profit growth driven by the healthcare cloud solutions which is recurring revenue, high margin business with a strong value proposition. Particularly in healthcare, SRE sees a large opportunity where there is a strong need for labor efficiency. Through it's differentiated AI solutions, SRE is winning new customers and sees a pipeline of opportunities in the medium-term.

② Operating Profit to grow 32%CAGR through FY27 and to reach ¥7bn

In this report, CGS forecasts number of customers in the Life & Healthcare Solution (LH) segment to triple by FY27, griving an acceleration in earnings. SRE sees a significant greenfield opportunity with a large TAM where it looks to growth through both new customer acquisition as well as through the cross-sell of new products developed over time.

③ Through the transformation to a recurring, asset light business, this warrants a re-rating of EBITDA multiple per 1% growth

For the valuation, CGS compares SRE to several industries related to the company's various segments based on EV/EBITDA per % profit growth. CGS believes that the company is significantly undervalued from all aspects. Based on the assessment of SRE's transformation into a more asset light business model and it's improvement in FCF generation there is an opportunity for a re-rating in valuation multiples.

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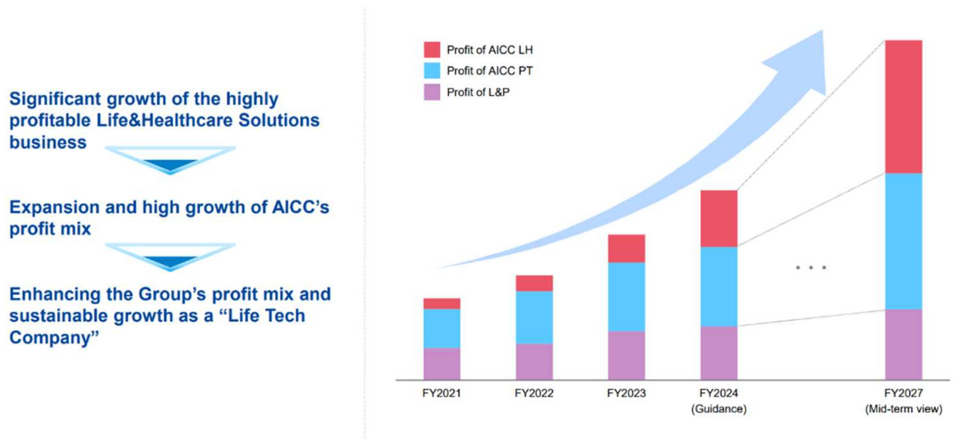
*CGS Estimates

Equity Story ① Significant opportunity for acceleration and business transformation through Life & Healthcare cloud solutions

Summary: We expect the fast-growing Life and Healthcare business in AI Cloud & Consulting (AICC) segment to become the main contributor for SRE's group-level revenue and profits over the Medium Term, driven by the strong interest from customers particularly in the healthcare field. This business has the potential to provide significant efficiency gains for healthcare clinics by providing a combination of BPO and cloud solutions leveraging AI developed by SRE to streamline customer's day-to-day operations.

○ With the healthcare industry seeing strong tailwinds for digital transformation (DX), we see a large market opportunity for SRE's solutions where we believe the company offers a competitive suite of products and services. Through this, we expect SRE's group revenue and earnings to accelerate, transforming SRE into a high growth, high margin cloud solution business.

Ex 1 : Company Medium-Term Plan Image



(Source: SRE)

Outline of the healthcare cloud business

○ SRE operates through 2 main segments which are AI Cloud & Consulting (AICC) and Life & Property (L&P). Within AICC there is the Life & Healthcare (LH) solution and the PropTech (PT) business. In recent years, SRE has been investing its resources to scale its AI Cloud & Consulting (AICC) services, a scalable solution which provides customers with a combination of Industry specific AI cloud solutions and Consulting services. This includes business process outsourcing to allow customers to focus on their main front-office workflow and maximize efficiency.

○ Application for its self-developed AI solution have been wide, ranging a variety of needs in multiple end markets. This is achieved in several ways. Firstly, such solutions can automate cumbersome workflow which previously required manual input, shortening the time required by several magnitudes. Secondly, the potential for human error can be reduced significantly thus reducing costs to related to such errors. Lastly, through such automation, employees can maximize time spent on the most value-additive components of their work based on their designated roles. At an organizational level this therefore leads to both growth opportunities and an improvement in the company's profitability with less reliance on hiring, something that is becoming more difficult to do.

○ SRE has now placed a focus on the healthcare field, where it is gaining strong traction and sees a pipeline of opportunities to expand for the coming years. Healthcare customers, mainly medical and welfare facilities appreciate the strong support from SRE through a combination of BPO/Consulting and Digital Cloud solutions which has reduced unnecessary workflow for already overburdened healthcare employees. An example is the support for reporting and keeping track of any regulatory changes.

○ Management is receiving strong interest from potential new customers and is confident that this will become a core growth driver. Compared to SRE's original Life & Property (L&P) business, this is a higher margin, asset light business that is cashflow generative. Thus, a fundamentally more robust business model.

○ The Life & Healthcare (LH) solutions is part of SRE's AI Cloud & Consulting (AICC) segment. Whilst this also includes various end markets such as finance and IT, management determined healthcare as the focus area in the coming years. Revenues involve a combination of recurring revenues coming from monthly subscription fees and flow-type revenue generated from consulting and BPO.

○ Cloud solutions provided in the healthcare field address a variety of problems to allow facilities to run more effectively and improve profitability. Such solutions can range from customer service tools, marketing and back-office automation solutions. For example, SRE has developed an AI Chatbot for such facilities, which was first created for its real estate business but now specialized for the healthcare domain. This creates additional touchpoints with patients which allows for continued relationship management, timely recommendation for check-ups and reservations managed through the platform. SRE also has a management support solution which allows facilities for an efficient streamlining of non-core workload and back-office tasks that are often tedious and limited value add for facilities.

○ Currently, the Life & Healthcare (LH) segment has 297 customers (as of December 2024). We note that the Monthly ARPC is ¥649,000, significantly higher than the PropTech (PT) segment. Thus, the sales contribution remains significant despite its smaller customer count compared to PropTech (PT). We believe that for the Life & Healthcare (LH) segment the healthcare field will be the core growth driver in the medium-term.

○ We summarize the 5 key rationales for growth in the Healthcare domain:

1. Strong recognition from clients and a highly skilled team
2. Strong need for healthcare DX creates a favorable environment
3. Healthcare market has a significant greenfield opportunity
4. SRE's competitive advantages due to its unique business model
5. Additional growth potential through M&A

1. Strong recognition from clients and a highly skilled team

○ SRE's unique approach of providing a set of AI SaaS Cloud solution alongside consulting and BPO services allows the company to develop solutions that are highly attuned to client's pain points resulting in high customer satisfaction. By directly working with clients to improve efficiency, SRE can identify ‘real world’ practical problems clients are facing which becomes a source to develop a digital solution. With this strategy, the company has been able to acquire strong expertise in healthcare in relatively short order.

○ SRE has been able to garner a strong reputation in the healthcare field in a relatively short time which has enabled the company to win further contracts from new facilities. We attribute this rapid success to SREs ability to hire and build a team of experienced business professionals and consultants within the medical industry which have previously worked at other well-established healthcare service technology firms. Such hires have allowed SRE to approach customers with a strong reputation, specific sales know-how and an eye for problem solving for key inefficiencies among facilities.

○ A key issue has been that medical professionals have been too busy to conduct any sales meetings with IT solution vendors to begin with. Through consulting and BPO services however, SRE is able to directly lend a hand to the operations of the facility and with it specify pain points to develop a digital solution together.

2. Strong need for Healthcare DX creates a favorable environment

○ Japan is suffering a shortage of labor owing to the aging demographics and consequently a shrinking labor force. The issue is particularly acute in the healthcare industry where the Job-to-Applicant ratio is 2-3 times depending on the specific role. This also comes at a time where the nation expects healthcare costs to accelerate due to the aging population creating urgency to find a more efficient way for medical institutions to work.

○ With this in mind there is also a favorable external environment as Japan is also going through a phase of digital transformation widely known as ‘DX’. As such, the healthcare industry is a prime candidate for further DX in order to help medical institutions operate more efficiently to prepare for the impending acceleration in healthcare service demand. We also see this as a government priority, which poses a tailwind for SRE. The government already provides subsidies to medical institutions to adopt more IT solutions. In 2024, the Ministry of Health, Labour and Welfare (MHLW) allocated ¥144.7bn to support the digital transformation of the medical and nursing care industry. This includes the adoption of systems to introduce the My Number Health cards and encouraging the widespread use of Electronic Healthcare Records.

○ SRE’s Consulting and Cloud solutions in this field therefore looks to meet a strong need providing significant value to the operations of the customer by allowing them to outsource non-core administrative workflow to SRE, which can manage it more efficiently through its cloud solutions and consultants. This way, medical professionals can focus more on specialized medical work to maximize healthcare service capacity.

3. Healthcare market has a significant greenfield opportunity

○ For example, there are 100,000 medical and welfare facilities in Japan. However, large facilities typically already have their own systems in place. Thus, SRE believes its main target customers are mainly small to medium sized facilities. The number of such facilities that can be approached is therefore estimated to be 80,000-90,000. Whilst the business does not break out its ARPC per industry within Life & Healthcare (LH), management indicates the ARPC is approx. ¥500,000 per month excluding customers in the financial field which tend to be large mega banks. We assume the ARPC in the healthcare field to be in line with this ARPC estimate. Thus we arrive at a potential TAM of ¥500-550bn for the healthcare field. From another perspective, consider that the Life & Healthcare (LH) segment currently has 297 contracts, only roughly 100 of this are healthcare customers compared to the 80,000-90,000 facilities it can potentially address. With their competitive offering with a combination of consulting and cloud products we think SRE can continue to take meaningful share. In addition, as SRE offers new solutions, this should enable it to take a larger portion of the market over the long term.

○ Furthermore, the company sees a potential to increase ARPC. Through its consulting service the company has identified 30 to 40 workflows that are non-core to medical professionals. SRE believes it can take over 80% of this. This involves a variety of tasks that are daily procedures but also monthly. This type of work does not involve medical procedures and is mainly administrative work. Examples of such workflows include HR, CRM, Regulatory Filing and Reporting. Given the shortage of labor in the medical industry, SRE believes there is an opportunity to instead deploy its own consultants and digital solution to streamline this work, enabling medical personnel to focus on medical tasks and therefore improve efficiency.

○ Additionally, the Life & Healthcare (LH) segment addresses other fields such as finance, IT and logistics. Whilst will not be the main focus for the business during the forecast period, such markets also have significant total addressable markets and thus there is a potential for such end markets to form as growth pillars for SRE in the future.

4. SRE's competitive advantages due to its unique business model

I. Strong relationship with customers from unique offering of Cloud + Consulting
II. Low Churn leading to recurring revenue streams
III. Unique Data Eco system
IV. Structural Cost advantage through affiliation to Sony Group

I. Strong relationship with customers from unique offering of Cloud + Consulting

○ We believe there are several differentiating factors involving SRE's unique AI Cloud & Consulting (AICC) business model which provides a combination of in-person consulting and cloud solutions.

○ Firstly, SRE has a strong involvement with customers' day-to-day operations through its consulting and BPO services as mentioned earlier. Companies in Japan are facing a labor shortage, and such help from consultants who can provide operational assistance effectively and efficiently can be highly convenient for short-staffed customers, whilst also creating a strong relationship and trust. Furthermore, there is a scale benefit as SRE's BPO staff are able to handle multiple customers concurrently and thus the productivity of healthcare professionals across multiple customers is maximized.

○ Secondly, due to SRE consultant's deep involvement with the customers operations, SRE is able to build an intimate understanding of the inefficiencies that need to be solved for a customer. Thus, its consulting and BPO allows SRE to identify and develop solutions which have a high likelihood of success and customer satisfaction. Such a strategy allows SRE to allocate development resources more effectively. We also believe this also contributes to low churn for SRE's AI Cloud & Consulting (AICC) segment.

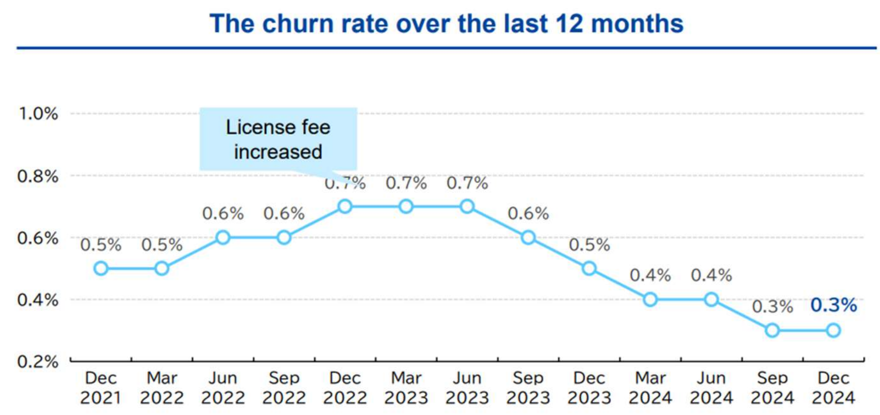
II. Low customer churn leading to recurring revenue streams

○ With the resulting high-quality offering through this combination of real-world services and cloud product, we believe SRE becomes indispensable to clients and is the reason for the low churn rate. This is currently at a monthly churn of 0.3% as of December 2024 for the overall AI Cloud & Consulting (AICC) business and have declined steadily over the last 24 months. We think the churn in the healthcare field is in line with this average.

〇 As SRE identifies more problems and digital solutions for a customer, its solutions and services become further entrenched to service a critical part of a company's operation. This would increase the reliance on SRE from a customer's perspective and therefore we think the churn will remain low.

〇 As a result of the recurring revenue business model, SRE is also able to allocate its resources more effectively given the predictability of growth compared to traditional real estate businesses, which are affected by market cycles.

