

Fujitsu General (6755)

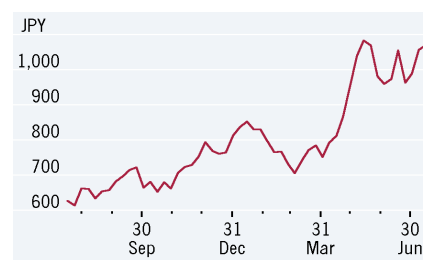
Initiating at Buy: An air-conditioner titan

■ Initiation of Coverage

- **Initiating at Buy** — We initiate coverage of Fujitsu General with a Buy rating as 1) we see substantial growth potential, particularly in emerging markets, for mainstay room air-conditioners, and 2) IT and device earnings are steady while wireless emergency management systems are benefitting from a spike in demand. The shares look undervalued on an FY3/14E PER of 12x and FY3/15E PER of 11x.
- **Restructuring paying off** — Fujitsu General restructured in the early 2000s and has strengthened its earnings power by eliminating the unprofitable PDP TV and refrigerator businesses and focusing on air-conditioners. The air-conditioner business boasts a strong product lineup backed by leading technology as well as global sales channels, and with continued growth both in Japan and overseas Fujitsu General looks to us like a blue-chip name that is not widely known. We think the company, which started restructuring ahead of peers, could be a role model for the revival of Japan's electronic equipment industry.
- **Air-conditioning titan making global strides** — Fujitsu General sells air-conditioners globally: in FY3/13 sales broke down to 28% in Japan, 16% in Europe, 11% in the Americas, 11% in Oceania, 20% in the Middle East and Africa, and 14% in China and other parts of Asia. We thus think it is in a good position to benefit from market expansion. The company manufactures air-conditioners overseas and then imports them into Japan, so we note yen weakness is negative for OP. However, we believe profit growth will continue on overseas expansion and lower input costs.
- **IT & devices** — Since FY3/12, this business has grown due to a spike in demand as wireless fire emergency management systems went digital. We believe profits will stay high through FY3/16. While we anticipate an earnings decline here from FY3/17 as the one-off demand drops out, Fujitsu General continues to bring in stable earnings from corporate sales in Japan, so we believe earnings levels prior to the demand spike (FY3/11 OP was ¥2.4bn) are sustainable.
- **¥1,330 TP** — We refer to our DCF-based theoretical price and the average PER for global household appliance manufacturers in setting our target price. Applying the household appliance average PER of 14x to our FY3/15 EPS estimate yields a theoretical share price of c¥1,410. Our DCF model yields a theoretical share price of c¥1,240, so we set a target price of ¥1,330.

Buy	1
Price (09 Jul 13)	¥1,056
Target price	¥1,330
Expected share price return	25.9%
Expected dividend yield	1.1%
Expected total return	27.1%
Market Cap	¥115,159M
	US\$1,162M

Price Performance (RIC: 6755.T, BB: 6755 JP)



Consol.	Sales		OP			RP		NP		EPS	PE
	¥M	YOY (%)	¥M	YOY (%)	OPM(%)	¥M	YOY (%)	¥M	YOY (%)	¥	X
3/12A	203,549	11.8	13,319	20.8	6.5	9,803	12.7	5,175	6.7	47	22.3
3/13A	209,167	2.8	15,120	13.5	7.2	20,129	105.3	13,009	151.4	119	8.9
3/14CE	235,000	12.4	16,000	5.8	6.8	15,000	-25.5	10,000	-23.1	92	11.5
3/14E	235,600	12.6	16,000	5.8	6.8	14,800	-26.5	9,600	-26.2	88	12.0
3/15E	250,600	6.4	18,000	12.5	7.2	16,900	14.2	11,000	14.6	101	10.5
3/16E	260,100	3.8	18,500	2.8	7.1	17,500	3.6	11,400	3.6	105	10.1

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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6755.T: Fiscal year end 31-Mar						Price: ¥1,056; TP: ¥1,330; Market Cap: ¥115,159m; Recomm: Buy					
Profit & Loss (¥m)	2012	2013	2014E	2015E	2016E	Valuation ratios	2012	2013	2014E	2015E	2016E
Sales revenue	203,549	209,167	235,600	250,600	260,100	PE (x)	22.3	8.9	12.0	10.5	10.1
Cost of sales	-154,388	-155,954	-179,600	-190,600	-197,600	PB (x)	3.5	2.5	2.1	1.8	1.6
Gross profit	49,161	53,213	56,000	60,000	62,500	EV/EBITDA (x)	8.1	7.0	6.2	5.4	4.9
Gross Margin (%)	24.2	25.4	23.8	23.9	24.0	FCF yield (%)	4.9	7.8	2.4	6.5	8.4
EBITDA (Adj)	16,565	18,439	20,000	22,500	23,500	Dividend yield (%)	0.8	1.1	1.1	1.4	1.9
EBITDA Margin (Adj) (%)	8.1	8.8	8.5	9.0	9.0	Payout ratio (%)	17	10	14	15	19
Depreciation	-3,246	-3,319	-4,000	-4,500	-5,000	ROE (%)	17.0	32.6	18.9	18.4	16.5
Amortisation	0	0	0	0	0	Cashflow (¥m)					
EBIT (Adj)	13,319	15,120	16,000	18,000	18,500	EBITDA	16,565	18,439	20,000	22,500	23,500
EBIT Margin (Adj) (%)	6.5	7.2	6.8	7.2	7.1	Working capital	-6,665	-9,206	-1,163	-3,272	-2,072
Net interest	-484	-385	-300	-200	-100	Other	-2,059	2,085	-6,100	-6,700	-6,800
Non-op/Except	-3,032	5,393	-900	-900	-900	Operating cashflow					
Recurring profit	9,803	20,129	14,800	16,900	17,500	Capex	-2,229	-2,373	-10,000	-5,000	-5,000
Tax	-3,906	-6,254	-4,400	-5,100	-5,300	Net acq/disposals	0	0	0	0	0
Extraord./Min.Int./Pref.div.	-721	-865	-800	-800	-800	Other	-870	-523	0	0	0
Reported net profit	5,175	13,009	9,600	11,000	11,400	Investing cashflow					
Net Margin (%)	2.5	6.2	4.1	4.4	4.4	Dividends paid	-651	-869	-1,309	-1,636	-2,181
Core NPAT	5,175	13,009	9,600	11,000	11,400	Financing cashflow					
Per share data						Net change in cash	-1,068	1,296	1,429	893	2,447
Reported EPS (¥)	47	119	88	101	105	Free cashflow to s/holders					
Core EPS (¥)	47	119	88	101	105		5,612	8,945	2,737	7,528	9,628
EPS* (¥)	47	119	88	101	105						
DPS (¥)	8	12	12	15	20						
CFPS (¥)	72	104	117	115	134						
FCFPS (¥)	51	82	25	69	88						
BVPS (¥)	303	428	504	590	675						
Wtd avg ord shares (m)	109	109	109	109	109						
Wtd avg diluted shares (m)	109	109	109	109	109						
Growth rates											
Sales revenue (%)	11.8	2.8	12.6	6.4	3.8						
EBIT (Adj) (%)	20.8	13.5	5.8	12.5	2.8						
Core NPAT (%)	6.7	151.4	-26.2	14.6	3.6						
Core EPS (%)	6.7	151.4	-26.2	14.6	3.6						
Balance Sheet (¥m)											
Cash & cash equiv.	4,639	5,935	7,363	8,256	10,703						
Accounts receivables	53,621	75,719	80,104	85,204	88,434						
Inventory	15,347	14,223	16,021	17,041	17,687						
Net fixed & other tangibles	34,472	34,477	40,477	40,977	40,977						
Goodwill & intangibles	2,162	2,155	2,155	2,155	2,155						
Financial & other assets	11,244	16,672	16,672	16,672	16,672						
Total assets	121,486	149,182	162,793	170,306	176,629						
Accounts payable	30,295	39,720	44,740	47,588	49,392						
Short-term debt	17,525	16,165	16,165	11,165	6,165						
Long-term debt	5,201	1,135	1,135	1,135	1,135						
Provisions & other liab	33,737	43,657	43,657	43,657	43,657						
Total liabilities	86,759	100,679	105,698	103,547	100,351						
Shareholders' equity	33,083	46,709	55,000	64,364	73,583						
Minority interests	1,643	1,794	2,094	2,394	2,694						
Total equity	34,727	48,503	57,095	66,759	76,278						
Net debt	18,087	11,366	9,937	4,045	-3,402						
Net debt to equity (%)	52.1	23.4	17.4	6.1	-4.5						

