

Ricoh (7752)

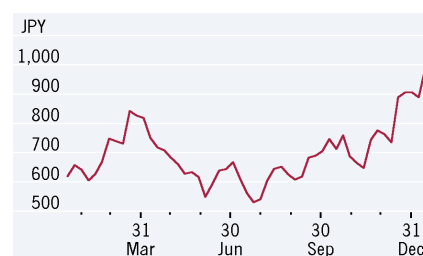
Maintaining Buy: Revising forex assumptions, factoring in possibility of further restructuring

- **Reiterating Buy** — We reflect the recent weaker yen (profit growth factor) in our forecasts. We raise our target price to ¥1,200 (PBR of 0.9x, PER of 11x on our FY3/14 estimates) from ¥1,000 (PBR of 0.9x, PER of 11x on our FY3/13 estimates) to factor in the change, and reiterate our Buy rating. Our revisions are due mainly to revised currency assumptions. However, we also highlight the potential for restructuring on top of the initiatives announced to date, and would see this as positive if it eventuates. Ricoh remains our top sector pick.
- **We raise our forecasts** — We raise our OP forecasts to ¥75bn from ¥71bn for FY3/13 and to ¥150bn from ¥130bn for FY3/14. We calculate that our changed currency assumptions (to ¥85/\$ from ¥80/\$ and to ¥115/€ from ¥100/€, effective Jan-Mar 2013) add ¥29bn YoY to FY3/14 profits, but see Ricoh channeling some of this to higher SG&A expenses. Aside from our currency assumptions, we make no other major revisions (e.g., to volume assumptions, for restructuring).
- **Reports Q3 on January 31** — We expect Q3 sales to be in line with Ricoh's internal targets (which initially struck us as slightly bullish). We also think concerns about the side-effects of restructuring have receded (see our December 17 memo, [Ricoh \(7752\) - Q3 preview discussions](#)). We think some investors could raise their hopes for an FY3/13 guidance hike, but advise against hoping for too much because the benefits of a weaker yen will not kick in fully until FY3/14. However, we see no need to reconsider our bullish stance if Ricoh does not revise guidance.
- **Room for further restructuring** — Ricoh cut its workforce for two years from May 2011 through March 2013, and expected to lock in all the benefits to fixed-cost cuts in FY3/14. However, we think its US staff count is still too high (Figure 1), and would hope that management announces further restructuring at the Q3 briefing or at its mid-May briefing (at which President Shiro Kondo usually outlines the company's medium-term targets). We think investors may be readier to acknowledge that Ricoh is indeed changing if it shows it is not content to rely on profit growth resulting from external factors (weaker yen) to improve its yen-based profits and indicates steps to make its US business more muscular in local-currency terms. See our November 15 memo, [Ricoh \(7752\) - Reiterating Buy: Market still underestimating restructuring scale](#), for a detailed analysis.

- Company Update
- Target Price Change
- Estimate Change

Buy	1
Price (15 Jan 13)	¥997
Target price	¥1,200
from ¥1,000	
Expected share price return	20.4%
Expected dividend yield	2.9%
Expected total return	23.3%
Market Cap	¥722,891M
	US\$8,142M

Price Performance (RIC: 7752.T, BB: 7752 JP)



Consol.	Sales		OP		Pretax Profit		NP		EPS	PE	
	¥M	YOY (%)	¥M	YOY (%)	OPM(%)	¥M	YOY (%)	¥M	YOY (%)	¥	X
3/11A	1,942,013	-3.7	60,196	-8.8	3.1	45,400	-21.1	19,650	-29.5	27	37.3
3/12A	1,903,477	-2.0	-18,068	nm	nm	-31,937	nm	-44,560	nm	-61	nm
3/13CE	1,900,000	-0.2	70,000	nm	3.7	62,500	nm	33,000	nm	46	21.9
3/13E	1,888,200	-0.8	71,000	nm	3.8	63,500	nm	33,640	nm	46	21.5
3/13RE	1,906,100	0.1	75,000	nm	3.9	67,500	nm	36,040	nm	50	20.1
3/14E	1,935,000	2.5	130,000	83.1	6.7	123,500	94.5	69,140	105.5	95	10.5
3/14RE	1,986,400	4.2	150,000	100.0	7.6	143,500	112.6	81,140	125.1	112	8.9
3/15E	1,990,600	2.9	140,500	8.1	7.1	134,500	8.9	75,740	9.5	104	9.6
3/15RE	2,037,800	2.6	164,000	9.3	8.0	158,000	10.1	89,840	10.7	124	8.1