Ex 2 : Monthly Churn Rate Trend



(Source: SRE)

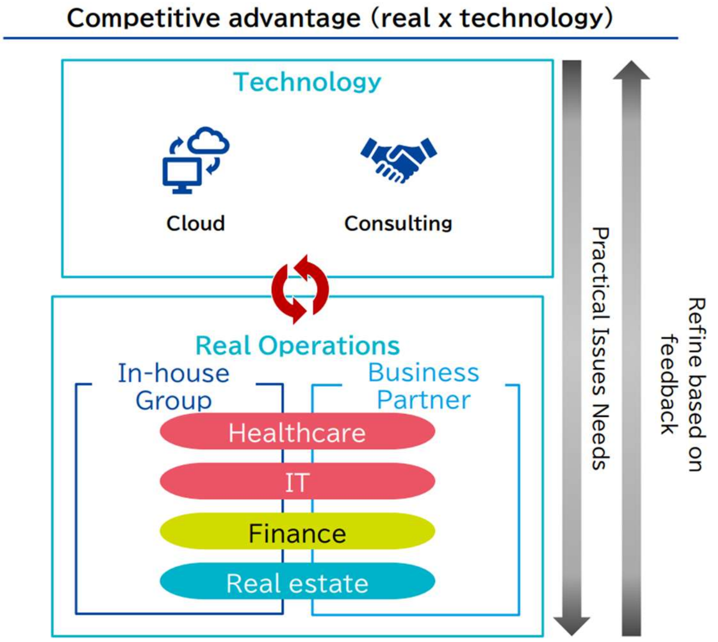
III. Unique Data Ecosystem

〇 SRE's strength is its ability to integrate knowhow and data from real-life examples into an AI solution. For example, it's experience in Real Estate has given it an advantage in the PropTech (PT) business, where it has been able to accumulate various data such as on property transaction, and gains insight on problems to be solved. As a result, the company can identify problems that can be solved in its own business through AI and subsequently develop, test and launch to external customers. Equally this strong technological capability developed is a differentiator in its Life & Property (L&P) business where the company can provide traditional real estate services enhanced using technology.

〇 We expect a similar development in the healthcare field. Whilst SRE did not have experience previously it has successfully gained experience through providing intimate consulting and BPO services to medical and welfare facilities. By the consultants inserting itself to the operational workflow of facilities, it is able to obtain valuable insights that can serve as a foundation for its cloud product development. Therefore, this has given SREs unique access to insights with which it can create value added solutions and helps differentiate its product and acts as a barrier to entry.

〇 Additionally, SRE forms alliances with other companies to co-develop solutions across various fields. Moreover, As the company wins more contracts, the company can collect more data which in turn allows the company to improve the quality of product and develop new solutions. This ultimately further enables more customer wins for SRE leading to more data, creating a flywheel effect through this data ecosystem.

Ex 3：AICC's Data Ecosystem



(Source: SRE)

IV. Structural Cost advantage through affiliation to Sony Group

○ Its close affiliation to Sony Group continues to be a major source of strength for SRE. The association of Sony's name gives SRE a strong credibility in the market and importantly it's R&D resources.

○ A key example would be Sony's offshore development team in India. The Sony India Software Center (SISC) is one of Sony's key development base housing close to 1500 high quality engineers and data scientists. The team has built extensive know-how working on globally competitive products for Sony, providing everything from development to testing capabilities. SRE can access the same resources to develop new AI cloud solutions. Importantly, this gives SRE a structural cost advantage as it can procure such services cheaper than a fully outsourced 3rd party provider. We think this should not be underestimated as SISC engineers cost 20% less than if SRE hired a local engineer while still being able to deliver high quality standards. Even when the price is benchmarked to a 3rd party provider, SRE is able to procure security testing such as vulnerability tests for instance, at 20% less than the market rate.

○ This also helps overcome growth bottlenecks as it makes it possible for SRE to focus on hiring consulting personnel, providing significant development flexibility. In other words, SRE can enjoy a focus on strategic development and handle more product development projects concurrently without being constrained by having to hire more personnel directly. Thus, this provides a strong foundation for growth without the challenge to spend aggressively on labor at the current scale.

○ As SISC has handled major development work for Sony products, the capabilities are best in class, ensuring a high standard for products delivered by SRE providing a competitive edge against competitors.

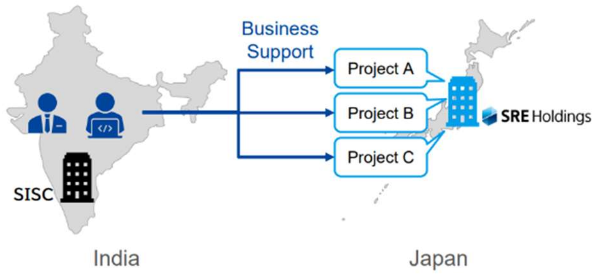
Ex 4：Collaboration with Sony's SISC

Through collaboration with the Sony India Software Centre (SISC), a software development base of the Sony Group, secured excellent engineers/data scientists in India

This time, have further strengthened the collaboration and form a PM specialist team within the Software Architecture Division (SARD) of SISC

By obtaining practical support from the upstream process, make it possible to expand the number of projects and scale that the company can handle, thereby strengthening the foundation for the sustainable growth of the AICC business

Reinforcement of Development Capability by Collaboration with SISC(Support for Development Operations)



(Source: SRE)

5. Additional growth potential through M&A

○ Whilst we believe that organic growth from the current healthcare business to be the core driver in the medium term and we do not model inorganic growth namely M&A in our forecast, we see further potential upside through M&A specifically for healthcare where it sees a pipeline of complementary solutions which SRE can integrate and strengthen its presence in the healthcare field.

○ The company has a dedicated team consisting of M&A professionals to source such opportunities and execute PMI (Post Merger Integration). Often times SRE is able to acquire these businesses among multiple bidders not due to price but as owners are looking to sell their business to a reliable, trusted acquirer with a long-term vision that can take care of the business. The M&A staff are also incentivized on specific KPIs. For example, achieving a 3-year profit target for the acquired company.

○ In terms of potential acquisition candidates, SRE is looking for companies in the healthcare field with complementary operational capabilities, valuable data or with an existing customer base for which it can provide an updated system and solution.

○ SRE's M&A will ensure responsible capital allocation by focusing on valuation. The company aims to pay anywhere between 5 to 10 times EV/EBITDA. If executed as planned such acquisitions should be value accretive to SRE as its own valuation will likely trade at a significant premium. Furthermore, through synergies with SREs business the implied valuation may in practice be lower than the headline acquisition price. While likely to be infrequent, SRE expects some use of debt to achieve this. However, the company intends to maintain an equity ratio above roughly 40% as a general rule and thus we think balance sheet risk is contained.

Recent Example of M&A

○ As an example, in March 2024 SRE acquired MEDIX which provides cloud-based medical treatment billing computers and support to orthopedic and acupuncture/moxibustion facilities. The company has a customer base of 2000 facilities.

Support services include billing task support.

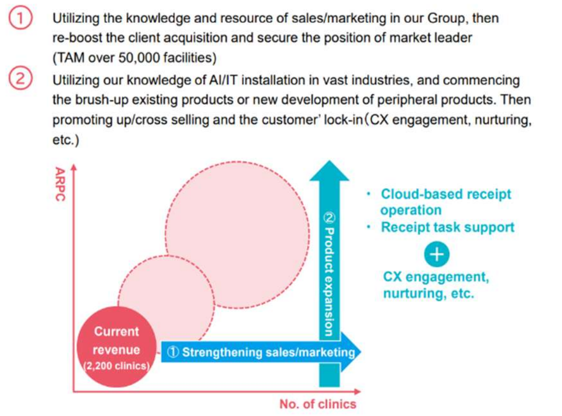
○ SRE sees an opportunity to combine its own AI and IT capabilities. This can create strong synergies as it brings MEDIX's knowledge of real-life problems among facilities clients and SRE's digital/technological capabilities. For example, it sees an opportunity to implement Predictive/Image analysis AI to existing products. Furthermore, SRE can leverage its sales and marketing resources to accelerate new customer acquisitions. The TAM remains large with SRE estimating over 50,000 facilities can be targeted compared to the current customer base of 2,000, a market share of 4%.

Ex 5 : Medix Financials

FY23 Revenue	¥1,255mn
FY23 Operating Profit	¥74mn
FY23 Net Income	¥50mn
Acquisition value	¥2,834mn
Enterprise Value	¥674mn
Net Assets	¥1,455mn

(Source: CGS, based on company data)

Ex 6 : Potential Synergies with MEDIX



(Source: SRE)

Ex 7 : Past Acquisitions

Company	Acquisition Period	Description	Enterprise Value
Medix	April 2024	Cloud medical billing solution, billing operation support	¥674mn
DORIRU(Formerly Gigsales)	March 2022	B2B Sales Support, Sales tech	¥485mn*
QCCS	April 2021	HR Solution, Sales Support system	¥131mn

*includes step acquisition

(Source: CGS, based on company data)

Equity Story ② OP to grow 32 %CAGR through FY27 and to reach ¥7bn*

Summary: SRE's main focus area of growth will be it's AI Cloud & Consulting Segment (AICC) a high margin, high recurring revenue business. Through the strong contribution of this AICC segment especially healthcare, we believe SRE is at an inflection point for its group profits to accelerate. Profit growth will remain high due to the high mix of AICC which represents 72% of group level operating profit. We expect revenue, operating profit, EBITDA and EPS to grow 13% CAGR, 32% CAGR, 28% CAGR and 34% CAGR respectively. We believe SRE's AICC segment in the medium term could achieve a revenue and operating profit growth of 35% CAGR and 39% CAGR respectively.

Note: The company has not disclosed medium-term management targets. At CGS, we have attempted to forecast performance through FY27 based on certain assumptions.

○ **Organic Growth assumptions in CGS Forecast:**

- **Contract growth in PropTech (PT) and Life & Healthcare (LH):** There were 4450 Contracts in PT and 297 Contracts in LH as of Q3 FY24. We estimate the number of contracts in each segment will reach 7000 and 1200 contracts through FY27 respectively.
- **ARPC growth in PT and LH**: ARPC was ¥67,000 and ¥615,000 as of year-end FY23 and we expect each to reach ¥67,000 and roughly ¥550,000 by FY27 respectively. In combination with the contract growth, we should thus expect an overall revenue CAGR of 35% through FY27 for the AI Cloud & Consulting (AICC) segment.
- **Operating Margin for AI Cloud & Consulting (AICC) and Life & Property (L&P)**: In AI Cloud & Consulting (AICC), we expect the PT business to increase margins to 45% while we also expect the margins of LH to improve as the recurring revenue cloud revenue expands. Furthermore, we see upside potential for the Life & Property (L&P) segment to expand margins as well due to the increasing contribution from the Asset Management business.
- **Growth of AUM for Asset Management in the Life & Property (L&P) segment:** Through FY27 we estimate the AUM for its Asset Management business to grow by ¥50b a year thus reaching a total AUM of ¥ 260bn.
- **Annual working capital increases and Debt levels to moderate:** As a result of the focus on the AI Cloud & Consulting (AICC) segment which requires de minimis working capital, we expect the overall working capital increase to slow significantly since we also expect the property development business in Life & Property (L&P) to only grow slightly through FY27. We also expect the amount of interest-bearing debt to grow only somewhat.

Ex 8 : SRE Mid-term Financial Forecast

¥mn	FY23	FY24E	FY25E	FY26E	FY27E	CAGR
Sales	24,219	28,147	30,928	34,758	40,132	**13%**
Operating Profit	**2,213**	**3,053**	**3,916**	**5,156**	**6,963**	**32%**
Operating Profit Margin	*9%*	*11%*	*13%*	*15%*	*17%*	
EBITDA	**2,587**	**3,650**	**4,524**	**5,808**	**7,690**	**28%**
EBITDA Margin	*11%*	*13%*	*15%*	*17%*	*19%*	
Net Profit	**1,389**	**1,981**	**2,643**	**3,505**	**4,762**	**34%**
Net Profit Margin	*6%*	*7%*	*9%*	*10%*	*12%*	
Diluted EPS	**85**	**121**	**162**	**214**	**291**	**34%**
BPS	750	817	832	991	1,109	11%
Net Working Capital	17,866	19,712	22,111	25,337	27,927	
Net Debt (Net Cash)	5,075	4,793	4,278	3,100	2,738	

（Source: CGS Estimates）

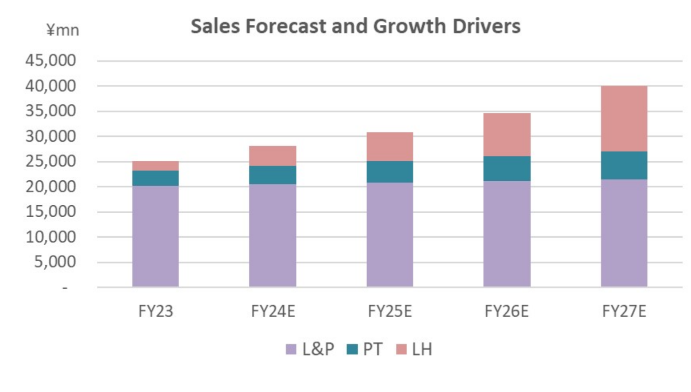
〇 **Simulated CGS Forecast Model Based on Assumptions Above:**

- **Revenue:** ¥40.1bn implying a 13% CAGR from FY24 through FY27
- **EBITDA:** ¥7.7bn implying a 28% CAGR from FY24 through FY27
- **Operating Profit:** ¥7.0bn implying a 32% CAGR from FY24 through FY27
- **Earnings Per Share (EPS):** ¥291 implying a 34% CAGR from FY24 through FY27

Main Growth Drivers

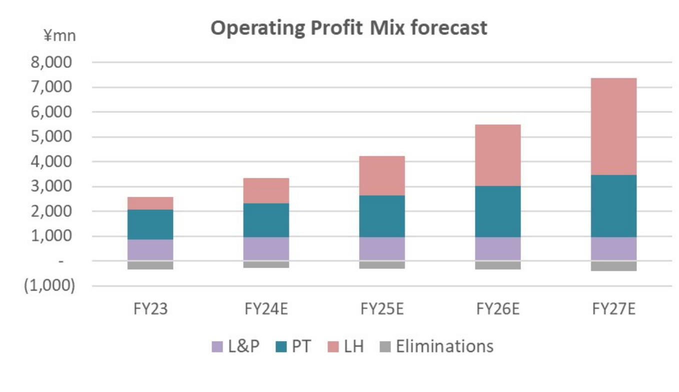
〇 In Equity Story ① we provided details on the qualitative aspects of the growth opportunity. In Equity Story ② we will discuss the quantitative aspects. For the AI Cloud & Consulting (AICC) segment the key growth drivers of revenue are i) Number of contracts and ii) ARPC (Average revenue per contract). ARPC is defined as the Revenue per client contract consisting of recurring software solution revenue and from consulting services provided to the client.