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

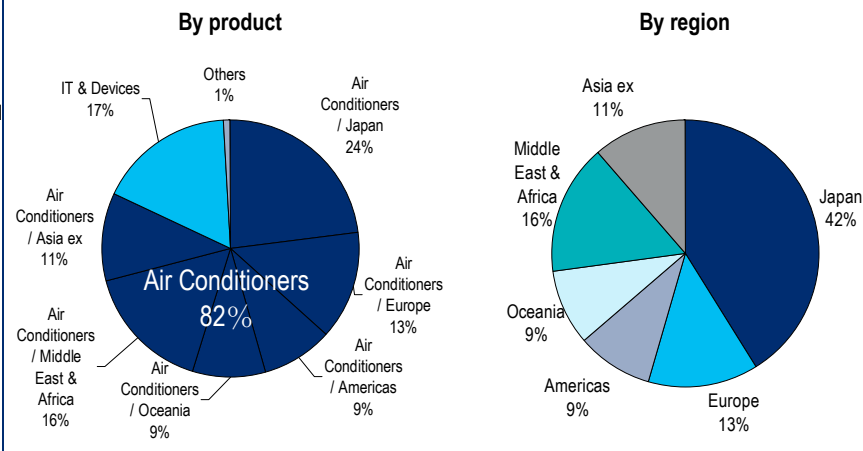
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Fujitsu General (6755) Investment Dashboard

Reasons to Buy

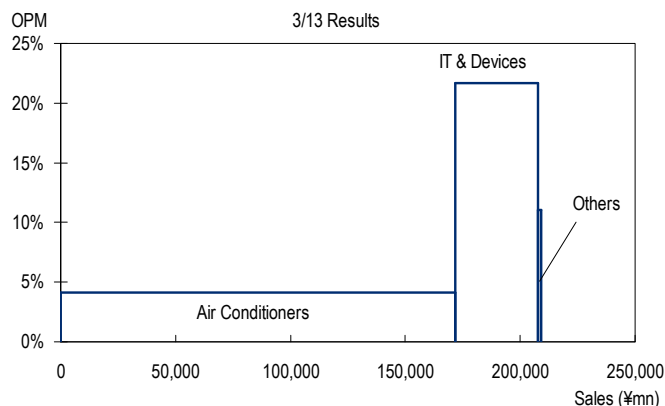
- Fujitsu General was first among Japan's electronic equipment firms to enact successful structural reforms
- The air-conditioner business boasts top-level technological capabilities and sales channels, and we anticipate strong growth in emerging markets
- IT & devices offer stable earnings and benefit from special demand related to digitization of wireless disaster management systems
- Air-conditioners are produced overseas and imported into Japan, so yen weakness is a concern. However, we think this can be offset via cost cuts
- The shares look undervalued on an FY3/14E PER of 12x and FY3/15E PER of 11x

Sales breakdown (FY3/13)



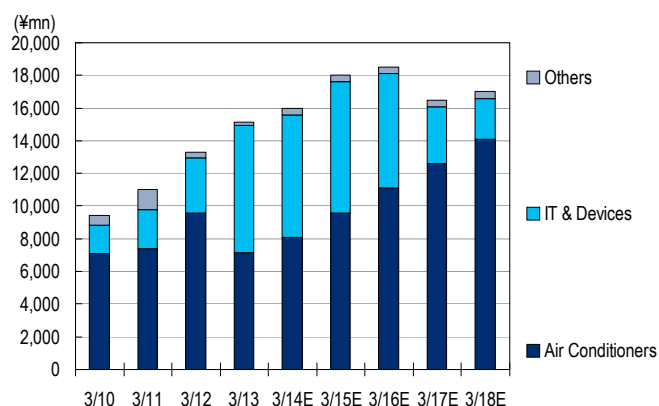
Source: Company data.

Business portfolio



Source: Company data.

OP by segment

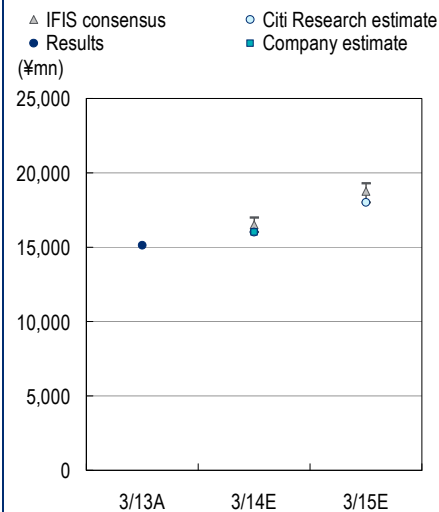


Source: Company data, Citi Research.

Alternate scenario: A more bearish case

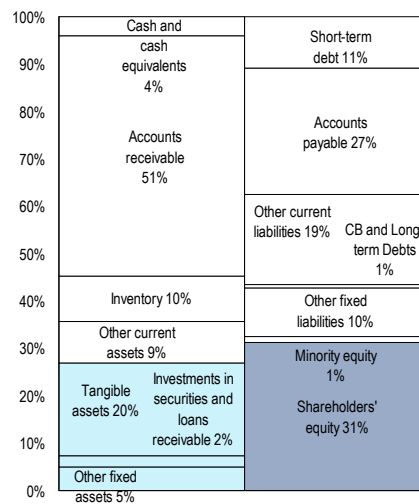
- A lower outlook for air-conditioner demand via deterioration in the global macroeconomy
- A decline in market share globally
- Greater-than-expected yen weakness

OP forecast comparison



Source: Company data, IFIS (July 16), Citi Research.

Balance sheet (end-FY3/13)



Source: Company data, Citi Research.

Share price drivers	Company description
<ul style="list-style-type: none"> A rise in air-conditioner demand could be positive for the shares Success in growing sales in North America and China/Asia could be positive for the shares Yen weakness or strength for developing market currencies could be negative for the shares 	<p>Fujitsu General is an electronic equipment maker that focuses on air-conditioners and wireless disaster management systems. It became a member of the Fujitsu Group in 1984 via a capital and business tie-up, and Fujitsu currently owns 46% of outstanding shares. Since the 2000s it has moved forward with structural reforms, such as withdrawing from unprofitable businesses like PDP TVs and refrigerators and focusing on air-conditioners. The company's strengths are its impressive technological capabilities and global sales network, and led by its energy-efficient models it sells air-conditioners in major developed and developing markets. The IT & devices segment is likely to see earnings rise from FY3/13 due to the digitization of wireless disaster management systems. As Fujitsu General manufactures air-conditioners overseas and imports them into Japan, one should keep in mind that yen weakness and/or strength for emerging market currencies is negative for OP.</p>