A: Actuals, E: Citi Research Ests, CE: Co. Ests, RE: Citi Research Revised Ests, CRE: Co. Revised Ests, NA: Not Available, NM: Not Meaningful

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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7752.T: Fiscal year end 31-Mar						Price: ¥997; TP: ¥1,200; Market Cap: ¥722,891m; Recomm: Buy					
Profit & Loss (¥m)	2011	2012	2013E	2014E	2015E	Valuation ratios	2011	2012	2013E	2014E	2015E
Sales revenue	1,942,013	1,903,477	1,906,100	1,986,400	2,037,800	PE (x)	37.3	-16.5	20.1	8.9	8.1
Cost of sales	-1,151,939	-1,150,855	-1,159,100	-1,203,400	-1,253,800	PB (x)	0.8	0.9	0.8	0.8	0.7
Gross profit	790,074	752,622	747,000	783,000	784,000	EV/EBITDA (x)	2.1	8.0	3.0	1.7	1.3
Gross Margin (%)	40.7	39.5	39.2	39.4	38.5	FCF yield (%)	8.8	-8.3	10.7	12.9	15.3
EBITDA (Adj)	127,435	46,916	139,000	213,500	226,500	Dividend yield (%)	3.3	2.5	2.9	3.3	3.3
EBITDA Margin (Adj) (%)	6.6	2.5	7.3	10.7	11.1	Payout ratio (%)	124	-41	58	30	27
Depreciation	-67,239	-64,984	-64,000	-63,500	-62,500	ROE (%)	2.1	-5.1	4.2	8.9	9.2
Amortisation	0	0	0	0	0	Cashflow (¥m)					
EBIT (Adj)	60,196	-18,068	75,000	150,000	164,000	EBITDA	127,435	46,916	139,000	213,500	226,500
EBIT Margin (Adj) (%)	3.1	-0.9	3.9	7.6	8.0	Working capital	-23,420	-42,615	23,000	-11,000	-2,000
Net interest	0	0	0	0	0	Other	26,035	6,905	-9,635	-43,860	-49,160
Non-op/Except	-14,796	-13,869	-7,500	-6,500	-6,000	Operating cashflow					
PreTax Profit	45,400	-31,937	67,500	143,500	158,000	Capex	-65,589	-71,739	-75,000	-65,000	-65,000
Tax	-22,621	-8,223	-27,000	-57,400	-63,200	Net acq/disposals	93,400	91,137	89,000	88,500	87,500
Extraord./Min.Int./Pref.div.	-3,129	-4,400	-4,460	-4,960	-4,960	Other	-119,819	-131,841	-93,325	-88,500	-87,500
Reported net profit	19,650	-44,560	36,040	81,140	89,840	Investing cashflow					
Net Margin (%)	1.0	-2.3	1.9	4.1	4.4	Dividends paid	-23,943	-23,942	-15,200	-21,000	-23,900
Core NPAT	19,650	-44,560	36,040	81,140	89,840	Financing cashflow					
Per share data						Net change in cash	-62,996	-16,011	55,840	52,640	36,440
Reported EPS (¥)	27	-61	50	112	124	Free cashflow to s/holders					
Core EPS (¥)	27	-61	50	112	124		64,461	-60,533	77,365	93,640	110,340
EPS* (¥)	27	-61	50	112	124						
DPS (¥)	33	25	29	33	33						
CFPS (¥)	177	15	210	219	242						
FCFPS (¥)	88	-82	107	129	152						
BVPS (¥)	1,281	1,134	1,216	1,295	1,386						
Wtd avg ord shares (k)	725,643	725,571	725,500	725,500	725,500						
Wtd avg diluted shares (k)	735,490	735,419	725,500	725,500	725,500						
Growth rates											
Sales revenue (%)	-3.7	-2.0	0.1	4.2	2.6						
EBIT (Adj) (%)	-8.8	nm	nm	100.0	9.3						
Core NPAT (%)	-29.5	nm	nm	125.1	10.7						
Core EPS (%)	-29.5	nm	nm	125.1	10.7						
Balance Sheet (¥m)											
Cash & cash equiv.	181,179	158,671	236,234	265,234	281,234						
Accounts receivables	657,817	686,930	670,000	684,000	688,000						
Inventory	171,033	195,009	190,000	198,000	203,000						
Net fixed & other tangibles	264,740	268,527	280,000	282,000	285,000						
Goodwill & intangibles	0	0	0	0	0						
Financial & other assets	987,627	980,221	975,896	975,896	975,896						
Total assets	2,262,396	2,289,358	2,352,130	2,405,130	2,433,130						
Accounts payable	250,483	252,209	253,000	264,000	271,000						
Short-term debt	151,023	216,432	220,000	210,000	320,000						
Long-term debt	479,422	525,435	520,000	510,000	350,000						
Provisions & other liab	398,704	416,264	416,000	416,000	416,000						
Total liabilities	1,279,632	1,410,340	1,409,000	1,400,000	1,357,000						
Shareholders' equity	929,877	822,704	882,330	939,330	1,005,330						
Minority interests	52,887	56,314	60,800	65,800	70,800						
Total equity	982,764	879,018	943,130	1,005,130	1,076,130						
Net debt	449,266	583,196	503,766	454,766	388,766						
Net debt to equity (%)	45.7	66.3	53.4	45.2	36.1						