Ex 9：Sales Mix Forecast



(Source: CGS)

Ex 10：Operating Profit Mix Forecast



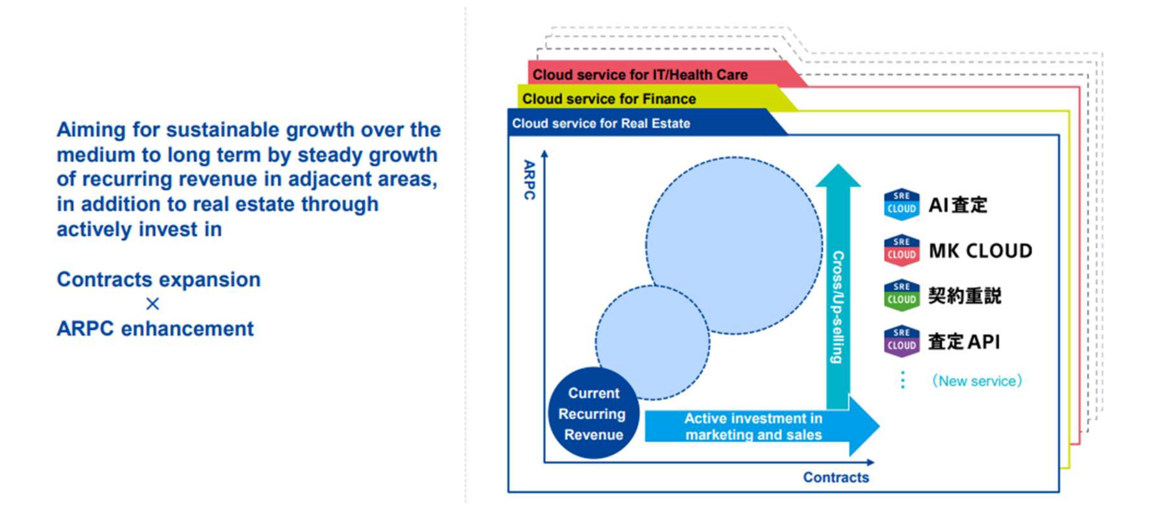
(Source: CGS)

〇 Overall we think there are 4 key growth strategies which SRE looks to pursue.

1) Customer acquisition with existing product suite
2) New Product launches driving cross-sell to existing customers and acquisition of new customers
3) SREs expansion into a new domain
4) M&A which can provide a new customer base and entrance into a new domain

〇 As we believe SRE's main growth will be organic, and M&A activities to be sporadic, we will focus on 1) - 3) for the purpose of this report and therefore will not assume any M&A. That said, the company is continuously assessing new M&A opportunities and may provide an upside surprise to our estimates.

Ex 11：Overview of growth strategy for AICC



(Source: Company Data)

○ We will now discuss the growth drivers of the two sub-segments namely its PropTech Solutions (PT) and Life & Healthcare solutions (LH).

Ex 12：KPI and estimates for AICC Segment

	FY23	FY24E	FY25E	FY26E	FY27E
PropTech					
ARPC	¥67,000	¥67,000	¥67,000	¥67,000	¥67,000
yoy%	-	*0%*	*0%*	*0%*	*0%*
No. of Contracts	3,861	4,600	5,400	6,200	7,000
yoy%	-	*19%*	*17%*	*15%*	*13%*
Life & Healthcare					
ARPC	¥615,000	¥598,000	¥581,000	¥564,000	¥550,000
yoy%	-	*-3%*	*-3%*	*-3%*	*-2%*
No. of Contracts	184	360	640	920	1,200
yoy%	-	*96%*	*78%*	*44%*	*30%*

(Source: CGS Estimates)

○ Life & Healthcare Solution (LH)

- **We expect number of contracts to grow at a 49% CAGR until FY27 reaching 1200 contracts**
- **Monthly ARPC to decline slightly to roughly ¥550,000 through FY27**
- **Margins should improve in the coming years as mix of cloud solution improves**

○ We expect a strong contribution from Life & Healthcare business (LH) particularly the healthcare field, where the company sees strong need to automate back office workflows. SRE is gaining strong interest from prospective customers and is expected to continue growing at a fast pace for the medium term. Notably the average contract size i.e. ARPC is significantly larger than in the PropTech (PT) solutions segment with the current ARPC per month at ¥649,000. This is due to the fact that the Life & Healthcare (LH) segment involves more consulting and BPO services as part of the contract whereas for the PropTech

(PT) Solutions, the service is more broadly cloud based. Furthermore, the absolute contract sizes per client are skewed larger due to the size of the clients in the financial field, which have been to megabanks. Excluding this, contract sizes are roughly ¥500,000 per month.

○ Consulting aspect is important for SRE to provide as this enables the company to identify practical ‘real world’ problems which it could solve and helps deepen industry expertise relatively quickly.

○ Whilst this would require more personnel versus its cloud products, this is still quite scalable. For example, this year, SRE hired around 10 new consultants with one of whom was a team lead. With this it was able to achieve strong growth YTD. Thus, based on our assumption we think consulting is a high value add service and thus poses a limited risk as a bottleneck. The management believes that one team lead can generate between ¥500mn - ¥600mn in operating profits.

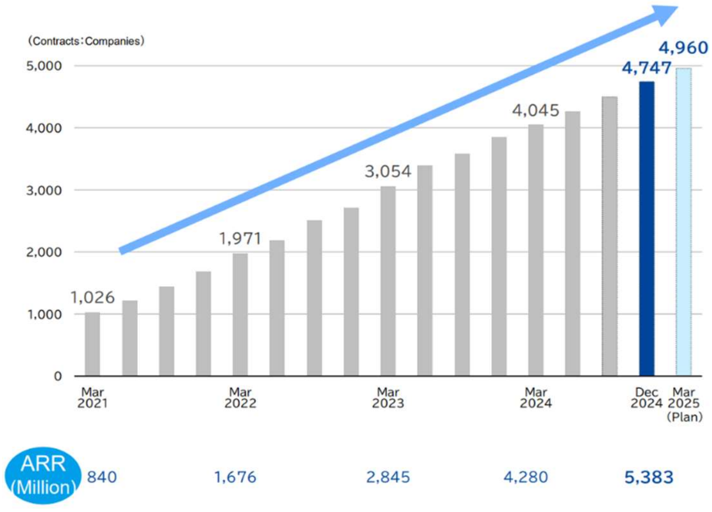
○ Overall we expect the ARPC (Average Revenue Per Contract) to moderate somewhat whilst the number of companies under contract to grow strongly. Therefore we believe customer growth will be the main growth driver for Life & Healthcare (LH). Currently ARPC for the Life & Healthcare (LH) segment is abnormally large due to reasons explained earlier, this should moderate as the company gains smaller clients.

○ However, we see an upside surprise potential for ARPC growth which SRE sees as an additional driver of long-term growth. This could be possible as SRE sees several opportunities. 1) Strong customer wins as it establishes its market presence 2) Cross-selling of additional consulting services and 3) Further up-sell of newly developed cloud solutions.

○ We further expect the operating margins for the AI Cloud & Consulting (AICC) segment to expand gradually due to the growth of Life & Healthcare (LH). Both the PropTech (PT) segment and the Life & Healthcare (LH) segment should be able to demonstrate this to a strong degree. We believe the AI Cloud & Consulting (AICC) segment’s operating margin can gradually expand from 32% to 35% through FY27. Whilst this is dependent on the mix of consulting services versus monthly license fees, over time the consulting fee base should decline in mix as the company continues to build a recurring revenue base from its AI cloud solutions.

○ SRE expects the composition of recurring revenue within the Life & Healthcare (LH) business to increase over time. For FY24 it targets a 40% composition versus 30% in FY23. We expect this to continue improving through FY27.

Ex 13 : Historical Contract and ARR Growth



(Source: SRE)

○ Another way to look at it is the growth in the recurring portion of AICCs overall business. SRE reports the Annualized Recurring Revenue (ARR) metric which has grown at a 65.3% CAGR from FY20 through Q2 FY24. We believe this could continue to grow faster than the overall AI Cloud & Consulting (AICC) business as the focus turns to developing and selling more AI enabled cloud solutions.

○ Given such recurring revenues mainly driven by its cloud solution license fees are higher margin than consulting services, we expect that an increased contribution from this should be margin accretive for the segment. For FY24 management expects to reach an ARR of ¥6.3-6.5bn.

○ We note that the company may be understating the true recurring nature of the AI Cloud & Consulting (AICC) segment. One point worth considering is that the consulting and BPO fees are categorized as a 'consumption fee' and therefore non-recurring. However, after the initial consulting project, customers are likely to use the same provider for future projects and the nature of many of its Business Process Outsourcing (BPO) services are also recurring. Such services can be a core part of a customer's operation and may be disruptive for customers to cancel it. Therefore, we believe that whilst this is not recurring in the sense of a monthly license fee, it is possible to categorize this as recurring in nature.

Impact of J-GAAP accounting

○ Due to the J-GAAP accounting, there will be a small negative impact on the margin from the acquisition of Medix which entails Goodwill Amortization Costs. The total goodwill was ¥1.47b with a straight-line amortization schedule over 13 years. Thus the annual amortization cost from this acquisition will be ¥113mn. However as this is a fixed cost as with most of the Life & Healthcare (LH) segment's other costs, we expect the margin to expand as revenues grow due to the inherent operating leverage potential.

PropTech Solution (PT)

- **We expect number of contracts to grow at a 15% CAGR until FY27 to 7000 contracts**
- **On a year end basis, monthly ARPC expected to remain flat at ¥ 67,000 through FY27**
- **Operating margin should expand to 45%**

○ For its PropTech Solution (PT), we believe SRE will enjoy a steady growth in customers whilst ARPC remains flat.

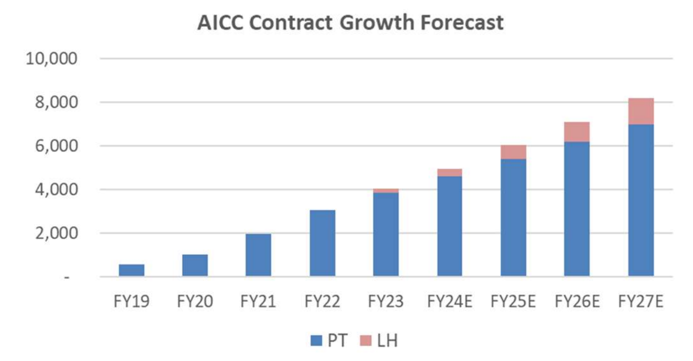
○ Through its own Real Estate business, SRE can identify the practical problems that can be solved through AI solutions. Furthermore, it is able to first test these solutions in its own subsidiary before launching to external customers. With this, it has been able to launch a suite of successful products over time with high adoption rates to help multiple aspects of the Real Estate Value chain. Examples include AI Home Valuation Cloud and AI Rent Valuation Cloud.

○ The company has 4450 contracts as of Q3 FY24 and we estimate the number of contracts can grow to 7000 contracts by FY27. We think this is possible due to SRE's notable presence in Real Estate through its Life & Property (L&P) segment providing a direct touchpoint to prospective clients.

○ The Q3 FY24 ARPC per month for this solution currently stands at ¥51,000 /month. However, there is a seasonality and ARPC is the highest in Q4. Therefore, at CGS we model estimates based on year-end figures which was ¥67,000/month last year. We believe this will remain constant through FY27 due to the growth contribution from AI Rent Valuation Cloud which has a lower ARPC.

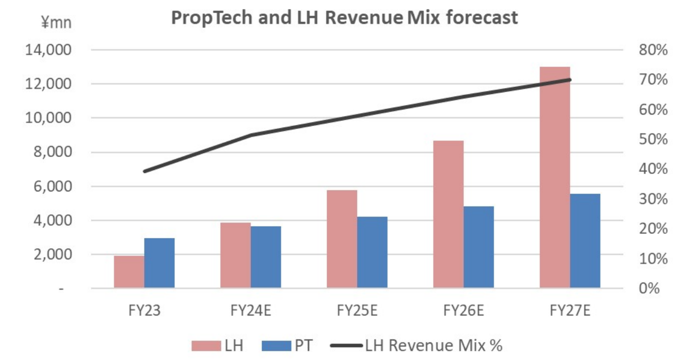
○ As of Q3 FY24, SRE has achieved a segment profit margin of 45.2% for PropTech (PT) with the expected margin to reach 38% for FY24. Whilst the contribution margin of the PropTech (PT) segment is already high we believe this margin is sustainable and could expand over the medium term as the revenue will mainly come from its cloud offering which requires less incremental labor costs. Thus, even as the company re-invests some of the profits into R&D, fixed costs as a % of total costs is high and should allow SRE to benefit from operating leverage.

Ex 14：AICC Contract Growth Forecast



(Source: CGS Estimates)

Ex 15：AICC Revenue Mix Forecast



(Source: CGS Estimates)

Life & Property (L&P) Segment

- **Property development business to remain flat growth through FY27**
- **Brokerage business to grow low single digit of ~3%**
- **Asset Management business to grow at a 33% CAGR between FY24 and FY27 driven by a ¥50bn annual increase in AUM.**

○ We believe the growth contribution from the Life & Property (L&P) segment to be limited in comparison to the AI Cloud & Consulting (AICC) segment. The expected key growth driver for this business segment will be its Asset Management Business, which is the main service of focus for this segment going forward due to the inherent recurring revenue business model with limited capital intensity. The key growth driver for this business will thus be the Assets Under Managment (AUM).

○ However, based on our estimates we believe that the revenue from Asset Management Business is still a small portion of segment revenues. Whilst the company does not disclose the revenue mix, based on current AUM and a stable estimated management fee of 0.5%, we think that the revenue from Asset Management is still roughly 2% of the segment. Given that property development revenues will stay flat, and we believe the brokerage business will only grow at low single digits going forward we expect a revenue growth of around 1% per annum for Life & Property (L&P) through FY27. Thus overall, we expect a small incremental growth in the medium-term for the time being.