Valuation

		Rating		Price	Mkt	FY1E=	EPS		PER (x)		PBR (x)	OPM	EV/EBITDA (x)			RoE	
Code	Company				Cap		FY1E	FY2E	FY1E	FY2E	FY1E	FY1E	FY2E	FY1E	FY2E	FY1E	FY2E
Home Appliances					(\$ bn)												
6367.T	Daikin Inds	2	JPY	4,685.00	13.7	3/14	254.8	290.1	18.4	16.1	2.0	7.5%	7.7%	7.8	6.9	11.5%	11.9%
6501.T	Hitachi	1	JPY	666.00	32.2	3/14	49.0	60.3	13.6	11.1	1.3	5.6%	6.4%	5.3	4.9	10.8%	12.0%
6502.T	Toshiba	1	JPY	480.00	20.4	3/14	36.4	42.6	13.2	11.3	1.7	5.4%	5.7%	5.2	4.5	13.6%	13.9%
6503.T	Mitsubishi Elec	2	JPY	1,092.00	23.5	3/14	57.5	73.7	19.0	14.8	1.7	5.7%	6.7%	6.5	5.5	9.2%	11.0%
6752.T	Panasonic	1	JPY	858.00	19.9	3/14	33.1	50.0	25.9	17.2	1.4	3.8%	4.4%	4.8	4.7	5.8%	8.1%
6753.T	Sharp	3	JPY	427.00	5.0	3/14	-2.3	12.4	nm	34.4	2.7	2.4%	2.6%	5.8	5.3	-1.9%	9.0%
6755.T	Fujitsu General	1	JPY	1,071.00	1.2	3/14	88.0	100.9	12.2	10.6	2.1	6.8%	7.2%	6.3	5.4	18.9%	18.4%
005930.KS	Samsung Elec	1	KRW	1,298,000.00	170.4	12/13	217,752.9	242,150.1	6.0	5.4	1.3	17.2%	18.2%	2.5	1.9	24.2%	21.6%
066570.KS	LG Elec	2	KRW	71,000.00	10.4	12/13	5,113.2	7,386.0	13.9	9.6	0.9	2.2%	2.3%	4.2	4.3	6.7%	9.2%
1169.HK	Haier Elec Grp	1	CNY	13.02	4.3	12/13	0.8	0.9	12.9	11.0	3.4	4.6%	4.7%	7.1	5.9	33.4%	30.1%
ELUXb.ST	Electrolux	1	SEK	176.60	8.2	12/13	10.0	15.0	17.6	11.8	3.3	4.0%	5.4%	8.4	6.9	16.3%	27.0%
ARCLK.IS	Arçelik	2	TRY	13.60	4.8	12/13	1.0	1.2	13.2	11.5	2.2	8.3%	8.6%	8.6	7.8	17.3%	18.1%
Telecom equipment																	
NOK1V.HE	Nokia	2H	EUR	3.08	15.1	12/13	-0.1	0.2	nm	20.4	1.5	-1.6%	4.8%	8.6	3.1	-8.2%	7.2%
ERICb.ST	Ericsson	1	SEK	80.90	39.9	12/13	6.0	6.0	13.5	13.6	1.9	7.0%	10.0%	9.1	7.4	7.5%	11.2%
MSI.N	Motorola Solutions	2	USD	59.17	16.1	12/13	4.8	4.3	12.4	13.7	4.8	15.9%	17.1%	8.9	8.2	41.5%	35.0%
2498.TW	HTC	3	TWD	192.50	5.5	12/13	7.0	7.2	27.5	26.7	1.9	2.2%	2.4%	6.8	5.3	7.0%	6.8%
EMS/OEM/ODM																	
SAPG.DE	SAP AG	2	EUR	57.52	92.3	12/13	3.4	3.9	17.0	14.8	4.2	25.8%	27.6%	13.3	11.2	21.7%	21.3%
2357.TW	ASUSTeK Computer	3	TWD	277.50	7.0	12/13	25.6	22.6	10.9	12.3	1.6	4.3%	4.2%	5.5	5.6	14.8%	12.5%
2317.TW	Hon Hai Precision	1	TWD	78.40	31.1	12/12	8.0	9.2	9.8	8.5	1.3	2.7%	3.2%	4.7	3.1	14.1%	14.2%
FLEX.O	Flextronics Intl	2	USD	7.94	4.9	3/14	0.8	1.1	10.3	7.4	2.1	2.5%	2.8%	3.4	2.6	19.0%	23.3%
2354.TW	Foxconn Tech	3	TWD	75.90	3.1	12/12	6.8	6.3	11.2	12.0	1.6	6.8%	6.3%	5.4	5.1	14.6%	12.3%
3231.TW	Wistron	3	TWD	28.65	2.1	12/12	3.0	3.2	9.4	8.9	1.0	1.2%	1.3%	4.8	4.0	10.8%	11.0%
LCD panels																	
034220.KS	LG Display	2	KRW	27,650.00	8.8	12/13	2,051.1	2,866.2	13.5	9.6	0.9	4.1%	4.8%	2.1	1.9	6.9%	8.9%
GLW.N	Corning Inc	2	USD	15.09	22.2	12/13	1.3	1.4	11.6	10.7	1.0	19.2%	19.2%	5.6	5.4	9.1%	9.1%
Electronic components																	
JBL.N	Jabil Circuit	2	USD	22.01	4.5	8/13	2.2	2.6	9.9	8.4	2.0	3.9%	4.2%	4.6	4.5	20.4%	20.8%
009150.KS	Samsung Elec-Mec	2	KRW	82,200.00	5.5	12/13	6,357.3	6,720.4	12.9	12.2	1.4	7.3%	7.1%	4.3	4.0	11.6%	11.2%
MOLX.O	Molex	2	USD	30.04	5.0	6/13	1.5	1.6	19.9	18.3	2.1	10.7%	11.6%	7.1	6.5	10.0%	11.4%
AVX.N	AVX	2	USD	12.87	2.2	3/14	0.6	0.8	19.9	16.5	1.2	10.0%	11.1%	5.3	5.1	5.7%	7.1%
APH.N	Amphenol Corp	1	USD	84.28	13.5	12/13	3.8	4.3	21.9	19.6	4.9	19.4%	19.3%	13.4	12.3	24.0%	23.4%
VSH.N	Vishay Intertech	2	USD	14.90	2.1	12/13	0.8	1.2	17.7	12.6	1.2	8.8%	10.8%	3.3	2.5	7.6%	9.7%
TEL.N	TE Connectivity	1	USD	47.28	19.6	9/13	3.1	3.7	15.0	12.6	2.5	13.8%	14.9%	8.3	7.2	18.5%	17.6%
051910.KS	LG Chem	1	KRW	273,000.00	16.1	12/13	22,823.7	28,934.9	12.0	9.4	1.5	8.3%	9.9%	6.5	5.3	13.4%	15.1%
Tech conglomerates																	
SIEGn.DE	Siemens	1	EUR	80.01	92.1	9/13	6.5	8.3	12.4	9.6	2.2	7.9%	11.6%	8.5	6.0	13.9%	18.9%
PHG.AS	Philips	3	EUR	22.73	29.0	12/13	1.7	1.8	13.3	12.6	1.8	8.7%	8.7%	5.6	5.3	12.0%	10.7%

Note: Share prices as of the July 16 close.
Source: Citi Research.

Initiating with a Buy

Initiating coverage with a Buy rating

We initiate coverage of Fujitsu General with a Buy rating for the following reasons: 1) growth potential for mainstay room air-conditioners is high, particularly in emerging markets; 2) IT & devices generate stable earnings and wireless emergency management systems are benefiting from extraordinary demand. The shares look undervalued on an FY3/14E PER of 12x and FY3/15E PER of 11x, so we rate them Buy.

A giant in air-conditioners

Fujitsu General is a maker of air-conditioners and electronic products, mainly wireless fire/disaster prevention systems. We consider the company an undiscovered blue-chip, with its mainstay air-conditioner business featuring advanced technologies, a broad product lineup, and sales channels worldwide supporting continued growth in Japan and overseas. We expect demand for air-conditioners to expand in both developed and developing economies. Fujitsu General is highly competitive in room air-conditioners and well positioned to benefit from market growth, in our view.

One of the first Japanese electronics makers to implement successful restructuring

Fujitsu General embarked on restructuring in the first half of the 2000s, disposing of unprofitable FPD TV and refrigerator businesses and concentrating resources in the growing air-conditioner business. Reforms have strengthened its earnings structure. Many Japanese electronics manufacturers are now in the middle of restructuring programs, and we see early-mover Fujitsu General as a role model for the revival of the Japanese electronics industry.

¥1,330 target price based on DCF and PER

We refer to our DCF-based theoretical price and the average PER for global household appliance manufacturers in setting our target price. Applying the household appliance average PER of 14x to our FY3/15 EPS estimate yields a theoretical share price of c¥1,410. Our DCF model yields a theoretical share price of c¥1,240, so we set a target price of ¥1,330.

Shares look undervalued

Restructuring and air-conditioner growth supports strong share price performance

Fujitsu General's share price has continued to rise over the last four years, reflecting business restructuring and air-conditioner business growth (Figure 1). The May 20 closing price of ¥1,094 was more than 7x higher than the February 2009 low of ¥142. This performance was not only better than that of TOPIX and major Japanese electronic sectors but also that of major overseas household appliance manufacturers, with the exception of Haier and some other Chinese companies.

Undervalued at current multiples

With the stock market pullback, the shares declined to ¥933 on June 26. They are now trading on a FY3/14E PER of 12x. 1) We believe this multiple is compelling on both an historical and peer-comparison basis. 2) Our DCF model suggests that investors have not priced in longer-term growth potential. Another point of appeal is the scope to increase shareholder returns.

Undervalued on a FY3/14E PER of 12x and FY3/15E of 11x

The FY3/14E PER (12x) and FY3/15E PER (11x) are lower than the averages for household appliance makers (19x and 14x, respectively) and also Fujitsu General's 10-year average of 15x (Figures 2, 3). Investors may have factored in the end of extraordinary demand for wireless disaster prevention systems driven by digitization, but considering Fujitsu General has a higher RoE and operating margin than peers, structural reforms are strengthening its earnings power, and the long-term growth potential for air-conditioners is good, we believe the stock is undervalued at these multiples.

DCF model suggests growth potential not adequately discounted

Our DCF-model yields a theoretical share price of ¥1,240 (WACC of 6.6%, assuming a risk free rate of 1%, equity-risk premium of 6%, terminal growth rate of 0%, beta of 1.1, and tax rate of 30%; and earnings forecasts for FY3/14 to FY3/18).

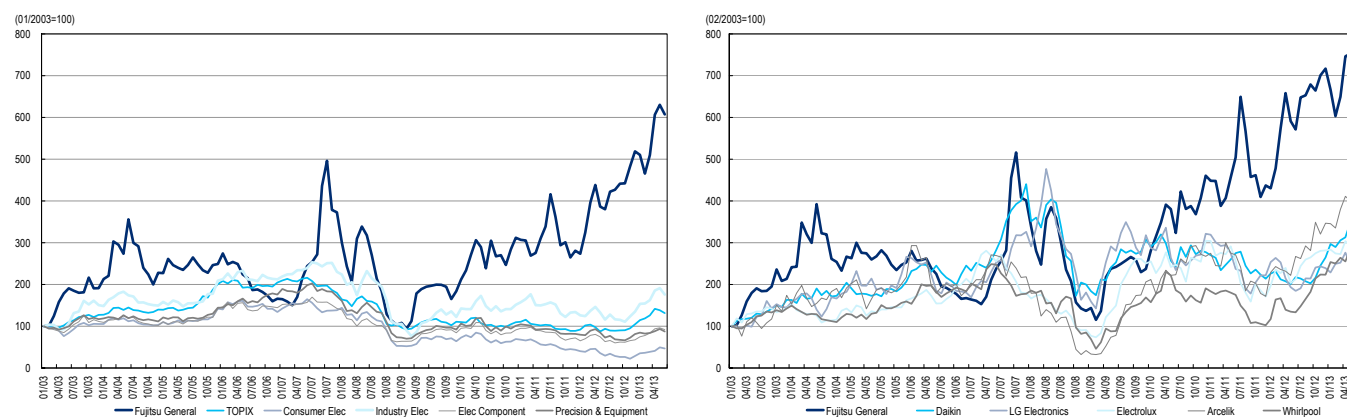
We do not believe long-term growth potential is adequately discounted at the current share price level (Figure 4).