Note: Consolidated data. * EPS: NP/Est Shares OS.

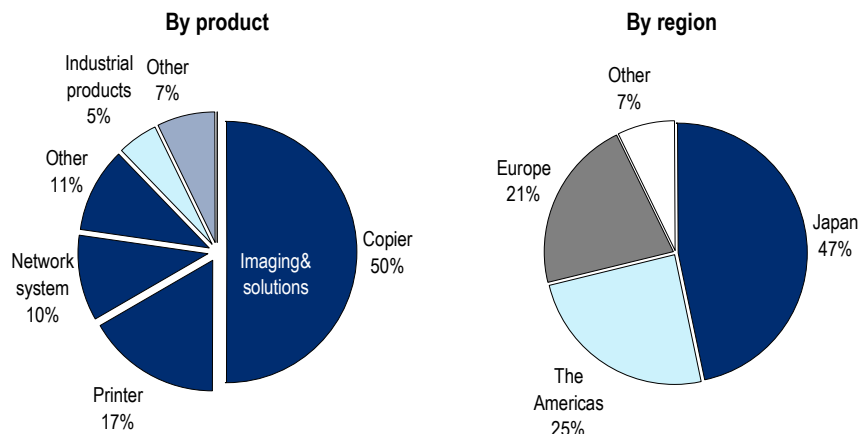
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Ricoh (7752) Investment Dashboard