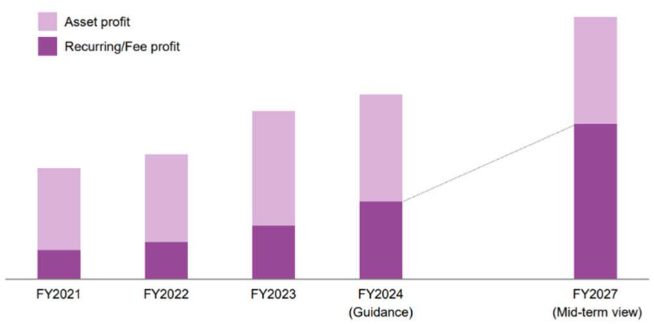
Ex 16：Life & Property Revenue Forecast by service

Life & Property Segment	FY23	FY24E	FY25E	FY26E	FY27E	CAGR
Brokerage + Development (¥mn)	19,846	19,945	20,045	20,145	20,246	**0.5%**
Asset Management (¥mn)	324	550	800	1,050	1,300	**33%**
AUM (¥bn)	65	110	160	210	260	**33%**
est. Asset Management Fee	0.50%	0.50%	0.50%	0.50%	0.50%	

(Source: CGS Estimates)

○ We note that there is upside potential to the growth in AUM. Managment comments indicate a strong pipeline and in particular through its affiliation with Sony Group, sees an opportunity to potentially for larger mandates based on some of the Real Estate owned. It sees an opportunity to grow AUM by ¥80b to ¥100b per year.

Ex 17：Life & Property Segment, Mid-term Profit mix projection



(Source: SRE)

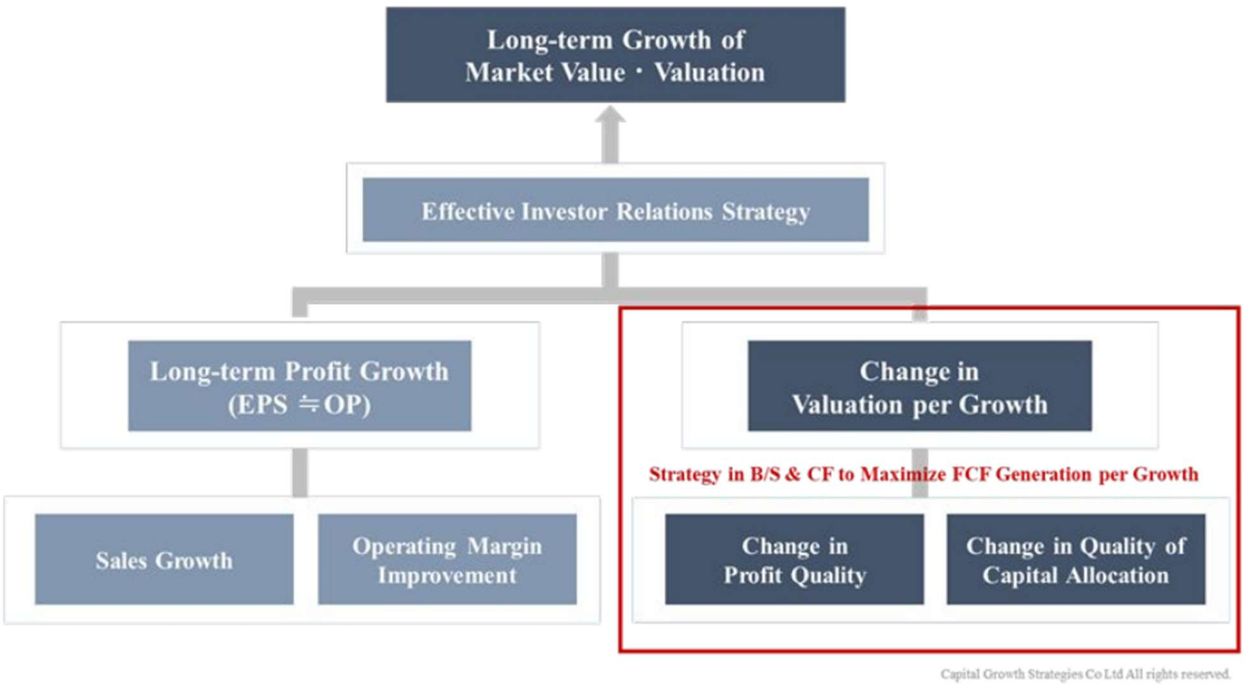
○ Nonetheless the Asset Management business is capital light unlike its property development business which requires significant upfront capital for each project, and capital commitments become increasingly large if SRE attempted to grow further. The Asset management business also requires less personnel. We therefore believe this business has a higher margin and expect slight margin expansion as this business scales. Overall, we forecast operating margins to reach 4.5% in FY27. The underlying Operating Profit Margin for this business is already 7 to 8% but due to overhead and R&D expenses, margins appear lower. We therefore believe our estimates are achievable for SRE in this context.

Equity Story ③ Through the transformation to a recurring, asset light business, this warrants a re-rating in multiples per 1% growth

Summary: The key drivers for valuation per 1% of profit growth is analyzed based on four indicators: capital efficiency, CF conversion, volatility of profit growth, and the quality of capital allocation. We believe that its stated intention to focus on growth via its AI Cloud & Consulting (AICC) business whilst their Life & Property (L&P) business remains more of a steady business should significantly improve the CF generation profile comparable to other SaaS companies. Given the increasing focus on cloud solutions going forward, we think the business should be more comparable to global companies with such business models that are valued at a higher Multiple per % growth. As such we see a significant re-rating potential for SRE as it executes its strategy.

○ So far, we've outlined SRE's growth story and our forecast. Now we turn to consider how investors might evaluate SRE's anticipated growth rate in terms of multiples over the long term. A critical point in this evaluation, as prioritized by CGS's leadership based on their extensive investment experience, is the multiple the stock market is willing to assign per 1% of profit growth rate. This perspective allows for a deeper understanding of how market expectations align with SRE's growth trajectory

Ex 18 : CGS's approach to Analyze Long-term Equity Valuation



(Source: CGS)

○ Even among companies with an expected long-term profit growth rate of 10% per year, some may be valued at an

EV/EBITDA multiple of 15x, while others may only achieve a multiple of 7x. This difference stems from the varying multiples that the stock market assigns per 1% of profit growth rate, and these multiples can change over time even for the same growth rate. Simply focusing on the anticipated profit growth rate when evaluating investments can obscure valuation logic when comparing historical or comps/benchmarks. CGS believes that this valuation per 1% of profit growth is a primary factor in understanding market valuations and is a crucial analysis point for long-term investors.

○ At CGS, we define the drivers of valuation per 1% profit growth rate as follows (Ex. 19). These drivers, in essence, represent the drivers of FCF generation per 1% of profit growth. In other words, even with an annual profit growth rate of 10%, companies with stronger FCF-generating abilities are granted higher multiples by the stock market. CGS uses this approach to analyze the fair multiples that the stock market may be willing to pay for each target company's long-term growth within the current interest rate environment. It should be noted that this analysis is based solely on CGS' independent perspective as long-term investors, without input or influence from the management of the companies analyzed on any of the valuation drivers or financial models.

Ex 19 : Company Medium-Term Plan image

Profit Quality:

① Capital Efficiency

② Cash Flow Conversion

③ Volatility of Profit Growth

Quality of Capital Allocation:

④ Change in Cash Usage & Change in Incremental ROI (Cash Flow Base)

(Source: CGS)

○ In the Life & Property (L&P) segment, management acknowledges that its property development business can create significant volatility to its cashflow and causes hesitance among investors. Going forward the company expects the business to remain relatively stable and thus inventories from this to remain more stable.

○ Furthermore, management instead sees an opportunity to transform the Life & Property (L&P) segment from a cyclical, capital intensive business to a more predictable, asset light business by focusing this segments growth on its Asset management operation. This is more of a recurring revenue generated through asset management fee and thus also requiring minimal capital. SRE sees a strong pipeline for this and expects it to be the main growth driver for the Life & Property (L&P) segment.

1. Capital Efficiency

○ We begin by examining capital efficiency, specifically ROIC. ROIC in particular, is crucial for CGS, as it reflects how much of the future operating CF will need to be reinvested into capital to generate expected profits. This allows us to gauge how much FCF can be retained, making it a key measure of FCF generation per profit growth. Typically, ROIC is calculated with NOPAT (net operating profit after tax) as the numerator. However, under Japanese accounting standards, SRE's NOPAT includes amortization costs for goodwill, which requires adjustment. Thus, CGS defines Cash NOPAT as the after-tax operating profit excluding goodwill amortization. Using this Cash NOPAT, we analyze SRE's Cash ROIC (ROIC adjusted for goodwill amortization).

〇 Taking a look at its historic ROIC for SRE, this has been volatile in the past due to the project-based nature of the Property Development business within Life & Property (L&P). As such developments are non-recurring in nature and revenue recognition timings are inconsistent, this periodically creates volatility in its working capital requirement and therefore its invested capital. We can see that the ROIC declined from 8% in FY21 to 5.9% in FY 21 and further to 5.6% in FY22. We note that this was due to the significant increase in inventories during that period related to property development. Inventories at group level rose from ¥ 2.7bn in FY19 to ¥ 15.8bn by FY21.

〇 Whilst this may look problematic, management determined it was necessary short-term investment to develop such properties as seed assets to launch its Asset Management Business, which it did in FY22. The management felt that without sufficient scale, it would be difficult to convince external investors to participate. The funds formed through this have limited balance sheet risk and is a more attractive business model.

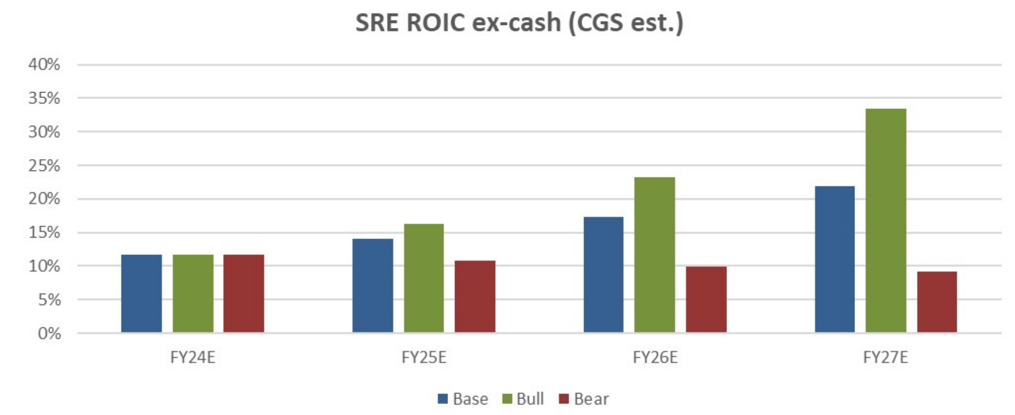
〇 From FY23 we can already see an early sign of ROIC improving. We see this as a result of working capital growth slowing. This can be attributed conversely to the deceleration in property related inventory. A shift away from this business means we expect invested capital growth to slow considerably. Thus, we expect the volatility of ROIC improve compared to the past. From a balance sheet perspective, we see debt levels moderating and now stabilizing from ¥11.6b in interest bearing debt in FY20 to ¥8.4b as of FY23 as a sign that AI Cloud & Consulting (AICC) is becoming the main priority for the company and is simultaneously generating cashflow to pay off this debt. AI Cloud & Consulting (AICC) profit contribution has steadily increased over this period. We see that Net Debt/EBITDA was at a peak of 3.4 times in FY22 and has shown steady improvement to 1.9 times in FY23 and on track to reach 1.4 times for FY24.

〇 Our base case assumes growth will come from the AI Cloud & Consulting (AICC) segment which is a high margin and asset light business. Furthermore, the Life & Property (L&P) segment expects to gradually move away from capital intensive development business to a less capital-intensive Asset Managment Business. However, we still expect modest growth from the development business therefore we expect debt levels to only grow slightly from its current balance of ¥8.4b. As we do not assume any M&A in our forecast, we believe the company will reach a net cash position of 0.4x Net Debt/EBITDA by FY27.

〇 With such growth we can expect the ROIC ex-cash of SRE to steadily improve as AI Cloud & Consulting (AICC) becomes a larger portion of SRE's total sales and profits. AI Cloud & Consulting (AICC) is a highly scalable business and main cost inputs are based on labor to provide consulting as well as development of AI cloud products. Thus, capital expenditure is not needed. We therefore think the theoretical ROIC of the AI Cloud & Consulting (AICC) business based on our Return on incremental invested capital analysis to be above 30%. Based on our base case projection we expect the ROIC ex-cash to steadily improve from 9% in FY23 to 22% by FY27.

〇 Breaking this down, we believe that whilst NOPAT can grow at a 32% through this period in our Base Case, we expect a growth in capital invested (ex-cash) to grow 7%, reflecting that significantly less capital will be required to achieve profit growth. We note that as our base assumption is that the development business will only grow moderately going forward and expect inventory levels to do the same. Thus, debt financing required will be also limited. Whilst M&A may require debt financing, given management comments that it looks to keep its Equity Ratio above 40%, we think any significant risk to the balance sheet is limited.

Ex 20 : ROIC ex-cash Forecast



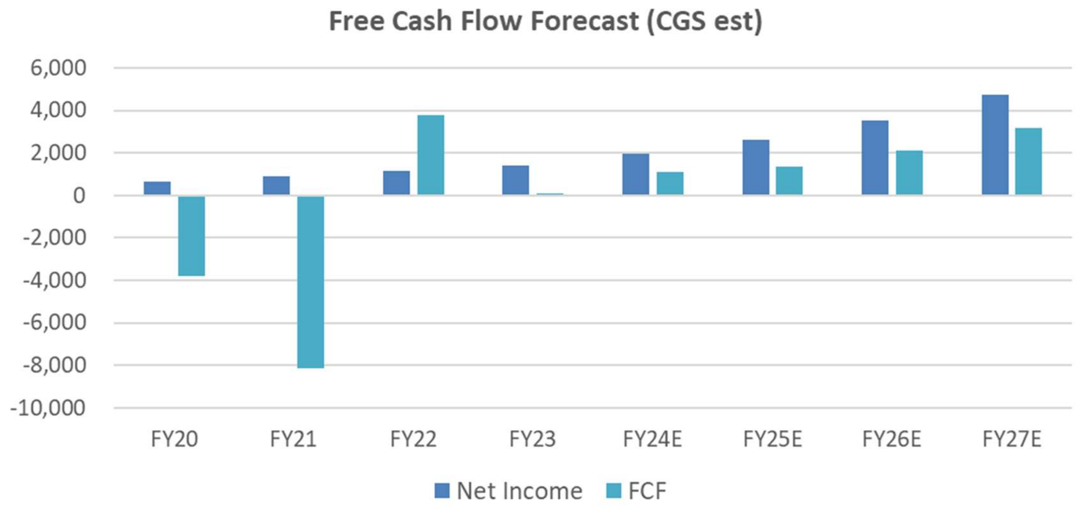
(Source: CGS Estimates)

2. Cash Flow Conversion

○ Profit on the income statement includes non-cash items such as depreciation and goodwill amortization, which means that it does not directly equate to cash flow. The cash flow conversion rate is an indicator of how effectively accounting profits on the income statement are converted into cash flow, and this measure is especially critical for long-term investors assessing FCF generation per profit growth. Specifically, we evaluate the conversion rate from EBITDA to operating CF (OCF/EBITDA conversion) and also the conversion rate from net income to FCF (FCF conversion). The primary driver of these metrics is the cash conversion cycle (CCC). For our analysis, CGS defines FCF as operating CF minus capital expenditures.