Expecting greater shareholder returns

We expect Fujitsu General to be in a solid financial position from FY3/17

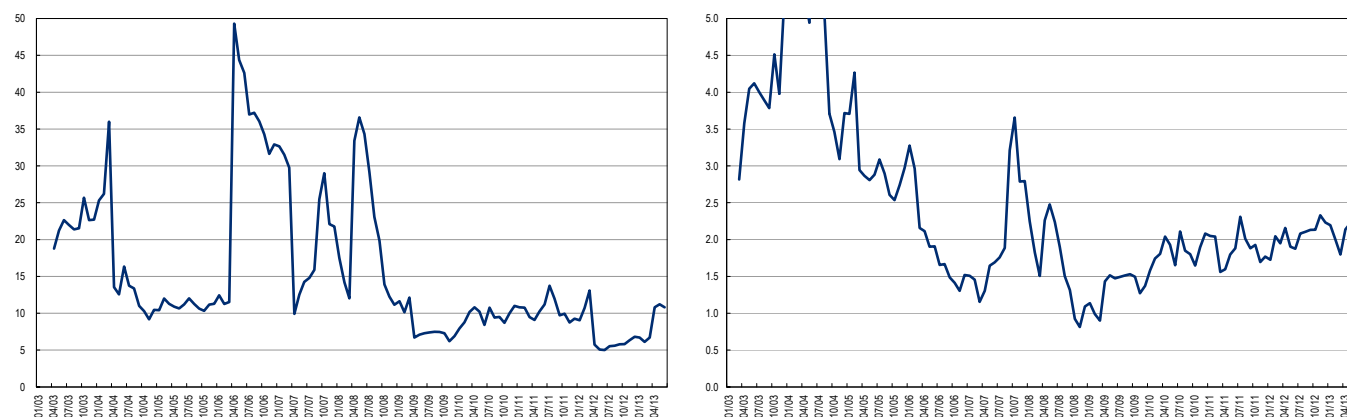
We expect shareholder returns to increase (Figure 5). Currently, Fujitsu General's priorities for use of free cash flow, in order, are 1) strengthening its business foundations (capex, sales channels, etc.) and 2) strengthening its financial position (debt repayment). We forecast the end of special demand for wireless disaster prevention systems will increase sales receivables turnover and reduce working capital requirements, resulting in net cash moving into positive territory from around FY3/17. The dividend payout ratio based on FY3/14 guidance is only 13%. As the financial position improves, we expect Fujitsu General to strengthen shareholder returns by buying back shares and raising the dividend payout ratio. We think European household appliance manufacturers Electrolux and Arcelik, whose dividend yields have reached 4% against the backdrop of stable FCF, will probably be used as benchmarks.

Figure 1. Fujitsu General: Shares have outperformed TOPIX and electronics sectors (LHS) as well as overseas competitors (RHS)



Note: The LHS is yen-based market cap and the RHS is dollar-based market cap.
Source: Company data, Citi Research.

Figure 2. Fujitsu General: PER (LHS) and PBR (RHS): Recent PER is low in historical terms



Source: Company data, Citi Research

Figure 3. Comparison of major household appliance manufacturers' valuations: Fujitsu General looks undervalued

	Market cap (\$bn)	Share price	Target price	Upside	DPS	Yield	PER		PBR		RoE (%)		OPM (%)	
	7/16/13	7/16/13		(%)	FY13E	(%)	FY13E	FY14E	FY13E	FY14E	FY13E	FY14E	FY13E	FY14E
6755.JP Fujitsu General	1.2	¥1,071	¥1,330	24.2%	12	1.1%	12.2	10.6	2.12	1.81	17.5%	17.1%	6.4%	6.4%
6367.JP Daikin	13.7	¥4,685	¥5,000	6.7%	60	1.3%	18.4	16.1	2.02	1.84	11.0%	11.4%	4.9%	7.0%
6752.JP Panasonic	19.9	¥858	¥930	8.4%	0	0.0%	25.9	17.2	1.43	1.34	5.5%	7.8%	2.3%	3.9%
066570.KR LG	10.4	KRW71K	KRW78K	9.9%	200	0.3%	13.9	9.6	0.93	0.84	6.7%	8.8%	1.8%	2.0%
1169.HK Haier	4.3	CNY13.02	CNY15.70	20.6%	0.10	0.8%	16.3	13.9	4.32	3.29	26.5%	23.6%	3.6%	4.0%
ELUXb.SE Electrolux	8.0	SEK176.6	SEK200.0	13.3%	7.25	4.1%	17.6	11.8	3.28	3.08	18.6%	26.1%	3.7%	3.8%
ARCLK.TR Arcelik	4.8	TRY13.60	TRY13.60	0.0%	0.51	3.8%	13.2	11.5	2.19	1.98	16.6%	17.2%	6.6%	7.5%
Appliance Avg.							19.3	14.2	1.98	1.78				

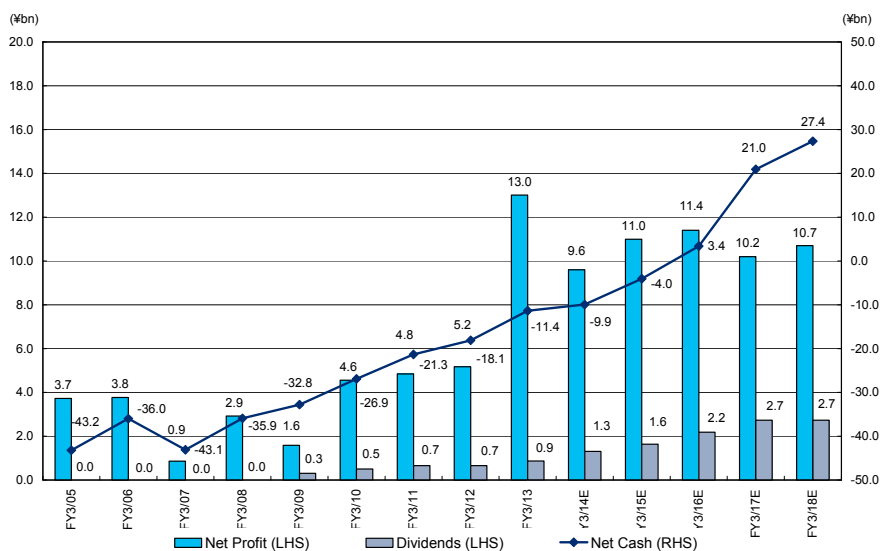
Source: Company data, Citi Research.

Figure 4. DCF model suggests long-term growth potential has not been priced in fully (¥mn)

	FY13E	FY14E	FY15E	FY16E	FY17E
NOPAT	10,695	12,075	12,420	11,040	11,385
Depreciation	4,000	4,500	5,000	5,000	5,000
Capex	-10,000	-5,000	-5,000	-5,000	-5,000
Working capital	-1,163	-3,272	-2,072	9,781	-1,870
FCF	3,532	8,303	10,348	20,821	9,515
WACC	6.6%				
Discount years	1	2	3	4	5
Discount ratio	1.07	1.14	1.21	1.29	1.38
Discounted FCF	3,313	7,304	8,537	16,109	6,904
DCF valuation					
Sum of NPV FCF	42,166				
Terminal value	104,224				
Net cash	-11,366				
Equity value	135,024				
Equity value per share (¥)	1,238				

Source: Company data, Citi Research.

Figure 5. NP, total dividends, and net cash: We expect shareholder returns to increase



Source: Company data, Citi Research.

Key investment points

Two core businesses: air-conditioners and wireless systems

Fujitsu General's core businesses are 1) air-conditioners, mainly domestic and overseas residential-use air-conditioners; and 2) IT& devices, mainly solutions for restaurants, hospitals, and agricultural businesses and wireless fire/disaster prevention systems. The air-conditioner business is positioned as the growth driver, and the telecom/electronic devices business as the cash cow (growth potential is not high, but earnings from domestic business users are stable). That said, since FY3/13 the IT & devices business has benefited from extraordinary demand for fire emergency wireless systems generated by digitization, and we forecast this will continue until FY3/16.

Weakening yen a concern

A feature of Fujitsu General's business is the import into Japan of air-conditioners made in China and Thailand. OP is hurt by the yen weakening or emerging market currencies strengthening. Below we explain our outlook for the three main earnings drivers.