Reasons to Buy

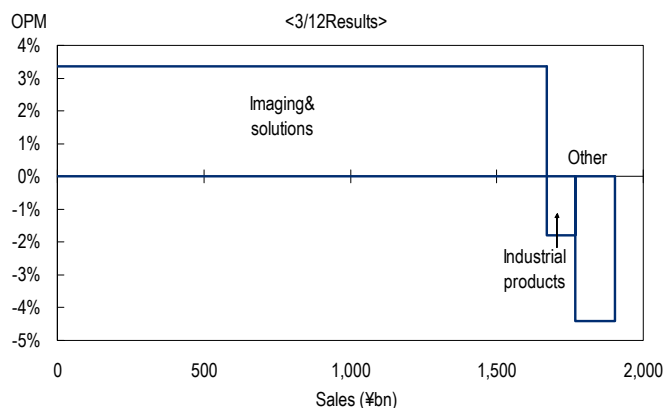
- On an FY3/14E basis, the shares are on a PER of under 9x, a PBR of 0.8x, and a dividend yield of 3% (assuming an annual ¥33 dividend)
- Earnings momentum is clearly better than peers, as restructuring benefits are emerging
- With a lack of macro visibility, the key is not top-line growth but Ricoh's own restructuring and structural reforms
- We believe market expectations are low, so we think investment appeal is strong among low-valued names from a risk/return perspective

Sales breakdown (FY3/12)



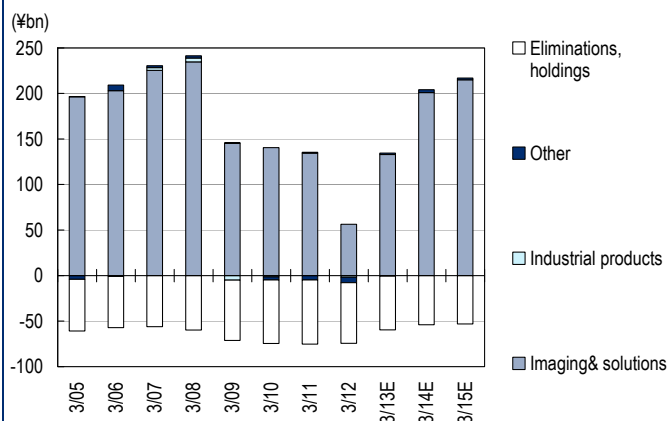
Source: Company data, Citi Research.

Business portfolio



Source: Company data, Citi Research.

Operating profits by segment

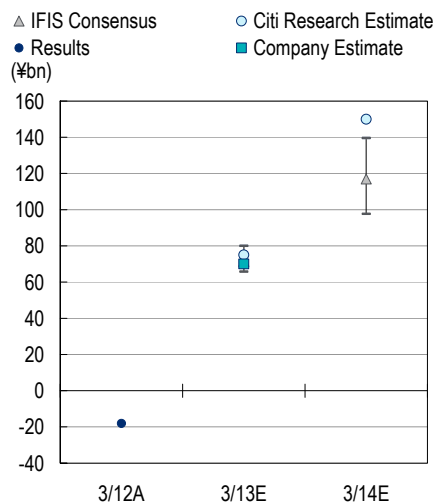


Source: Company data, Citi Research.

Alternate scenario: A more bearish case

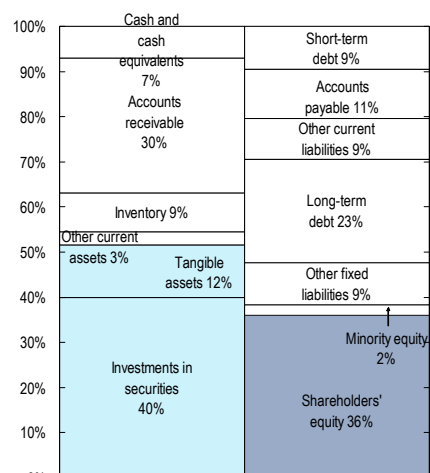
- 1) Rapid yen strengthening
- 2) Restructuring (headcount cuts) produce less of a fixed cost cut impact than expected
- 3) Costs coming first if Ricoh aims for rapid sales growth in digicams and new businesses
- 4) Greater-than-expected slowdown in office equipment market on macro environment and changes in customer attitudes
- 5) Emergence of a negative impact on marketing activity from restructuring, in contrast to recent experience

OP forecast comparison



Source: Company data, IFIS (January 15, 2013), Citi Research.