○ Firstly, analyzing the historical figures since its listing in 2018, we see that both FCF conversion and OCF/EBITDA conversion has been extremely volatile, with the average FCF and OCF/EBITDA conversion being negative during the period. As the company has seen steady and consistent growth in profits, we attribute this volatility in cashflow to the drastic changes in working capital year-over-year mainly caused by changes in inventory. The inventory in turn is impacted by the timings at which SRE takes on property development projects, which require significant upfront cash commitments. Such volatility could be a cause for concern for investors. In our base scenario however, we believe SRE's property development business will only grow modestly based on company comments and therefore expect both FCF and OCF/EBITDA conversion to improve due to the focus on the AI Cloud & Consulting (AICC) segment. This segment unlike the Life & Property (L&P) segment and specifically its property development business has limited working capital requirements. It may even have negative working capital as it is common practice for customers to pay its monthly licenses in advance. It is also not asset intensive given the major cost component for this business is labor. Furthermore, capex requirements for AI Cloud & Consulting (AICC) remain minimal due to its nature of business as a mostly digital service. Therefore, we think this will improve SRE's free cash flow generation. As a result, we expect an improvement in cash flow conversion metrics. We see a sustainable FCF and OCF/EBITDA conversion of 67% and 52% respectively, during our forecast period.

Ex 21 : FCF Conversion Forecast



(Source: CGS Estimates)

3. Volatility of Profit Growth

○ The next factor is earnings growth volatility. Even if a company doubles its operating profit over five years, the aggregate FCF in the same period varies significantly depending on whether the growth is achieved linearly or through volatility. This volatility in earnings growth directly affects capital costs due to less consistent CF generation per 1% of expected growth. Consequently, industries with cyclical earnings are generally valued at a discount compared to non-cyclical industries even on a similar expected long-term growth rate. Thus, for valuation, earnings growth volatility is one of the critical elements in analyzing FCF generation and assessing the sustainable equity multiple that investors are willing to pay per 1% growth.

○ In order to do this we assess the volatility in two factors. 1) revenue cyclicality and 2) profit margin volatility. Revenue cyclicality can be caused by the nature of the industry and exposure to certain market cycles, whilst profit margin cyclicality may be due to the nature of the business. For example, if the company requires substantial investments every several years this creates a volatility in profit margins.

○ Analyzing its past performance since listing in 2018, the company has demonstrated stable revenue and operating profit growth showing limited cyclicality. We see this as a pattern in both the Life & Property (L&P) segment as well as the AI Cloud & Consulting (AICC) segment. However, we note that the operating margin has declined since FY20, which was more than offset by strong revenue growth. Seeing that there has been a decline in gross margin, we attribute this to SRE's large investments required for land acquisition for property development projects. At the same time, we note that the company invested heavily in this period to accelerate growth of AI Cloud & Consulting (AICC), particularly ARR which the company deliberately chose to do to capitalize on the large opportunity. Such investments included R&D and hiring more sales personnel. This has been a worthwhile spend so far, as the company is seeing strong traction for its cloud products and strong sales growth.

○ Going forward we believe SRE can continue to demonstrate stable profit growth whilst improving its FCF profile since it will be focusing on expanding its recurring revenue. We believe group margins will start rising again due to AI Cloud &

Consulting (AICC) and the likely risk of profit growth volatility to reduce further. This is thanks to both the expanding Annual Recurring Revenue (ARR) within the AI Cloud & Consulting (AICC) segment as well as the growth of its Asset Management Business in the Life & Property (L&P) segment.

○ A high portion of recurring revenue and profits as a % of group should greatly reduce the volatility of profit and warrant a higher Multiple per 1% growth due to the consistency of cashflow generated as a result.

4. Change in Cash Usage & Change in incremental ROI

○ Finally, we will examine the quality of capital allocation. Here CGS focuses on how cash utilization evolves and how efficiently the CF could increase relative to the incremental invested capital (i.e. incremental ROI).

○ Taking a look at the historical cash usage, the company has been focused mostly on organic growth with some infrequent M&A activity. We note here that the cash spend on organic growth since FY19 has been focused on the property development business which consequently increased inventory levels for the company and resulted in a low incremental ROI. Looking back at the historical trend of ROI for SRE, we see that this has been inconsistent and largely dependent on the timings for its property development projects in Life & Property (L&P). Given the size of such development projects, we note that this was also financed through debt. Due to the capital constraints caused by this, the company has done an equity capital raise causing dilution to existing shareholders. This however was mainly to finance its AI Cloud & Consulting (AICC) business to scale it quickly which in turn has a substantially higher incremental ROI.

○ On a go forward basis, due to the focus on organic growth and unpredictability of SREs M&A activity, we assume that 100% of cash will go to organic growth investments and expect this to continue over the mid-term given the size of the opportunity in AI Cloud & Consulting (AICC). We believe our base case model will likely be conservative as there is considerable upside surprise potential from M&A, specifically in the healthcare field where management sees a strong pipeline of potential M&A opportunities. Furthermore, we expect the allocation of its investments will be increasingly towards its AI Cloud & Consulting (AICC) segment given that in the Life & Property (L&P) segment SRE will be focusing more on Asset management and therefore leading to less capital requirements.

○ From an investor's perspective, the key consideration is the incremental return generated by these future investments. To assess this, we analyze how the company’s incremental ROI on CF-base has evolved from the past and how it may change going forward.

○ In CGS’s forecast, invested capital is expected to grow modestly from FY24 through FY27 at a CAGR of 7%. On the other hand, we expect NOPAT to grow at a faster rate at a CAGR of 32% during the same period. This thus implies a high return on incremental invested capital which we estimate to be above 40%. We believe this is possible as SRE continues to scale its more capital light AI Cloud & Consulting (AICC) segment and away from Life & Property (L&P).

○ What could potentially add to the volatility of this ROIC is if SRE decides to take on one-off undertakings of a larger property development project in the Life & Property (L&P) segment, which could then increase inventories i.e. require more capital investments and dilute ROIC temporarily. However, as the AI Cloud & Consulting (AICC) segment is already more than 70% of group profits, we expect the risk of this to decline as this segment continues to scale.

Ex 22 : Mid-term Change in Key Drivers of valuation per growth table

	SRE (Current)	3 Year Forecast	Base Case	Bull Case	Bear Case
ROIC ex-cash	9%		28%	38%	13%
FCF Conversion	5%		67%	79%	26%
Profit Growth Volatility	Mid		Low	Low	High
Incremental ROI *	5 %**		43%	63%	-2%

*Incremental ROI:
NOPAT Growth / Invested Capital Growth
**Historic Median Incremental ROI

Improving or Strong | No Change or Neutral | Deteriorating or Weak

(Source: CGS)

○ Here we will examine what the potential multiple investors will be willing to pay for based on what SREs business could transform into over the medium term. Namely, by transforming from a real estate services company to a fast-growing AI SaaS platform we think the valuation merited for such a business will change. We attempt to do this by identifying and comparing with global peers with similar business models both for the AI Cloud & Consulting (AICC) and Life & Property (L&P) segments.

○ SRE's business model with a combination of Real Estate, Consulting and Cloud solutions is unique both globally and domestically, thus, we compare the business model to several types. For this we have selected both domestic and global businesses which we believe SRE could resemble as AI Cloud & Consulting (AICC) becomes it's main contributor. Therefore, rather than focusing on property development companies we put an emphasis on scalable software and technology companies, especially those with similar end market exposure. Thus, for AI Cloud & Consulting (AICC) peers we focus on the real estate industry and the healthcare industry which is becoming the main driver of growth. For the Life & Property (L&P) segment we look to find businesses that provide recurring property management services. The common traits among these categories are that it has a recurring revenue model and are also asset light in nature.

○ As such we have chosen Appfolio for its Real Estate focused SaaS solutions, VeeVa for life science SaaS, First Service for its property management business, Doximity for healthcare cloud solutions and M3 as a domestic Healthcare Technology business. Notably these businesses are related to one type of service SRE may offer but does not overlap across multiple business lines. By comparing against multiple types of businesses, we can assess the different ways in which investors may look at SRE and the appropriate market multiple they may apply.

Ex 23 : Comparison of SRE with selected global peers

	SRE (Base Case)	Veeva	Doximity	Appfolio	FirstService	M3
Market Cap ($bn)	$311mn As of Mar. 2025	$37.9bn	$12.1bn	$7.6bn	$7.4bn	$7.9bn
EV/EBITDA	14x As of Mar. 2025	25x	34x	28x	16x	13x
EBITDA CAGR (3Y forward)	~28% (CGS 3Y est.)	~14%	~11%	~20%	~8%	~8%
EV/EBITDA Multiple per 1% of EBITDA Growth	0.5x As of Mar. 2025	1.8x	3.1x	1.4x	2.1x	1.6x
ROIC ex-cash	~22% (CGS 3Y est.)	~56%	~85%	~9%	~9%	~23%
FCF Conversion	~67% (CGS 3Y est.)	~168%	~125%	~71%**	~187%	~109%
Profit Growth Volatility	Mid	Mid	Low	High	Low	High
Incremental ROI * (CF Base)	~41% (CGS 3Y est.)	~110%	~71%***	~37%	~9%	~24%

*Incremental ROI: OCF Growth / Invested Capital Growth
**based on a 5-year average due to volatility
***Based on L3Y due o availability of data, others use L5Y
Note: Peer's Forecast is based on Bloomberg Consensus.

Stronger than SRE | Comparable with SRE | Weaker than SRE

(Source: CGS)

○ For the peers selected, we note that the investments and use of cash is mainly towards organic growth for the cloud peers similar to what we expect for SRE whilst FirstService and M3 have made more frequent opportunistic acquisitions. Ex 23 summarizes the valuation of peers compared to SRE based on EV/EBITDA per 1% growth model.

○ We have not included GA Technologies, a domestic Property Technology company in the comparison. Although we see similarities in the potential exposure of end markets within PropTech (PT) as well as it's FCF Conversion, when considering what SRE's business can become, we believe that the margin, cash ROIC profile and high profit volatility of GA Technologies is not illustrative of what we believe SRE can achieve over the medium-term. In addition, it has a more M&A driven growth strategy compared to SRE.

○ As can be seen, the comparative companies have lower expected earnings growth for the next 3 years compared to SRE, which we believe to be in an earlier stage of growth given the relatively smaller revenue size versus the total addressable market.

○ Due to the uniqueness of SRE's business we think it is prudent to take multiple perspectives to determine our view on SRE's valuation. Here we consider the valuation from 3 different standpoints.

1. Compared to Cloud Solution peers overall, some discount to SRE's EV/EBITDA per % of profit growth will likely persist as the company would not have transformed completely to a recurring revenue business over the forecast period. However, SRE's FCF generation will improve significantly and become more comparable to the others by FY27. We

also note that the scale of SRE is smaller, and it is worth keeping in mind the issue of lower liquidity that can be a reason for a discount in valuation. Taking a long-term perspective however, we think the peers are indicative of the re-rating potential should the FCF generation and incremental ROI continue to improve driven by a higher contribution from AI Cloud & Consulting (AICC). The improvement in FCF generation through FY27 could act as a catalyst and nonetheless narrow the gap versus such peers as the business models start to increase in similarity. With SRE's EV/EBITDA per % growth at 0.5x we believe it is significantly undervalued.

2. If we look at FirstService in isolation to think about the Life & Property (L&P) business, EV/EBITDA per % profit growth is high even compared to the other peers despite lower expected EBITDA growth and ROIC ex-cash. We think this is because the FCF conversion is higher than the SaaS companies and due to the low profit volatility. This is a positive indication that the potential valuation the Life & Property (L&P) segment would warrant should be higher due to the increase in recurring revenue through the expansion of the asset management business. Therefore, we also believe that over the long term a discount to peers is unlikely to persist due to the Life & Property (L&P) segment as the reason assuming it continues to expand the Asset Managment business.

3. Finally, we compare SRE to the domestic healthcare technology company M3. We see similarities due to the end market exposure as well as its domestic focus. It is a more mature company with a lower growth profile but higher margin than SRE, we note that the EV/EBITDA multiple is lower compared to SRE. However, we note that the EV/EBITDA per % profit growth is higher despite the lower expected growth than SRE at 1.6x. Given the higher growth and improving FCF generation profile expected in our base case, we think this should trade at least closer to a similar multiple. Implying a –69% undervaluation in this case.

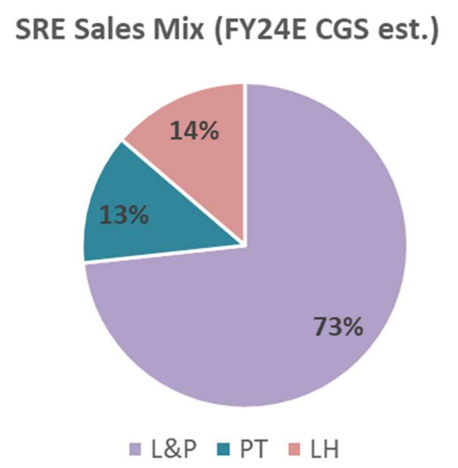
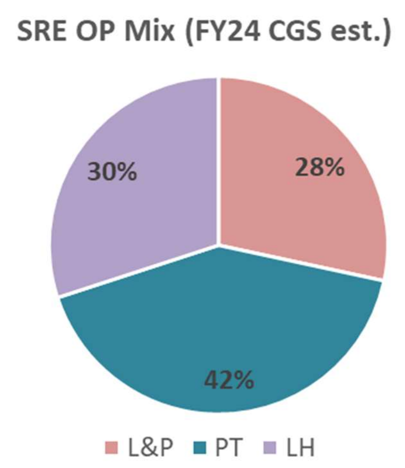
○ Overall, having compared SRE to multiple types of businesses related to its different segments, we believe that SRE is significantly undervalued based on EV/EBITDA as % of profit growth from all aspects. The focus on strong profit growth through its high margin AI Cloud & Consulting (AICC) business, we believe this could act as a catalyst to narrow the valuation gap between such peers.