- 1) **Earnings forecasts for the air-conditioner business, the long-term growth driver**
- 2) **Forex earnings impact**
- 3) **Earnings forecasts for the IT & devices business, which is benefits from special demand for fire emergency wireless systems**

1) Strong growth potential in AC business

Fujitsu General sells air-conditioners around the world; earnings have grown in Japan and overseas

Fujitsu General began strengthening its air-conditioner business around 2000 and domestic and overseas earnings have expanded (Figure 6). The FY3/13 air-conditioner sales breakdown by region was: Japan 28%, Europe 16%, the Americas 11%, Oceania 11%, Middle East/Africa 20%, and China/Asia 14%. This shows Fuji General sells air-conditioners in almost all regions. Average sales growth for the last 10 years is 5%. Topline growth has been maintained despite a strong yen and the operating margin has remained stable at 4%–5%.

Fujitsu well positioned to benefit from air-conditioner market growth

We expect demand for air-conditioners to expand in both developed and developing economies (please see our July 17 report, Home Appliances in a Global Context, for more details). Fujitsu General is highly competitive in the field of room air-conditioners and well positioned to benefit from market growth, in our view.

Strengths: R&D, sales network, and cost competitiveness

Strong product development and sales networks

We highlight product development and sales networks as strengths that have supported air-conditioner earnings growth. The market for household appliance, including air-conditioners, is fragmented by lifestyle, climate, and region. Fujitsu General has used its product development expertise to create a strong product lineup, established solid sales networks in all regions, and strengthened its brand power. We believe these factors have enabled it to grow earnings in a crowded market that includes Panasonic, Daikin, and LG Electronics.

Product development expertise used to create a strong lineup

Excellent energy conservation technologies and a broad lineup are key strengths in the area of product development. Fujitsu General has responded to the needs of different regions: for example, it was the first company to introduce air-conditioners with automatic filter cleaning in Japan, and in the Middle East, it introduced window air-conditioners to counter the dry and dusty climate.

Solid sales networks around the world

Fujitsu General has sales networks around the world and sells air-conditioners in developed and developing economies. The company has a particularly strong

presence in Europe, the Middle East, and Oceania, where its market share (value basis) ranges from just under 10% to almost 20% (Figure 7). Fujitsu General began developing business overseas in the 1970s, and we believe this early start (compared with other Japanese companies) is the reason it has solid sales networks. Local brand strength is also notable.

Concentrated production in Asia and in-house production of key components underpins cost competitiveness

Large air-conditioner production capacity in China and Thailand and the in-house production of motors and compressors underpins strong cost competitiveness. We believe Fujitsu General's efforts to expand production overseas while many Japanese companies kept production predominantly at home has given it an advantage on the cost side. Fujitsu General plans to further reduce CoGS by sharing components and leveraging design and procurement power (value analysis value engineering [VAVE] achieved by strengthening local design capabilities and increasing parts procurement from local companies) and we expect progress on this front.

A degree of success in North America, China, and Asia

Accelerating development in North America, China, and Asia an issue

Slow development in North America, China, and other parts of Asia is an issue, however. This is because duct air-conditioners (which use ducts to control the ventilation of entire buildings) are the mainstream in North America and low-price, energy-inefficient air-conditioners are the mainstream in China and other parts of Asia. Unlike Japan and Europe, energy-efficient room air-conditioners have yet to make significant market penetration in these regions.

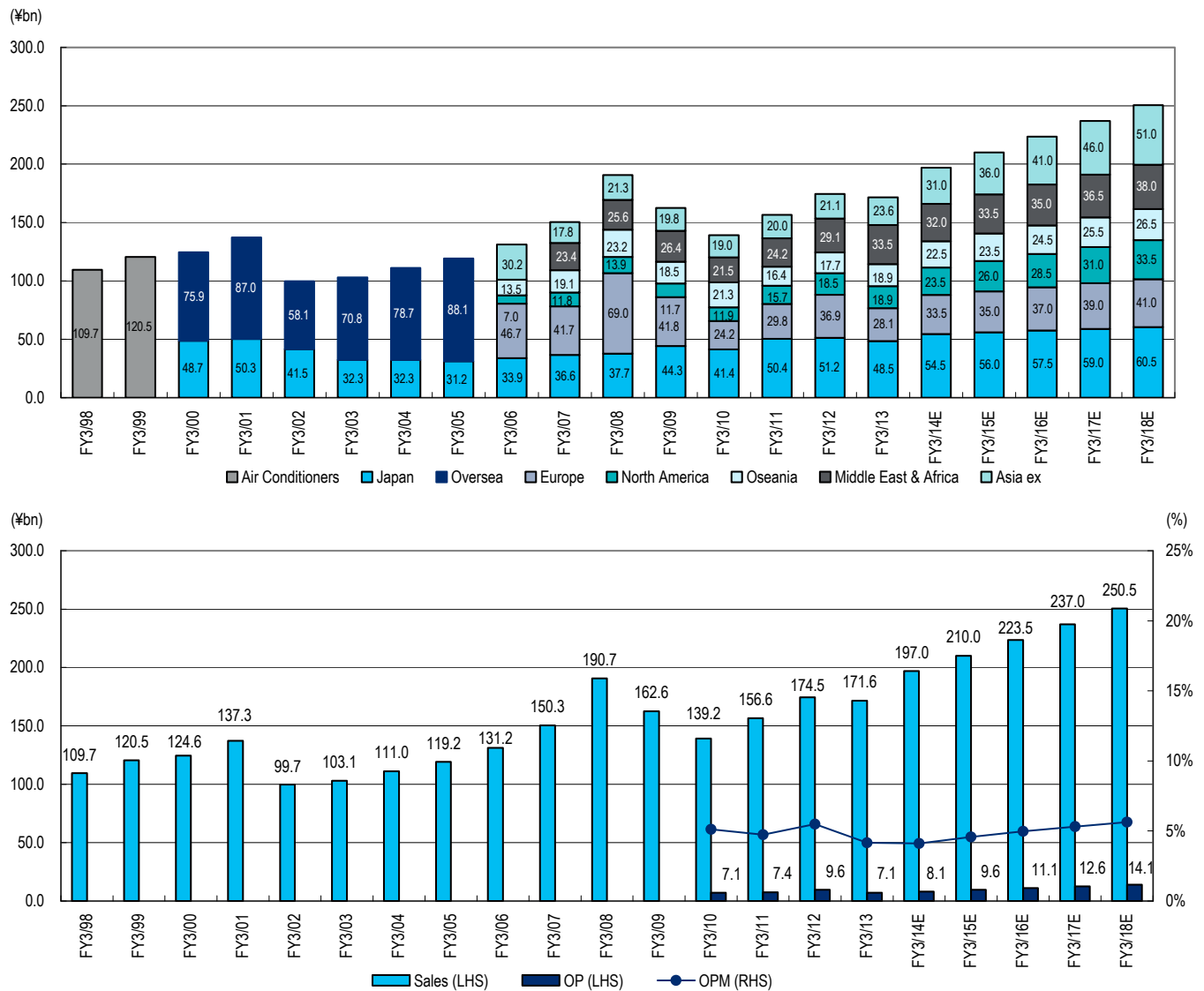
Demand for energy-efficient air-conditioners increasing amid rising environmental awareness

Demand for energy-efficient room air-conditioners in China and the US is increasing as environmental awareness increases. For example, in the US we understand interest is shifting from duct air-conditioners to room air-conditioners for energy-efficiency reasons. China introduced energy-efficiency regulations for air-conditioners in 2005 and since then it has constantly introduced upgraded regulations. This has led to a rapid increase in the weighting of inverter air-conditioner sales. Many developing economies are introducing energy labeling systems, and we expect this still stimulate demand for energy-efficient air-conditioners.