Balance sheet (end-FY3/12)



Source: Company data.

Potential for further restructuring

Comparison of Americas and European direct sales, staff counts

Although it is difficult to determine the efficiency of individual operating regions based on the materials Ricoh discloses, we have compared staff counts with local-currency sales (direct sales basis, considering direct sales ratios) for its Americas and European office equipment businesses (which it classifies as imaging solutions).

Our analysis based on company disclosure shows efficiency in Americas more than 20% lower than in Europe

Our analysis shows per-staff sales (dollar terms, based on company's FY3/13 targets) of \$166,000 in the US and \$219,000 in Europe. Although we estimate that investment in new businesses (managed document solutions and production printing, where spending for future growth is likely substantial) may be greater in the Americas than in Europe (or that the Americas is carrying the cost of investing in growth in other regions), our calculations indicate that efficiency in the US is 24% lower than in Europe. They show clearly that staff growth has outpaced growth at the top line around the time of the Ikon acquisition (2008).

Case study: Americas would not catch Europe even if medium-term sales grew 15% over FY3/13 target and it cut a further 3,000 staff

We next consider the leeway for further restructuring. As the continuing entity, Ricoh can be expected to formulate staffing plans based on its medium-term sales targets. We have conducted a case-study based on particular sets of sales assumptions. We posit two scenarios: scenario A, where local-currency sales (medium term) increase 5% over the FY3/13 target, and scenario B, where they rise 15%. We also assume that the Americas business cuts an additional 3,000 staff (and that there are no further headcount cuts in Europe). Our case study shows that dollar-based per-staff sales in the Americas are still 19% lower than in Europe even if in the Americas grow 15% over their current level. Although our analysis may be overly simplistic (Ricoch does not release detailed data by staff category, e.g., marketing, indirect operations, after-sales service), the substantial efficiency gap between the Americas and Europe (i.e., differential higher than 5%-10%) suggests the company's current plans to cut fixed costs will very likely be insufficient to close the gap.

Figure 1. Comparison of sales per person in Ricoh's Americas and Europe operations

—Even if Americas sales rise 5% versus the company plan for FY3/13 on a local currency basis and headcount were to be cut by an additional 3,000 people, dollar-basis per person sales would be 19% lower than in Europe, so there is room for improvement to efficiency versus Europe

Americas	3/06	3/07	3/08	3/09	3/10	3/11	3/12	3/13CE	Case A +5%	CaseB +15%
Sales in ¥mn	368,184	405,457	416,446	487,563	544,206	509,904	453,570	453,600	524,266	574,196
US\$/¥	113	117	114	101	93	86	79	77	85	85
Sales converted to US\$mn	3,251	3,465	3,640	4,849	5,857	5,945	5,736	5,874	6,168	6,755
Direct sales ratio (%)	50%	50%	53%	67%	84%	84%	84%	85%	85%	85%
Employee in Americas	11,319	11,832	13,195	37,314	34,811	33,866	32,875	30,000	27,000	27,000
YoY (person)	-1,076	513	1,363	24,119	-2,503	-945	-991	-2,875	NA	NA
Sales per employee										
US\$ conversion (\$'000)	143.6	146.4	146.2	142.5	141.3	147.5	146.6	166.4	194.2	212.7
Negative impact to Europe (%)	-18%	-9%	-31%	-35%	-32%	-27%	-31%	-24%	-19%	-19%
¥ conversion (¥mn)	16.3	17.1	16.7	8.8	13.1	12.6	11.6	12.9	16.5	18.1
Europe	3/06	3/07	3/08	3/09	3/10	3/11	3/12	3/13CE	Case A +5%	Case B +15%
Sales in ¥mn	412,550	479,859	571,481	501,887	441,649	399,382	389,931	382,700	460,590	504,456
€/¥	138	150	162	144	131	113	109	100	115	115
Sales converted to €mn	2,993	3,197	3,534	3,492	3,366	3,526	3,576	3,814	4,005	4,387
Direct sales ratio (%)	65%	65%	67%	68%	75%	75%	75%	75%	75%	75%
Employee in Europe	13,439	16,652	15,738	15,493	17,194	17,308	17,483	17,000	17,000	17,000
YoY (person)	1,258	3,213	-914	-245	1,701	114	175	-483	NA	NA
Sales per employee										
€ conversion (€'000)	144.7	124.8	150.5	149.8	146.8	152.8	153.4	168.3	176.7	193.5
US\$ conversion (\$'000)	176.2	160.1	212.7	219.1	207.3	201.8	211.5	218.6	239.1	261.8
¥ conversion (¥mn)	20.0	18.7	24.3	22.0	19.3	17.3	16.7	16.9	20.3	22.3