Company Overview and Business model

○ The business was originally founded under Sony as Sony Real Estate in 2014 as a real estate tech company with the aim to provide traditional Real Estate services and leveraging technology to enhance it. It developed its first Real Estate Valuation Engine in 2015 using AI for in-house use. Since, they have used their capabilities to develop new solutions leveraging the power of AI and started commercializing the solutions as a SaaS product from 2018. The company listed on the mothers exchange in December 2019 and later re-listed to the TSE 1st Section in December 2020 and is now listed on the prime market.

○ Sony Group continues to own 21% of the business (after stock offering in March 2025). There is currently no board representation from Sony Group. However, SRE continues to have a commercial relationship with Sony, which provides SRE with the resources necessary to scale efficiently.

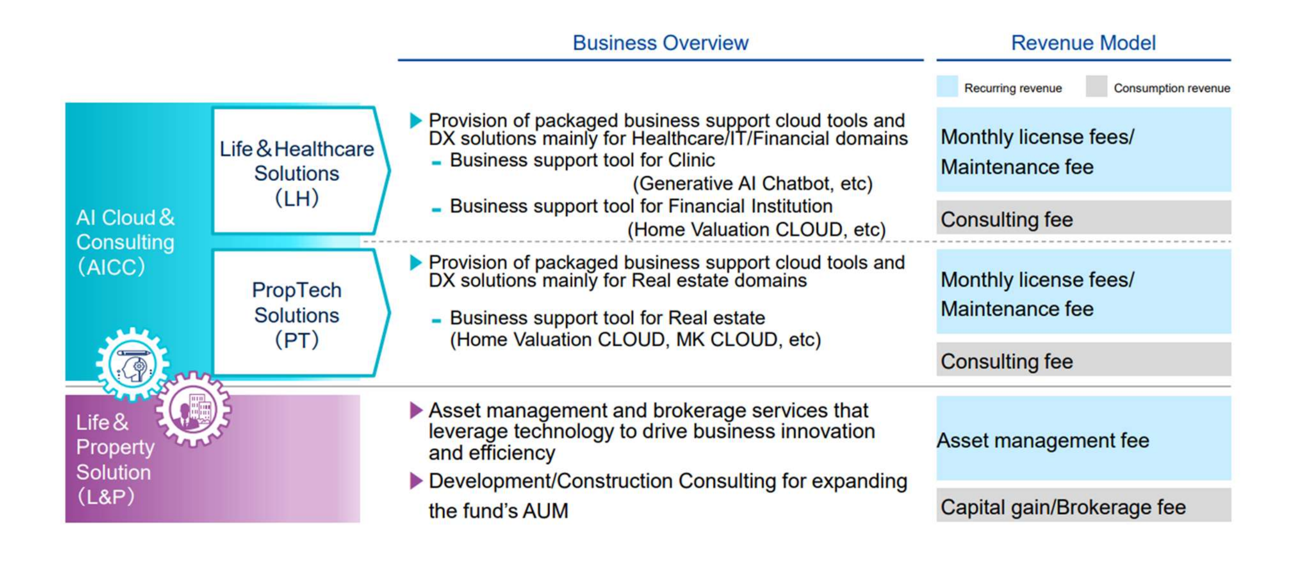
○ From the IPO in FY18 through FY23 SRE has grown its revenues at a 50.4% CAGR and Operating Profit at 38.6% CAGR, owing to their fast growth in the AI Cloud & Consulting (AICC) business which we find impressive.

Ex 24：SRE Sales Mix	**Ex 25：SRE Operating Profit Mix**
 (Source: CGS)	 (Source: CGS)

Business Model

○ SRE's business model can be broadly broken down into two segments which are AI Cloud & consulting (AICC) and Life & Property (L&P). The two have distinct business models which are discussed below:

Ex 26 : Overview of SRE's business models



(Source: SRE)

AI Cloud & Consulting (AICC)

○ Their newer segment which focuses on providing AI solutions across various verticals. Originally focused on their core property market SRE is now expanding to other verticals such as healthcare and finance. This segment provides clients with a combination of consulting services which may involve Business Process Outsourcing (BPO) type services in combination with their AI Cloud solutions. The segment can be split into two further subsegments which are namely, PropTech Solution (PT) and Life & Healthcare Solution (LH).

Ex 27 : AI Cloud Platform Product Lineup

Product lineup for Life&Healthcare Solution		Product lineup for PropTech Solution	
Generative AI chatbot for Healthcare domain	Always supports attentive customer service with natural dialogue, and enables nurturing such as encouraging follow-up examination/re-visit	SRE Home Valuation CLOUD	AI assesses real estate by using actual transaction data and auto-generates appraisal reports with higher accuracy than expert. Also, reducing working time from 180 to 5 minutes
Digital Marketing Solution	A digital marketing solution that supports new patient acquisition, branding for clinics, and strengthening customer management	SRE Marketing CLOUD	A one-stop digital marketing service with AI appraisal and nurturing features
Management Support Tool for Clinic	A cloud tool that supports the efficiency/ streamlining of clinic management and tedious back-office tasks.	SRE Contract Creation CLOUD	Contracts/documents creation tool that reduces working time by 60%, in addition to lowers omission risk by referencing history and templates
Sales Tech Tool	Enables target company analysis/list extraction and KPI visualization/analysis for inside sales.	SRE Appraisal API CLOUD	Companies can integrate their systems/websites with our real estate valuation engine via API to utilize high-precision AI appraisals
Home Valuation CLOUD for Financial Industries	A tool that adapts SRE Home Valuation CLOUD for financial institutions and enhances/optimizes real estate collateral valuation and other processes	AI Chatbot Integrated with an Appraisal System	A generative AI chatbot capable of handling specialized contents, and the first in the real estate industry to incorporate the appraisal function

(Source: SRE)

Life & Healthcare Solution (LH)

○ The company provides packaged business support cloud tools in addition to consultancy services focused on other fields. This currently includes healthcare, finance and IT field. SRE prefers to take a portfolio approach by entering multiple fields in order to avoid disruption and obsolescence risk in a similar philosophy to Sony. Revenues involve a combination of recurring revenues coming from maintenance and monthly subscription fees and flow-type revenue coming from consulting fees.

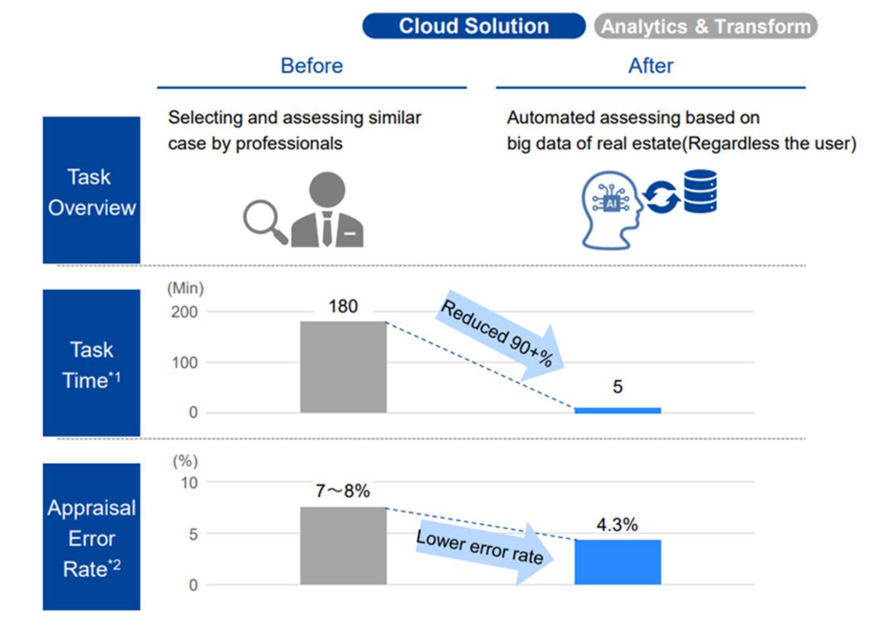
PropTech Solution (PT)

○ The company provides packaged business support cloud tools in addition to consultancy services focused on Real Estate. Revenues involve a combination of recurring revenues coming from maintenance and monthly subscription fees and flow-type revenue coming from consulting fees.

○ Currently, this business has 4450 customers constituting a large majority of the AI Cloud & Consulting (AICC) customer base.

○ An example of a PropTech solution is its SRE Home Valuation cloud. This is an AI solution which, using a large dataset of historical transactions can create an accurate and highly automated real estate appraisal report. Historically this involved a manual assessment by professionals. With the solution professionals are now able to reduce their time spent on each appraisal by more than 90% whilst also reducing error rate significantly from 7-8% to 4.3%, creating practical value for the customer.

Ex 28 : Example of an AICC solution in PropTech (PT)



(Source: SRE)

Life & Property (L&P)

○ The segment consists of SREs Real Estate Intermediary business, Asset management business and a property development business. The key aim for SRE here is to leverage technology in traditional real estate services. This includes things such as Internet of Things (IoT), ESG compliance and AI solutions.

A) ‘Smart Property’ Development Business

○ This business provides traditional property development services with further added value of SRE’s digital solution. Here SREs earnings comes from capital gains.

B) Brokerage Business

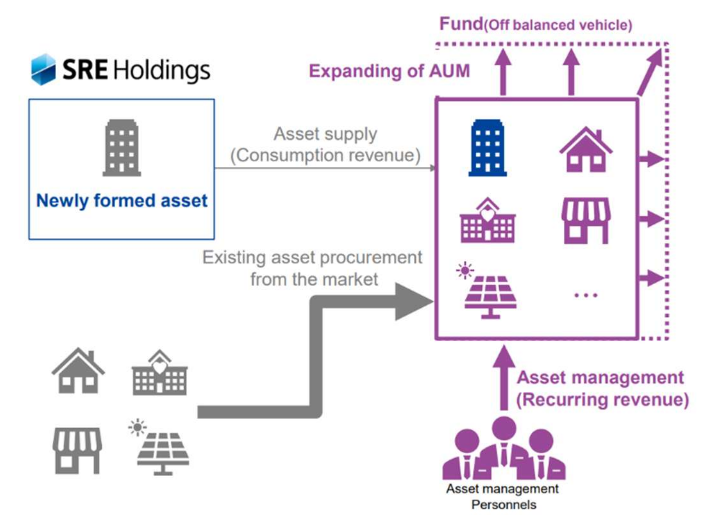
○ Brokerage involves the intermediation and consulting of purchase and sale of real estate assets. Brokers fees are roughly 3%.

C) Asset management Business

○ Involves the management of real estate assets through a fund structure. Properties type can vary widely from housing, office, shopping centers etc. Revenue model business is through a recurring management based on a percentage of AUM which his in-line with industry rates below <1%. There can be some potential one-off revenues through asset disposal or acquisitions from time to time.

○ Revenues for this business is earned through a mix of asset management fee which is recurring as well as from capital gains and brokerage fee which are more transactional and one-off.

Ex 29 : Asset Management Business Overview



(Source: SRE)

Shareholder Return Policy

○ SRE plans to begin paying dividends to shareholders in March 2025, implying a yield of 0.5%. Management believes that the company is still in the early stages of growth and that the best use of capital is reinvestment, particularly in AI Cloud & Consulting (AICC), which is an area with structural tailwinds and high profit margins. The Company believes that reinvestment of funds for business growth is the best option to maximize long-term shareholder value. We agree with this policy and believe it is a rational decision. On the other hand, Life & Property Solutions (L&P) is now at a stage where it can generate stable earnings compared to the previous development model due to increased stock earnings from the expansion of the asset management business, and the company believes that it is now in a position to continue returning profits from this division through dividends. Therefore, the company believes that the commencement of dividend payments indicates its commitment to continue focusing on the recurring revenue business in the Life & Property Solutions (L&P) segment. More specifically the company will look to pay out 35% of the net profits generated by the Life & Property (L&P) segment as dividends.

○ The company has conducted a share buyback worth ¥500mn in April 2024. Management looks to conduct share buybacks opportunistically. In this instance this has been mainly to offset share dilution caused by share based compensation (SBC). We think this buyback was accretive to shareholders given the undervaluation of the company currently.

○ Overall, the company will intend to focus its capital allocation efforts on re-investing in organic growth and M&A where it sees ample opportunity and is the optimal choice for maximizing long-term shareholder returns. The AI Cloud & Consulting (AICC) segment as a standalone likely will be able to generate more than 30% ROIC per year given the scalability and operating leverage inherent in the business model. Thus, as the sales composition of AI Cloud & Consulting (AICC) grows larger we should see continued expansion of ROIC.

Total Addressable Market (TAM)

○ SRE’s TAM can be large for its core AI Cloud & Consulting (AICC) segment, as end market applications can be broad.

○ In Japan, there is still a significant white space for companies of all sizes to achieve Digital Transformation, known as ‘DX’. Across almost all industries, companies are facing efficiency constraints due to the labor shortage caused by the declining population in Japan. Thus, automating various operations through the use of AI proposes an effective solution to a nationwide problem. SRE’s AI Cloud & Consulting (AICC) business can identify the pain points of an industry and develop an effective AI solution that can help companies achieve significant productivity improvements.

○ In AI Cloud & Consulting (AICC) there are many areas in which SRE sees an opportunity to develop scalable AI solutions to help streamline their customer operations:

- PropTech: sees a TAM of ¥1.2 trillion.
- Healthcare and IT/Others: identified a TAM of ¥3 trillion.
- FinTech a TAM of ¥3.9 trillion.

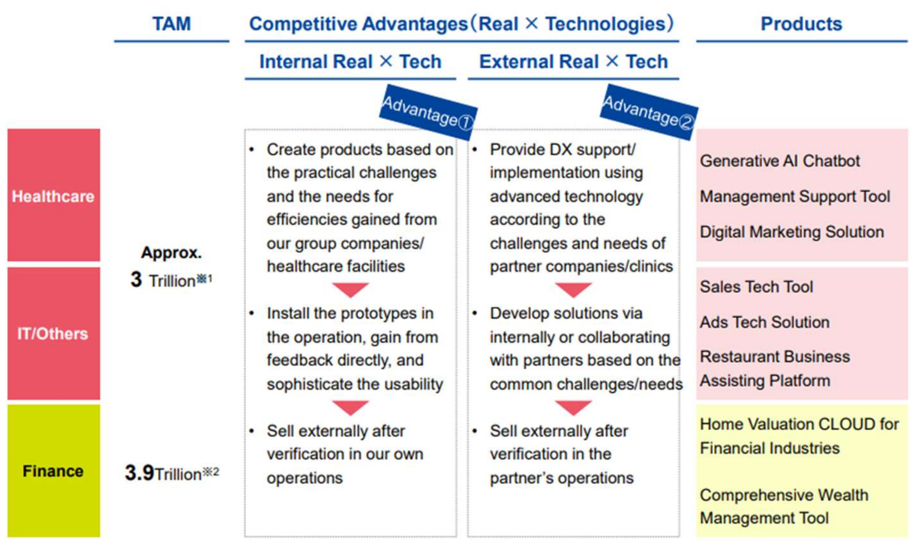
○ SRE sees an opportunity to expand into other potential fields by initially providing AI consulting services to customers and consequently helping them develop an AI SaaS solution that is tailored for the related field.