Expanding sales of energy efficient air-conditioners in China and North America reflect some success

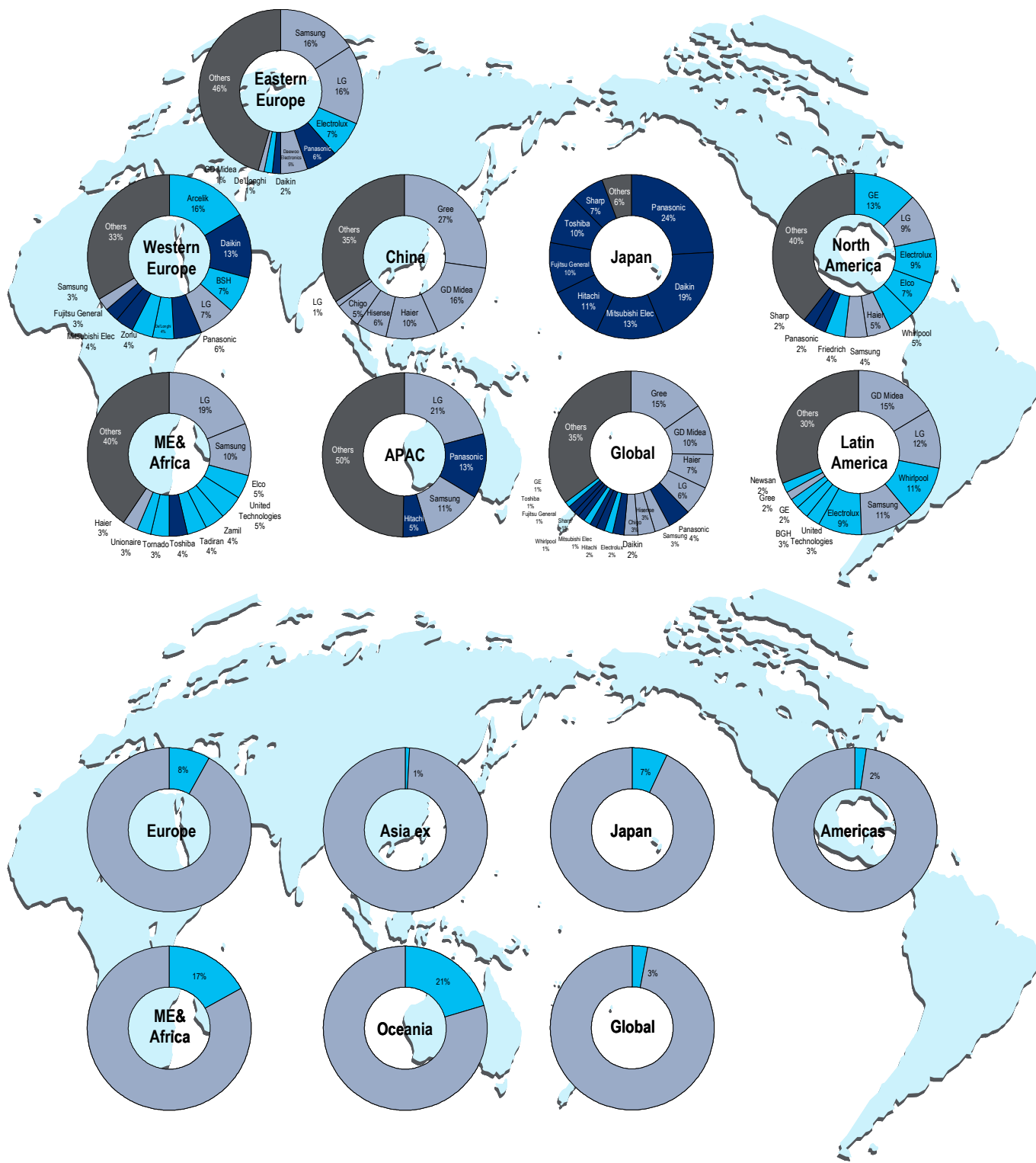
Amid rising awareness of energy-efficient room air-conditioners in North America and China, Fujitsu General aims to cultivate markets by introducing products that meet local specifications. In China, the introduction of locally-designed mass-market inverter air-conditioners and the expansion of sales channels, centering on southern coastal cities, supported sales growth of 40% YoY (local-currency basis) in FY3/13. We see this as evidence that Fujitsu General's efforts are starting to yield rewards.

Figure 6. Air-conditioner sales by region and OP: Growth set to continue, driven by developing markets



Source: Company data, Citi Research.

Figure 7. Air-conditioner market shares by volume (top), Fujitsu General's market share by revenue (bottom, in blue): Fujitsu General has a presence in Japan, Europe, Oceania, and the Middle East/Africa, but needs to establish more of one in China/Asia, North and Latin America



Source: Company data, Euromonitor, JEMA, Citi Research.

2) Impact of forex

Given complicated air-conditioning business trade relationships, it is hard to assess the forex impact

OP forex hit of ¥300mn if yen weakens by ¥1 versus dollar, euro, and Australian dollar collectively

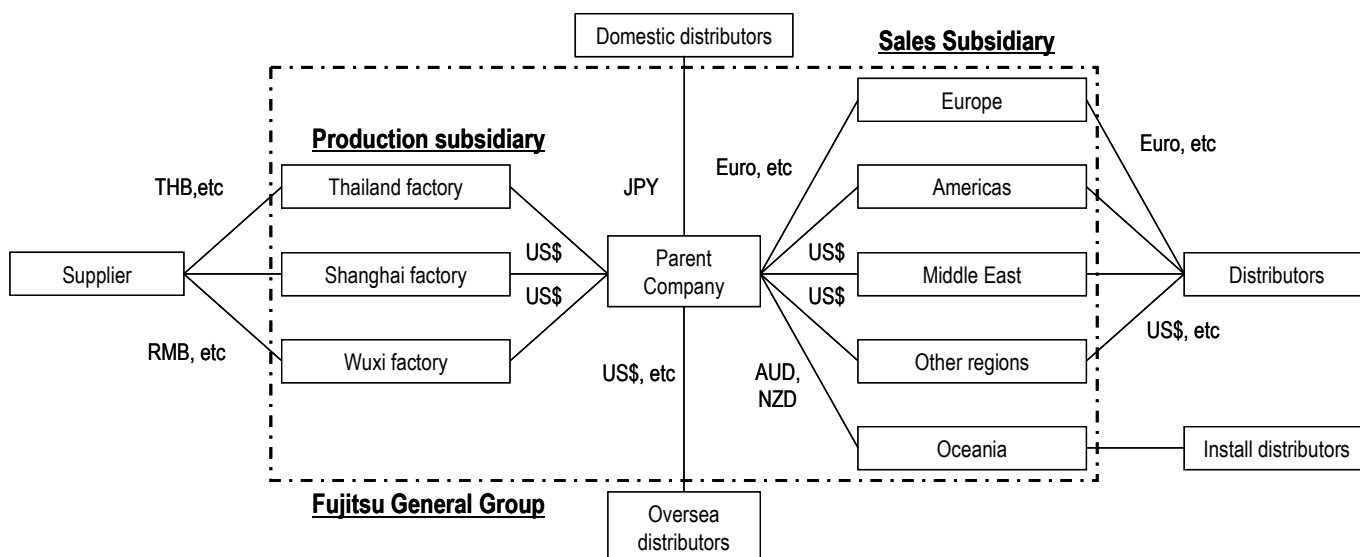
Profit growth trend looks sustainable on input cost cuts and growth overseas

Fujitsu General produces its air-conditioners overseas and then imports them into Japan, so one should keep in mind the fact that yen weakness and/or strength for developing market currencies is negative for OP. The currencies used in sales and production differ by region, so gauging the forex impact is quite complicated (Figure 8). The RMB accounts for a large proportion of production costs, so we think RMB fluctuations have a relatively large impact on OP.

The company's FY3/14 forecasts assume ¥100/\$, ¥130/€, and JPY105/AUD. In FY3/13A, forex rates were ¥85/\$, ¥109/€, and JPY84/AUD. The company estimates that a ¥1 change against the currencies collectively produces a swing of ¥300mn in OP. At the same time, Fujitsu General assumes forex factors will produce a ¥7.9bn hit to profit in FY3/14, but given YoY changes in forex rates (¥15/\$, ¥21/€, JPY21/AUD), we think the company might be being conservative in this assumption.

While it is true that yen weakness is negative for air-conditioner profits, we think the current growth trend for profits is sustainable via progress in input cost-cutting and continued growth overseas. In particular, the company anticipates a ¥5bn boost to profits from cost cuts in FY3/14, and it believes significant cost savings are possible via design revisions and improved productivity at plants as well as due to a sharp improvement in the procurement environment for major air-conditioner components. What is more, the company thinks the air-conditioner product mix will improve in Japan while sales in overseas markets rise, boosting FY3/14 OP by ¥3.9bn. In FY3/15 and out, too, Fujitsu General anticipates sales growth, particularly overseas, so we think profit growth is likely to continue.

Figure 8. Air-conditioner business trade relationships: Relations are complicated, so it is difficult to assess forex impact, but yen weakness and/or strength for developing market currencies tend to be negative for OP



Source: Company data, Citi Research.

3) IT & devices generating stable earnings

IT & devices can generate stable earnings in sales to corporates in Japan

The IT & devices segment consists of the IT and telecom systems unit, which offers a variety of solutions in areas such as wireless systems for firefighting, wireless systems for disaster prevention, restaurants, hospitals, and agriculture, mainly in Japan, and the electronic devices unit, which mainly focuses on automotive cameras, electronic components, and modules. These are all mature markets and growth potential is limited, but the operations focus on demand from domestic corporates, where product performance and quality are imperatives, so we think the segment can generate stable earnings.