Note: Sales in ¥mn in the Figure are the values for the Americas and Europe in sales by region in the imaging and solutions segment.. We convert to the local currency at the period-average forex rate. Personnel counts for both regions are for the main local subsidiaries in the *Yuko* as of the end of each fiscal year (Lanier, Ricoh Americas Corporation, Infoprint Solutions Company, Ricoh Production Print Solutions, Ikon Office Solutions, Ricoh Europe, Gestetner, NRG Group and other firms that we believe are in charge of management and operations). Sales per employee reference direct sales ratios by region and are values derived by dividing direct sales (local currency basis) by number of employees. Underlined numbers are assumptions.

Source: Company data, Citi Research.

Related reports

November 15: [Office MFPs \(copiers\) - YoY momentum softened for a while but is relatively firm](#)

November 15: [Ricoh \(7752\) - Reiterating Buy: Market still underestimating restructuring scale](#)

December 17: [Ricoh \(7752\) - Q3 preview discussions](#)

Ricoh

Investment strategy

We rate the shares of Ricoh Buy (1), with a ¥1,200 target price (FY3/14E PBR of 0.9x). Ricoh is a specialist office equipment maker which makes the bulk of its earnings from the copier business. It is the global number one in copier shipment volume, with a 21% market share in 2011. Earnings have been weak since it acquired major US office equipment dealer Ikon in October 2008. Ricoh fell into the red at the consolidated operating level in FY3/12 for the first time since listing, due to the eastern Japan earthquake, the Thai floods, and the start of restructuring. However, we see the stock being favored by investors anticipating the drop-out of one-time negatives and the emergence of restructuring benefits in FY3/13 and out. The shares look very undervalued if we look out to the earnings improvement in FY3/14, on which visibility has been rising. If Ricoh announces the outline of additional restructuring, we think the benefits of fixed cost cuts would outweigh the cost of upfront headcount cuts and we note the potential for profit upside versus our earnings forecasts for FY3/14 and FY3/15.

Valuation

We set our Ricoh target price at ¥1,200 (FY3/14E PBR of 0.9x). The shares have been assigned a discount of 10%-50% versus the market average since the global financial crisis, as they have been trading in a PBR range of 0.5x-1.3x. Our target price assigns a discount of around 15%, close to the level of spring 2010, when hopes of post-global financial crisis earnings momentum improvement were high. Our target price equates to an FY3/14E PER of 11x and dividend yield of 2.8%.

Risks

We see potential downside risks as 1) rapid yen strengthening, 2) shrinking expectations for fixed cost cuts via structural reform (i.e., job cuts), 3) a clear rise in costs should the company aim for rapid sales expansion in its digital camera business or other new businesses, and 4) changes in the macroeconomic environment or customer attitudes, resulting in a larger-than-expected decline for office equipment. As for upside risks, we would envision 1) yen weakening; 2) proof of cost cutting benefits, an area where we think the company will fall short of its plans; 3) changes in the macroeconomic environment or customer attitudes, resulting in faster-than-expected growth for office equipment; and 4) should Ricoh earnings look more reassuring relative to peers as concerns about slower demand mount.