Life & Healthcare (LH)

○ Whilst SREs focus areas has been in healthcare which we estimated to be a TAM of ¥500-550bn earlier, management sees an opportunity to expand into other industries. The company is already undertaking projects for clients in other areas such finance, IT, retail and manufacturing. This could potentially translate into a larger opportunity for SRE to acquire consulting clients to which it can develop AI solutions for new applications. Moreover, the company is also open to expand into new fields through partnerships with other external companies. An example of this would be its partnership with Kasumigaseki Capital to develop the COLD X NETWORK an on-demand platform for frozen storage space throughout Japan.

○ Similarly, the TAM for finance business is estimated to be ¥3.9 trillion. The application for DX can be broad in the financial industry and a clear white space remains. SRE already serves Mega bank clients and expects to acquire regional banks as customers as well.

Ex 30 : Life & Healthcare (LH) TAM Overview



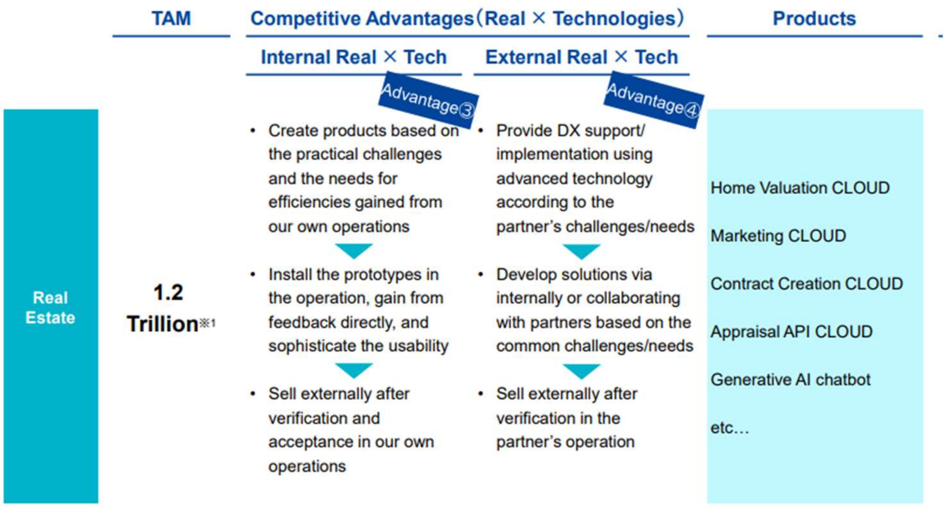
(Source: SRE)

PropTech (PT)

○ The Real Estate Tech TAM is estimated to be worth ¥1.2 trillion. The TAM is large and is dependent on SREs ability to acquire new customers and develop new solutions. That being said, many workflows still involve manual labor as well as paper, it is clear that there is significant room in the real estate industry to employ more automated, digital solutions such as those provided by SRE.

○ To get to a more tangible figure of the size of opportunity, we can illustrate an example through discussing the opportunity for SREs AI Rent Valuation CLOUD. This solution provides real estate rental fee valuation reports using an AI engine to estimate the values. Previously its PropTech (PT) business was aimed at the 130,000 Real Estate brokers in Japan. Through the development of new products such as AI Rent Valuation CLOUD, SRE can now expand its potential target customers to other rent management related businesses of which there are approximately 90,000. Considering that there are 4450 customers in SRE's PropTech (PT) segment as of Q3 FY24, we see a significant greenfield opportunity for SRE to pursue.

Ex 31 : PropTech (PT) TAM overview

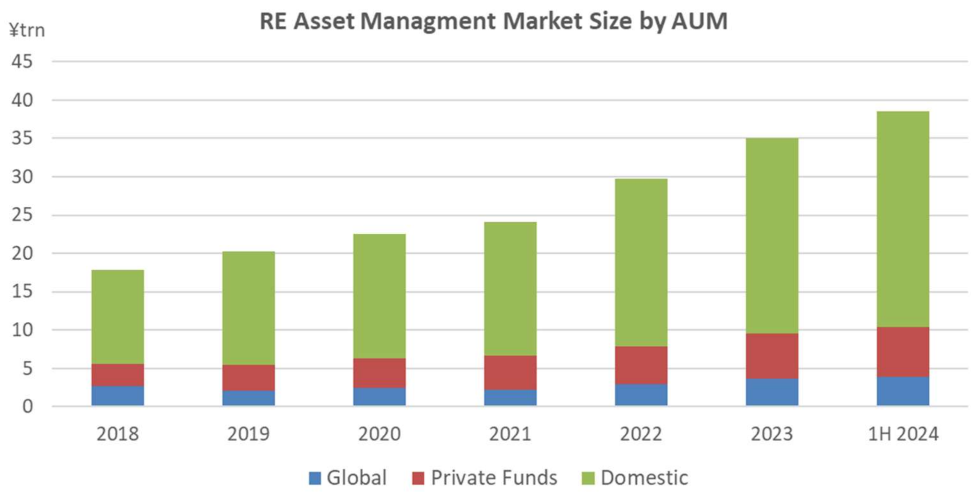


（Source: SRE）

Life & Property Business

○ Across the 3 business lines, opportunity for SRE's business lines remain vast. Here we focus on the main growth driver going forward which is its Asset Management Business in the Life & Property (L&P) Segment. For this the market size for Private Real Estate funds based on Asset Under Management (AUM) is estimated to be worth ¥38.6 trillion according to the Sumitomo Mitsui Trust Research Institute and ARES. The market has seen a strong growth since 2019 with the market growing at a 15% CAGR.

Ex 32 : Asset management TAM and market growth by AUM



（Source: CGS based on ARES and Sumitomo Mitsui Trust Research Institute Report）

Risk Factors

○ **Downturn in the Real Estate Market:** SRE is currently focusing on transforming its Life & Property (L&P) segment to a more predictable, recurring revenue model. However, there is a portion of the business that will remain as ‘flow type’ transactional revenues namely their brokerage and property development operations. Thus, in the event of an economic downturn, this can negatively affect the overall earnings of the company.

○ **Post Merger Integration (PMI) is more costly than initially expected:** Whilst we do not assume further M&A in our base case, through its M&A opportunity, there is a possibility that the company may incur higher than expected PMI costs, which therefore negatively impact value creation and ROIC. This may also be the case with the recent acquisition of Medix. However, we think the risk of this is minimized as management is focused on the price paid for each acquisition, typically ranging between 5 to 10 times PER.

○ **Product Obsolescence:** Artificial Intelligence and technology are a fast changing, dynamic market which could make certain AI Cloud & Consulting (AICC) solutions less relevant for SRE. The risk is mitigated here due to their close relationships with clients to whom it also provides consulting/BPO type services. Furthermore SREs ‘portfolio approach’ i.e. diversifying product range and end market should help mitigate such risks.

○ **Sony Relationship:** SRE has a close relationship to parent company Sony which provides valuable resources that enables SRE to scale efficiently, providing the company an advantage against competitors. However, should this relationship change, or Sony decides to sell its ownership completely, this could negatively impact the stock. We find it unlikely and given Sony still owns 21% of SRE (after March 2025), we believe the companies’ interest are aligned.

○ **Interest Rate Environment:** The Real Estate market has a high reliance on debt capital markets. In the coming years, this may impact SRE’s business from a demand perspective if interest rates continue to rise.

Interview with the CEO

Summary:

○ SRE Holdings is a life-tech company that provides solutions using AI and DX while being involved in real business. Although it started in the real estate sector, the healthcare sector is now the growth driver. This impact is significant. They believe that by creating a success formula in this field, they can expand to various industries and overseas in the medium to long term.

○ The current TAM (Total Addressable Market) for healthcare solutions is large, with 100,000 cases. They envision the number of contracts to be 5 to 8 times higher in about five years. ARPU (Average Revenue Per User) is also expected to rise due to the larger scale of target facilities. The service, which integrates cloud services, consulting services, and BPO (Business Process Outsourcing), is highly profitable and has a structure that makes it difficult to cancel. The profitability of BPO can be increased through the use of AI and overseas resources.

○ Capital allocation is recognized as an important issue. Although real estate inventory temporarily increased as seed assets for the establishment of a real estate fund, the proportion of capital invested in real estate inventory will decrease in the future, improving CF (Cash Flow) and increasing ROIC (Return on Invested Capital). Regarding M&A, they have been able to execute at low valuations. They are targeting owner companies that seek to improve productivity and introduce technologies such as AI through SRE's support, rather than focusing on price.

CGS: Today, we have the pleasure of welcoming Mr. Nishiyama, President and CEO of SRE Holdings. We have arranged this interview to incorporate the management's firsthand insights into our report, addressing topics that are likely to be of high interest to long-term investors considering their investment options.

Photo of Mgmt. Meeting: From right, Nishiyama (President & CEO, SRE Holdings) and Nobuzane (CEO, CGS)

CGS: First, I would like to ask about your overall strategy. Since your company's listing in 2020, you have achieved high growth centered on cloud services for the real estate sector, such as AI-based real estate price assessments. However, for the past two years, you have focused on Life & Healthcare solutions, particularly cloud services and BPO services in the healthcare sector, as a new axis of your growth strategy. You have also conducted M&A in this field. This strategic shift is significant. Could you explain the background of this change? Why did you choose the healthcare sector, and how did you identify opportunities for success in this field?

Nishiyama, SRE: SRE Holdings has never aimed to focus solely on real estate tech from the beginning. Our concept has always been to "create a social impact," "improve society and the world," "pursue advanced initiatives," and "make today's efforts the norm in ten years." Our first venture was in real estate tech. The real estate market is vast and has significant social impact. However, it was an industry that lagged in digitalization and AI adoption. Recognizing this potential, we developed products that are easy to use in practical settings, while valuing real business and understanding the actual operations. This approach allowed us to create solutions that are well-received in the field.

At the same time, by including nursing homes and hospitals in our real estate funds, we have also been involved in the healthcare sector. With the acceleration of the aging population, we recognized the growing need not only for disease treatment but also for extending healthy life expectancy and preventive healthcare. On the other hand, the number of doctors and nurses providing services is decreasing, while the number of elderly patients is increasing. This supply-demand gap is widening every year, making it essential to use DX and AI to increase productivity in this industry, just as in real estate.

We have experience in engaging with real-world operations in real estate and have connections with Sony Life and Sony Lifecare within the Sony Group. Our desire to align our ability to provide solid solutions based on field observations with the rising latent needs led us to enter the healthcare sector. This vision has resonated with many talented individuals who have joined our company. As we expand our capabilities, our output is also increasing.

This sector has significant growth potential and can be expanded globally. By extending our focus beyond real estate and finance to healthcare and eventually to various other industries, we believe we can thrive as a life-tech company. Developing a success formula in the healthcare sector is crucial for this ambition. It will also elevate the caliber of talent we can attract and enhance our external perception.

CGS: I would like to ask about your growth strategy in the healthcare sector. Dividing revenue into quantity and unit price, let's start with quantity. It is said that there are about 100,000 medical and welfare facilities in Japan, and your target for the number of contracts in the healthcare sector this fiscal year is 360. Considering the TAM of approximately 100,000, the upside potential is significant. On the other hand, your business includes BPO services, which require manpower. Recruitment can be a driver, but it can also be a constraint if not managed well. Could you discuss how you plan to grow your healthcare business, including BPO services, in the future?

Nishiyama, SRE: We believe that sustainable growth is extremely important. Regarding your concern about potential constraints due to a shortage of personnel, we have a long-term strategy in place. Those involved in the healthcare sector are not necessarily individuals who have worked in the healthcare industry for many years; we also have talent who originally worked in strategic consulting or IT consulting. Additionally, with the rapid development of generative AI, we anticipate that simple tasks such as document creation will be significantly streamlined over the next two to three years.

By combining the following elements, we are not worried about the risk of human resource constraints for the business volume we envision over the next five to ten years: Talent from the healthcare industry, talent acquired from other industries and their development, utilization of generative AI, and collaboration with external experts such as freelancers.

CGS: Could you tell us how many contracts in the healthcare sector you expect to achieve in the next three to five years? Additionally, how do you plan to recruit and manage the performance of the necessary personnel and teams to achieve this growth?

Nishiyama, SRE: Regarding our quantity targets, we envision scaling up to approximately five to eight times our current size in about five years. To secure the necessary capabilities, let me elaborate on our approach. We are not only hiring highly specialized professionals in the medical field but also recruiting talent from other industries, such as consultants and DX-related personnel. We are implementing a training program of about six months to enable them to excel in our company.

Additionally, with the remarkable advancements in generative AI, we anticipate that simple administrative tasks and document creation will be largely automated in the next two to three years. As a company that specializes in introducing AI to clients, we aim to enhance our own productivity by integrating generative AI into our operations.

When introducing complex technologies like AI to client companies or medical settings, the recipients need a certain level of capability. However, by consolidating work and personnel on our side as a BPO provider and incorporating AI to streamline operations, the hurdles are relatively lower since it is within our own operations. We believe that instead of proposing AI solutions to clients for their use, the trend will shift towards us taking over operations and using AI internally to achieve efficiency.

CGS: Next, I would like to ask about unit price. Regarding the average unit price (ARPU) in the healthcare sector, I believe there are two components: (1) digital cloud-based recurring revenue centered on AI chatbots, and (2) revenue from BPO services that require manpower. Could you share your thoughts on the future trends of ARPU created by the sum of these two components?

Nishiyama, SRE: This fiscal year, ARPU appears to be on a slight downward trend from the beginning to the end of the year. The Life & Healthcare Solutions sub-segment includes not only healthcare but also high-ARPU services provided to financial institutions such as megabanks. Therefore, the initial figures were somewhat higher. As the proportion of the healthcare sector has gradually increased during the year, ARPU has decreased towards the end of the fiscal year due to the mix. However, from next fiscal year onwards, we do not expect ARPU to decline further, as we anticipate contributions from the larger scale of target facilities in the healthcare sector.