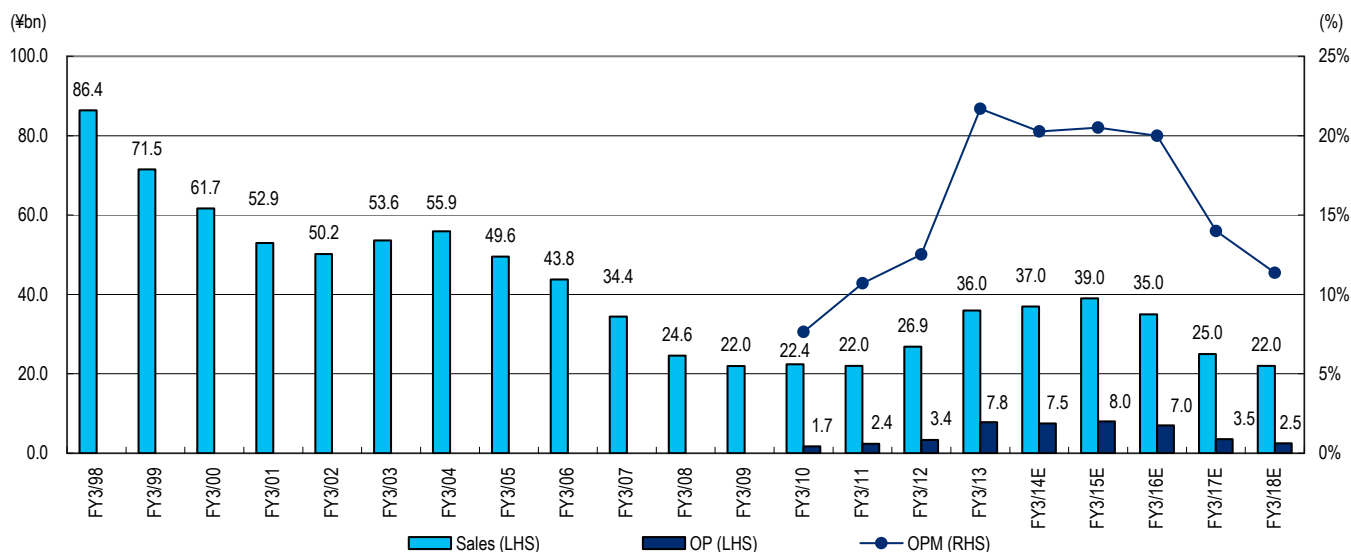
Spike in demand for emergency firefighting wireless from FY3/13

In FY3/13, electronic device unit sales slumped 23% YoY to ¥8.0bn, on lower demand for automotive cameras due to the end of subsidies for eco-cars and lower demand for industrial electronic components. In contrast, sales in the IT and telecom systems unit surged 71% to ¥27.9bn. This is because of legislation that mandates that emergency firefighting wireless system reception be shifted to digital by May 2016, resulting in a spike in demand from around 2012.

The spike in demand will no longer contribute from FY3/17 but even so we think the unit can generate a certain level of profits

Through FY3/16, we think the IT and telecom systems unit can maintain earnings on par with FY3/13 (sales of ¥36.0bn, OP of ¥7.8bn), mainly thanks to the spike in demand resulting from the digital shift in emergency firefighting wireless systems. We forecast that from FY3/17, revenues and earnings will trend lower for a while on the end to the demand spike. However, we think the core operations can generate a certain level of profits, as stable earnings in Japan look feasible, and in electronic devices, Fujitsu General is carving out new demand in areas such as power conditioners, so we conclude that it will be able to generate a certain level of profits. We think that longer term, it can maintain earnings on par with FY3/11, before the spike in demand from the shift to digital (sales of ¥22.0bn, OP of ¥2.4bn). See Figure 9 below.

Figure 9. IT & devices segment outlook: Should be able to maintain stable profits even after the spike in demand for emergency firefighting wireless systems that began in FY3/13 peters out



Source: Company data, Citi Research.

History

Success with early restructuring

Fujitsu General was an integrated consumer electronics maker but went through protracted trials and tribulations

We think that one of the sources of Fujitsu General's appeal lies in the way it succeeded in restructuring earlier than other Japanese electronics makers. It is a long established electrical equipment manufacturer, having been founded in 1936, and from the 1950s to the 1970s it was an integrated electronics maker, manufacturing and selling TVs, refrigerators, washing machines, air-conditioners, and calculators. However, operations deteriorated in the 1980s, as domestic demand became saturated, the yen strengthened, and competition between consumer electronics makers grew fiercer. It came under the auspices of the Fujitsu group via a capital and operational tie-up with Fujitsu and the company name changed to Fujitsu General in 1985. It displayed something of a presence in the market in the 1990s, producing subcontracted Fujitsu brand PCs and selling the world's first PDP TV, but earnings were unstable and it booked a net loss of over ¥10bn in FY3/02 on weak demand for air-conditioners.

Fujitsu General pushed restructuring in the first decade of this century

Fujitsu General pushed restructuring in the first decade of this century in response to earnings deterioration. The main planks of restructuring were the winding up or shrinking of unprofitable businesses, such as PDP TVs, refrigerators, and unprofitable models in the electronic device business and at the same time the making of aggressive upfront investments in mainstay air-conditioners. In a bid to boost earnings power, Fujitsu General slimmed back-office divisions, concentrated production facilities in China and Thailand, and bolstered supply-chain management. As a result, losses in unprofitable businesses shrank and the mainstay air-conditioner business expanded, with the consequence that earnings have been improving since the second half of the last decade.

A role model for the revival of Japan's electronics industry

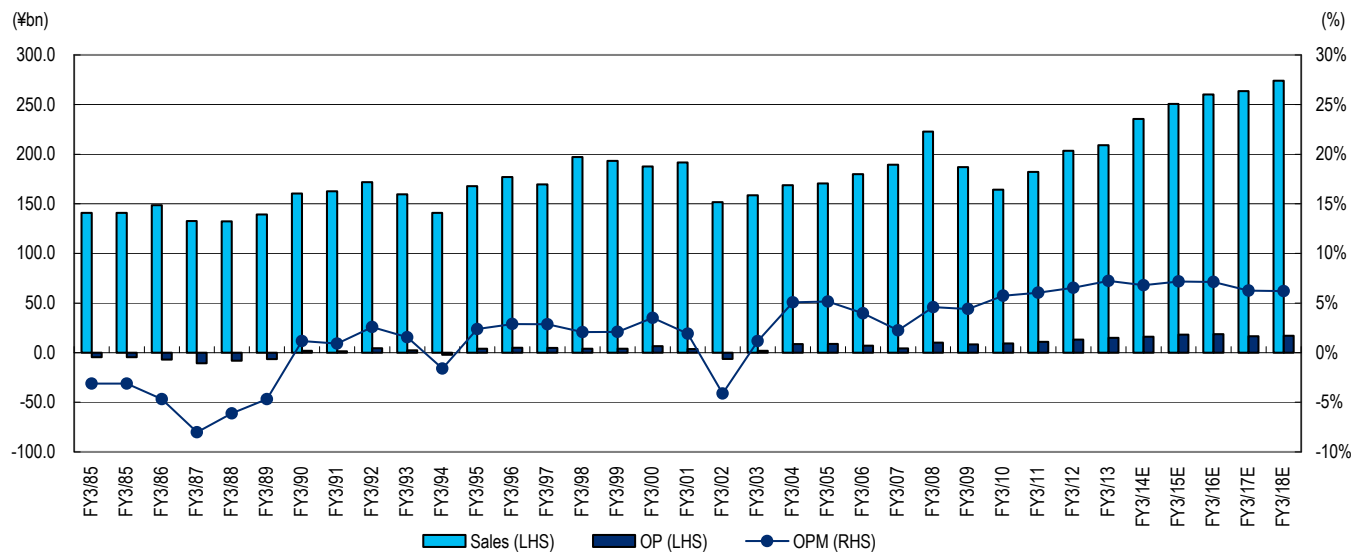
Japan's electronics industry is currently in the midst of restructuring, with firms working to restructure by shrinking losses in areas where their earnings power has ebbed, such as "black goods" (FPD TVs and mobile phones), semiconductors, and LCD displays, and by growing earnings in core businesses such as household appliances and social infrastructure. By withdrawing from unprofitable units such as FPD TVs and refrigerators and focusing on air-conditioners, where it was competitive, Fujitsu General succeeded in restructuring ahead of other firms and in a sense, we feel that it is a role model for the revival of the Japanese electronics industry.

Figure 10. Fujitsu General: Has been restructuring since the last decade by withdrawing from unprofitable businesses and concentrating investment in the core business

Date	Major events
Before WWII	Established as Yao Shoten by Keijiro Yao in 1936 to manufacture and market gramophones. Moved subsequently to manufacture radios, wireless equipment, measuring equipment, etc.
1950s	Began manufacturing and marketing TVs and washing machines
1960s	Began manufacturing and marketing wind-type coolers, refrigerators, calculators, etc. Company name changed to General Ltd. in 1966
1970s	Established sales subsidiaries in the US, Europe, Australia, Brazil etc, as overseas expansion moved into full swing
1984	Financial difficulties led to a capital and business tie-up with Fujitsu and the company became part of the Fujitsu Group. Company name changed to Fujitsu General in 1985
1991	Established air-conditioner manufacturing subsidiary in Thailand
1993	Established air-conditioner manufacturing subsidiary in China. Launched the world's first PDP TV
1997	Established air-conditioner manufacturing subsidiary in Thailand
2001	Instigated reorganization of operations after sluggish air-conditioner sales in Japan and Europe led to an operating loss in FY3/02. Production of air-conditioners became concentrated in Thailand and China. Weeded out unprofitable electronic device models
2002	Streamlined back-office and administrative functions
2003	Withdrew from the refrigeration business. Established a motor manufacturing JV company in China
2005	Restructured the domestic air-conditioner sales system. Established a VRF manufacturing and marketing JV company in China
2007	Withdrew from the home theatre projector business. Made the VRF manufacturing and marketing JV company in China a wholly owned subsidiary
2008	Transferred shares in its system development subsidiary to Fujitsu. Construction of a new VRF plant in China completed
2009	Construction of new compressor plant in Thailand completed. Completed construction of a new consumer appliance recycling plant in Hamamatsu
2011	Transferred part of the mass production design department from Kawasaki to China
2012	Constructed a new Fujitsu General Electronics plant. Established a compressor manufacturing JV company with Toshiba Carrier

Source: Company data, Citi Research.