Appendix A-1

Analyst Certification

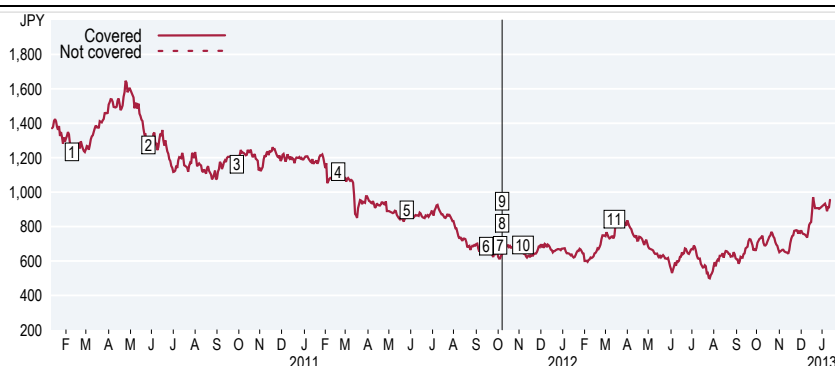
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IMPORTANT DISCLOSURES

Ricoh (7752)

Ratings and Target Price History Fundamental Research

Analyst: Masahiro Shibano



	Date	Rating	Target Price	Closing Price
1	9-Feb-10	2M	*1,300	1,266
2	27-May-10	2M	*1,400	1,306
3	29-Sep-10	2M	*1,300	1,200
4	18-Feb-11	2M	*1,250	1,113

* Indicates change

	Date	Rating	Target Price	Closing Price
5	26-May-11	2M	*980	885
6	15-Sep-11	2M	*700	662
7	5-Oct-11	2M	*670	615
8	7-Oct-11	Stock rating system changed		

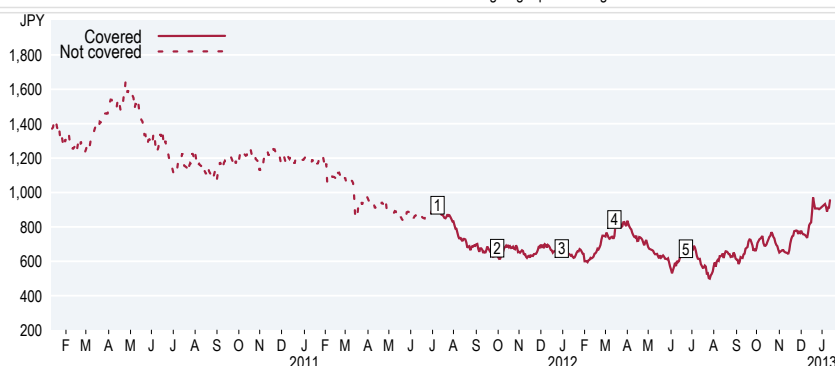
	Date	Rating	Target Price	Closing Price
9	7-Oct-11	*2	670	638
10	7-Nov-11	2	*700	660
11	14-Mar-12	*1	*1,000	746

Rating/target price changes above reflect Eastern Standard Time

Ricoh (7752)

Ratings and Target Price History Best Ideas Research Relative Call (3 Month)

Analyst: Masahiro Shibano



	Date	Rating	Target Price	Closing Price
1	8-Jul-11	*ADD LP	-	926
2	30-Sep-11	*REM LP	-	654

* Indicates change

	Date	Rating	Target Price	Closing Price
3	30-Dec-11	*ADD LP	-	671
4	14-Mar-12	*REM LP	-	746

	Date	Rating	Target Price	Closing Price
5	22-Jun-12	*ADD MP	-	670

Rating/target price changes above reflect Eastern Standard Time

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12 Month Rating			Relative Rating		
Buy	Hold	Sell	Buy	Hold	Sell
49%	38%	12%	7%	86%	7%
53%	49%	45%	60%	49%	55%

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