Our strength lies in our comprehensive offering, which includes not only cloud solutions but also consulting and BPO services, enabling us to manage real business operations. While providing only cloud services might seem purer, medical professionals prefer to focus on diagnosis and treatment. They appreciate a company that can provide end-to-end solutions rather than dealing with various cloud, consulting, and BPO vendors separately. By firmly offering these three services, we have established high profitability and high ARPU.

Additionally, there is the advantage of being less prone to cancellations. When providing only cloud services, as seen in the real estate industry, cancellations are more common. By offering consulting, BPO services, and handling miscellaneous tasks, we create a structure that makes it difficult for customers to cancel. Since we take on the actual operations, it not only reduces the likelihood of cancellations but also allows us to increase unit prices. This strategy is not only applicable to the healthcare industry but also to other industries we plan to expand into in the future, making it a very important strategy.

CGS: If ARPU in the healthcare sector recovers steadily from next fiscal year onwards, one straightforward scenario might be the introduction of new cloud services. What growth drivers do you envision in this context?

Nishiyama, SRE: There are several ways to achieve this. Of course, we will continue to develop new services, which will allow us to purely use technology to increase ARPU. Additionally, by building a track record, we believe we can also achieve larger-scale facilities, which will help increase ARPU.

Unlike the real estate industry, where we have contracts with thousands of companies, we have only been able to provide services to a few hundred companies in the healthcare industry. We have often been asked by clients about our track record. As we accumulate more achievements in healthcare facilities, we are receiving more positive evaluations, with clients recognizing the quality of our services. As a result, we are gradually being approached by larger facilities.

Currently, many of the facilities we serve are relatively small medical and welfare facilities, but we see opportunities to shift towards larger medical and welfare facilities and large hospitals. Although it may be a long-term goal, we are also considering global expansion.

CGS: Regarding the profitability of the healthcare sector, AI chatbot-based cloud services have a very high contribution margin, making it easier to link revenue growth with high profitability. On the other hand, BPO services incur costs, making efficiency a crucial factor. Could you share your thoughts on the profitability of the healthcare sector and the efficiency of BPO services?

Nishiyama, SRE: Our cloud services, consulting services, and BPO are integrated, and the high added value of the first two services results in very high current profit margins. The LTV (Lifetime Value) in the healthcare sector is exceptionally high within the company. We believe that the current gross profit margin is more than sufficient.

Regarding the future handling of human resources, as previously mentioned, we do not see growth or profitability risks due to the utilization of AI and overseas resources. Reducing simple administrative tasks through generative AI is one of our strengths. Additionally, the shortage of personnel performing administrative tasks in medical settings is less severe compared to doctors and AI engineers. With AI addressing language barriers to some extent, overseas personnel can also contribute. Considering that we already outsource work to an offshore center in India for engineering, we believe that utilizing overseas resources for BPO services is also feasible.

CGS: Next, I would like to ask about capital allocation, specifically how you plan to distribute operating cash flow to enhance corporate value and how this will affect capital efficiency. At our company, we believe that capital allocation has a significant impact on corporate value, particularly stock valuation. We analyze this based on the premise that the resulting changes in ROIC (Return on Invested Capital) will be a major driver of stock valuation.

Looking at your company's ROIC, it maintained a very high level of around 15% at the time of your IPO in 2020. Subsequently, due to the expansion of working capital, particularly the increase in inventory for Life & Property Solutions (L&P) involving real estate asset management and brokerage, invested capital quadrupled, and ROIC decreased to the mid-single digits. Over the past year or two, you have been accumulating profits without expanding invested capital, and ROIC has been on an improving trend.

Could you share your thoughts on how you plan to manage invested capital, particularly working capital, and how you expect ROIC to change in the future?

Nishiyama, SRE: This is a very important issue and one that institutional investors are paying close attention to. Since our IPO, we have aimed to grow as a life-tech company that provides tech solutions in various fields, including finance and healthcare, while maintaining real estate as one of our segments. Therefore, we initially wanted to avoid holding too much real estate inventory. However, we recognized that off-balance sheet real estate funds would be a crucial strategy if we continued to be involved in real estate.

When forming a real estate fund, it is essential to have a certain amount of seed real estate within the fund to attract investors. Small funds of 100 million or 200 million yen are not attractive to investors, so scale is necessary. We created private real estate funds for off-balance sheet purposes and needed to stockpile a certain amount of real estate as seed assets for these funds. This process led to an increase in inventory and a temporary decline in ROIC.

Let me explain why cash flow and ROIC have improved over the past one to two years. Two years ago, we started our real estate fund and have been gradually transferring real estate inventory into it. We have shifted from a business model focused on real estate development to one where we manage real estate funds and earn management fees as our main revenue source. As a result, our inventory and cash flow have been moving towards a cleaner state.

Our investment strategy has transitioned to using cash for investments in tech solutions and supporting M&A activities. We want investors to understand this progression. We needed to create real estate funds because we did not want to hold real estate inventory. To establish these funds, we had to accumulate seed assets for a certain period. Now that this period has passed, we can reduce our real estate inventory.

In response to your question, the proportion of capital invested in real estate inventory will decrease, cash flow will improve, and ROIC will continue to rise.

CGS: Lastly, I would like to ask about your M&A strategy, which is one way to utilize operating cash flow. To expand in the healthcare sector, you acquired Medix last March, a company that provides cloud and BPO services for clinics such as chiropractic offices. Assuming you will continue to explore acquisitions in the healthcare sector, there is a concern that SaaS businesses, being high-growth and high-capital efficiency industries, tend to have high valuations. How do you maintain valuation discipline to avoid the risk of deteriorating capital efficiency due to overpriced acquisitions?

Nishiyama, SRE: Since we do not follow US accounting standards, goodwill amortization is recorded as an expense on the P&L. Our role is to improve various metrics such as ROIC, and we need funds for M&A, so we are very strict about valuations during acquisitions. While we do not disclose specific investment criteria, we aim for valuations that are not too high, and preferably low.

When a good company is up for sale, there are often 7-8 potential buyers. We only pursue acquisitions if we can be the first or second lowest bidder. We do not chase prices. When we ask the selling companies why they are considering selling, they often say, "We are a traditional company with many clients and have developed some cloud services. However, we want to take on challenges such as introducing generative AI and creating advanced products, but we cannot hire AI engineers or highly skilled technology personnel on our own. We want the acquiring company to help us introduce technology and improve productivity to provide greater value to our existing clients." We are well-suited to these types of owners. Since they do not choose buyers based on price, we can acquire these companies even if our offer is the lowest.

Conversely, we do not target companies that are already highly digitalized, have high profit margins, and want to exit at very high valuations. Our approach of valuing real-world operations and introducing highly practical AI technology allows us to achieve such M&A. We believe this is a very rational method economically, and we intend to continue using this approach for future M&A.

CGS: Thank you very much. We have discussed key points from the perspective of long-term investors. Lastly, if you have any message for investors as the management team, please feel free to share it.

Nishiyama, SRE: Recently, when speaking with both domestic and international investors, I have often heard comments like, "I thought SRE Holdings was primarily focused on real estate, but I am surprised to see how extensively you are involved in AI-related businesses." This has sometimes led to immediate investment decisions in our stock. This is not necessarily a good thing, as it indicates that our IR and company explanations are still insufficient. I hope this interview serves as a good opportunity to address this.

We want to share our vision with stakeholders: "By being involved in real estate, finance, and healthcare businesses, we aim to identify the real challenges and implement DX for ourselves or others, becoming a tech solution company that can make an impact in the face of aging populations and the advent of generative AI-driven work style reforms." We refer to ourselves as a life-tech company. Our current focus is on the healthcare sector, which serves as a touchstone for our efforts. We believe we can build a solid foundation this fiscal year and the next. Progress has been very smooth, and we hope investors will continue to watch our evolution into a life-tech company and support our long-term growth.

Financial Model

JPY mn	FY21	FY22	FY23	FY24E	FY25E	FY26E	FY27E	FY27E Base Case	Bull Case	Bear Case
Income Statement										
Sales	13,573	18,542	24,219	28,147	30,928	34,758	40,132	40,132	43,983	26,323
COGS	9,403	12,764	16,759	18,478	19,206	20,351	22,072	22,072	21,991	18,426
Gross Profit	4,170	5,778	7,460	9,669	11,722	14,408	18,059	18,059	21,991	7,897
SG&A	2,778	4,092	5,248	6,616	7,807	9,252	11,096	11,096	11,454	5,000
Operating Profit	1,392	1,686	2,213	3,053	3,916	5,156	6,963	6,963	10,538	2,897
Pretax Profit	1,247	1,619	2,057	2,922	3,776	5,006	6,803	6,803	10,378	2,736
Income Tax	354	450	604	877	1,133	1,502	2,041	2,041	3,113	821
Minority Interest	0	21	65	65	0	0	0	0	0	0
Net Income	892	1,148	1,389	1,981	2,643	3,505	4,762	4,762	7,264	1,916
EBIT	1,392	1,686	2,213	3,053	3,916	5,156	6,963	6,963	10,538	2,897
D&A	272	318	374	597	608	652	727	727	426	770
EBITDA	1,664	2,004	2,587	3,650	4,524	5,808	7,690	7,690	10,963	3,667
Diluted Shares Outstanding	16	16	16.4	16.4	16.4	16.4	16.4	16.4	16.4	16.4
GAAP EPS (Diluted)	56	71	85	121	162	214	291	291	444	117
DPS	0	0	0	14	14	14	14	14	18	7
COGS/Sales	69.3%	68.8%	69.2%	65.6%	62.1%	58.5%	55.0%	55.0%	50.0%	70.0%
Gross Margin	30.7%	31.2%	30.8%	34.4%	37.9%	41.5%	45.0%	45.0%	50.0%	30.0%
Other SG&A/Sales	20.5%	22.1%	21.7%	23.5%	25.2%	26.6%	27.6%	27.6%	26.0%	19.0%
OPM	10.3%	9.1%	9.1%	10.8%	12.7%	14.8%	17.4%	17.4%	24.0%	11.0%
EBITDA Margin	12.3%	10.8%	10.7%	13.0%	14.6%	16.7%	19.2%	19.2%	24.9%	13.9%
Cash Flow Statement										
Net Income	892	1,148	1,389	1,981	2,643	3,505	4,762	4,762	7,264	1,916
D&A	272	318	374	597	608	652	727	727	426	770
Changes in Working Capital	-8,469	2,981	-1,604	-981	-1,255	-1,367	-1,495	-1,495	-1,539	-1,402
OCF	-7,306	4,360	453	1,597	1,996	2,789	3,994	3,994	6,151	1,284
CAPEX	-850	-579	-379	-500	-619	-695	-803	-803	-440	-790
FCF	-8,156	3,781	74	1,097	1,378	2,094	3,192	3,192	5,711	494
Acquisitions	-556	317	61	0	0	0	0	0	0	0
Cash Dividends Paid	0	0	0	-232	-234	-235	-237	-237	-294	-110
FCF III (OCF - ICF -Div)	-8,944	3,933	76	865	1,144	1,859	2,954	2,954	5,417	384
Share Issuance (Repurchase)	888	76	-170	0	0	0	0	0	0	0
Issuance (Reduction) of Debt - Net	8,420	-3,216	-298	0	0	0	0	0	0	0
Net Change in Cash	362	808	-478	865	1,144	1,859	2,954	2,954	5,417	384
Conversion										
OCF/EBITDA	-439.1%	217.6%	17.5%	43.8%	44.1%	48.0%	51.9%	51.9%	56.1%	35.0%
FCF/NI	-913.9%	329.3%	5.3%	55.4%	52.1%	59.7%	67.0%	67.0%	78.6%	25.8%
Balance Sheet										
Cash & Cash Equivalents, ST Inv	2,999	3,838	3,360	4,225	5,369	7,227	8,323	8,323	11,311	5,137
Accounts Receivable	411	635	1,002	694	763	857	990	990	1,085	649
Inventories	15,814	12,201	13,940	15,055	16,259	17,560	18,965	18,965	18,965	18,965
Total Current Assets	20,264	18,611	20,607	22,280	24,697	27,950	30,583	30,583	33,667	27,056
Net PP&E	615	686	694	597	608	652	727	727	426	770
LT Investments	250	280	289	289	289	289	289	289	289	289
Intangible/Goodwill	786	1,440	1,535	1,535	1,535	1,535	1,535	0	1,535	1,535
Total LT Assets	2,755	3,345	3,410	3,313	1,789	1,832	1,908	1,908	1,606	1,951
Total Assets	23,019	21,956	24,017	25,593	26,485	29,783	32,491	32,491	35,273	29,007
ST Debt & Curr. Portion LT Debt	3,797	4,282	1,148	1,148	1,148	1,148	1,148	1,148	1,148	1,148
Accounts Payable	119	94	629	456	474	502	544	544	542	454
Other Current Liabilities	1,225	1,587	2,112	2,112	2,112	2,112	2,112	2,112	2,112	2,112
Total Current Liabilities	5,141	5,963	3,889	3,716	3,734	3,762	3,805	3,805	3,803	3,715
LT Debt	7,844	4,391	7,286	7,869	8,499	9,179	9,913	9,913	9,913	9,913
Total LT Liabilities	8,079	4,677	7,667	8,250	8,880	9,560	10,294	10,294	10,294	10,294
Total Liabilities	13,221	10,640	11,557	11,966	12,614	13,322	14,099	14,099	14,097	14,009
Total Equity	9,798	11,316	12,460	13,627	13,871	16,461	18,393	18,393	21,176	14,999
Total Liabilities & Shareholder's Equity	23,019	21,956	24,017	25,593	26,485	29,783	32,491	32,491	35,273	29,007
CCC										
Days of Sales Outstanding (DSO)	8	10.3	12	9	9	9	9	9	9	9
Days of Inventory Outstanding (DIO)	448	400.6	285	280	280	280	280	280	250	300
Days of Payables Outstanding (DPO)	3	3.1	8	9	9	9	9	9	9	9
Cash Conversion Cycle (Days)	452	407.8	289	280	280	280	280	280	250	300
	0	0								
ROE	10.1%	11.0%	12%	15%	20%	24%	28%	28%	38%	13%
ROIC	5.9%	5.6%	7%	10%	11%	13%	16%	16%	23%	7%
ROIC (ex. Cash)	7.1%	6.7%	9%	12%	14%	17%	22%	22%	33%	9%
Net Debt / EBITDA	2.8	3.4	1.9	1.4	1.0	0.6	0.4	0.4	0.1	1.5
Net Cash per Share	-73	-63	-310	-293	-262	-189	-167	-167	15	-362

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