Figure 11. Fujitsu General: Had a protracted struggle as an integrated consumer electronics manufacturer but earnings have been improving since last decade thanks to restructuring



Source: Company data, Citi Research.

Earnings forecasts

Our OP estimates: From ¥15.1bn in FY3/13A to ¥16.0bn in FY3/14, ¥18.0bn in FY3/15, ¥18.5bn in FY3/16, ¥16.5bn in FY3/17, ¥17.0bn in FY3/18

Following OP of ¥15.1bn in FY3/13, we look for OP of ¥16.0bn in FY3/14, ¥18.0bn in FY3/15, ¥18.5bn in FY3/16, ¥16.5bn in FY3/17, and ¥17.0bn in FY3/18 (Figure 12 and Figure 13). We assume profit will decline YoY in FY3/17, as extraordinary demand for digital wireless disaster prevention systems tapers off, but we expect the profit growth trend to continue thereafter on growth in air-conditioner earnings.

We forecast sustained growth in air-conditioner earnings

We forecast sustained growth in sales in the air-conditioner business, based on current earnings trends and assuming a stable share of the air-conditioner market. In FY3/14, we expect domestic sales to continue higher as in addition to the weakening of the yen, we also foresee sales mix improvements in Japan and domestic market share growth. We forecast further YoY sales growth in FY3/14 too in Europe as the ending of inventory adjustments leads to an increase in demand. We see a similar trend in North America and China, where we expect the company to capture demand and grow sales of room air-conditioners. We forecast overall FY3/14 air-conditioner segment sales of ¥197.0bn, up from ¥171.6bn in FY3/13.

Yen weakening a concern, but we believe profit growth is possible on sales growth and cost-cutting

While yen weakening is a concern, we think air-conditioner OP can rise to ¥8.1bn in FY3/14 from ¥7.1bn in FY3/13, on sales growth and cost-cutting progress. The company has said that procurement conditions for key raw materials have improved considerably in FY3/14 and scope for cost reductions is greater than usual. With major rivals cutting back on procurement volumes due to the slowdown in the Chinese market, we understand Fujitsu General has been able to source components and materials on more favorable terms than before. From FY3/15 too, we think the uptrend in sales in profit will continue on sustained growth in the overall air-conditioner market and ongoing cost-cutting.

IT & devices segment to continue to make a steady earnings contribution even after demand spike subsides

We expect earnings levels in the IT & devices segment to remain high through FY3/16 on extraordinary demand for wireless disaster prevention systems. We expect a temporary drop in profit from FY3/17, as extraordinary demand dries up, but we still expect the business to continue to make a steady contribution to overall profit stemming from domestic corporate systems and electronic devices.

Q1 preview

We forecast Q1 OP of ¥1.5bn. We expect seasonal factors to keep earnings levels in the IT & devices segment low in Q1, as orders are driven primarily by government and public agencies. Meanwhile, in air-conditioners, we forecast a steep YoY drop in profit owing to the weak yen. But from June to July, air-conditioner demand tends to fluctuate sharply depending on weather conditions, and so it should be noted that quarterly earnings can vary greatly. While we expect the weak yen to trigger a drop in profits in H1, we believe the company's targets are attainable.

Guidance has been reliable

Our ¥16.0bn FY3/14 OP forecast is in line with guidance. We believe the company's projections are reliable, as over the past number of years, excluding the post-Lehman global financial crisis era, it has met its targets, and guidance tends to be based on realistic assumptions.

Figure 12. Fujitsu General: Income statement

(¥mn)	3/13 Q1A	Q2A	Q3A	Q4A	3/14 Q1E	Q2E	Q3E	Q4E	3/11 FYA	3/12 FYA	3/13 FYA	3/14 FYE	3/15 FYE	3/16 FYE	3/17 FYE	3/18 FYE
Sales	47,412	48,359	36,832	76,564	50,900	53,900	49,900	80,900	182,105	203,549	209,167	235,600	250,600	260,100	263,600	274,100
QoQ (%)	-21.8%	2.0%	-23.8%	107.9%	-33.5%	5.9%	-7.4%	62.1%	10.9%	11.8%	2.8%	12.6%	6.4%	3.8%	1.3%	4.0%
YoY (%)	-19.8%	-1.2%	5.6%	26.3%	7.4%	11.5%	35.5%	5.7%	10.9%	11.8%	2.8%	12.6%	6.4%	3.8%	1.3%	4.0%
Operating Income	4,588	2,213	-451	8,770	1,500	1,800	1,400	11,300	11,029	13,318	15,120	16,000	18,000	18,500	16,500	17,000
YoY (%)	-28.8%	13.0%	nm	67.4%	-67.3%	-18.6%	nm	28.8%	16.9%	20.8%	13.5%	5.8%	12.5%	2.8%	-10.8%	3.0%
Operating margin	9.7%	4.6%	-1.2%	11.5%	2.9%	3.3%	2.8%	14.0%	6.1%	6.5%	7.2%	6.8%	7.2%	7.1%	6.3%	6.2%
Recurring Income	4,558	2,244	2,295	10,463	1,200	1,500	1,100	10,500	7,466	9,385	19,560	14,300	16,400	17,000	15,200	15,900
Income taxes	939	1,304	715	3,296	400	400	300	3,300	2,185	3,906	6,254	4,400	5,100	5,300	4,700	4,900
Effective tax rate	20.6%	58.1%	31.1%	31.5%	33.3%	26.7%	27.3%	31.4%	29.3%	41.6%	32.0%	30.8%	31.1%	31.2%	30.9%	30.8%
Net Income	3,541	913	1,601	6,954	750	1,050	750	7,050	4,848	5,174	13,009	9,600	11,000	11,400	10,200	10,700
R&D expenses	2,256	2,424	2,453	2,671	2,750	2,750	2,750	2,750	7,761	8,546	9,804	11,000	11,000	11,000	11,000	11,000
% of sales	4.8%	5.0%	6.7%	3.5%	5.4%	5.1%	5.5%	3.4%	4.3%	4.2%	4.7%	4.7%	4.4%	4.2%	4.2%	4.0%
Depreciation	797	803	829	890	950	950	1,050	1,050	3,546	3,246	3,319	4,000	4,500	5,000	5,000	5,000
Capital expenditure	263	906	616	1,390	2,500	2,500	2,500	2,500	2,391	3,122	3,175	10,000	5,000	5,000	5,000	5,000
Cash flow	4,338	1,716	2,430	7,844	1,700	2,000	1,800	8,100	8,394	8,420	16,328	13,600	15,500	16,400	15,200	15,700
Free cash flow	4,075	810	1,814	6,454	-800	-500	-700	5,600	6,003	5,298	13,153	3,600	10,500	11,400	10,200	10,700

Source: Company data, Citi Research.

Figure 13. Fujitsu General: Sales and OP by segment

(¥mn)	3/13 Q1A	Q2A	Q3A	Q4A	3/14 Q1E	Q2E	Q3E	Q4E	3/11 FYA	3/12 FYA	3/13 FYA	3/14 FYE	3/15 FYE	3/16 FYE	3/17 FYE	3/18 FYE
Sales																
Air-conditioners	42,323	39,586	30,272	59,385	46,000	44,000	43,000	64,000	156,562	174,535	171,566	197,000	210,000	223,500	237,000	250,500
Japan	16,043	14,072	8,379	9,999	16,500	15,500	11,000	11,500	50,399	51,212	48,493	54,500	56,000	57,500	59,000	60,500
Oversea	26,280	25,514	21,893	49,386	29,500	28,500	32,000	52,500	106,163	123,323	123,073	142,500	154,000	166,000	178,000	190,000
Europe	5,576	5,805	3,076	13,686	7,500	7,500	6,000	12,500	29,831	36,920	28,143	33,500	35,000	37,000	39,000	41,000
Americas	4,283	3,833	2,247	8,560	5,000	4,500	4,000	10,000	15,740	18,531	18,923	23,500	26,000	28,500	31,000	33,500
Oceania	2,595	5,721	3,662	6,905	4,000	6,000	5,000	7,500	16,366	17,705	18,883	22,500	23,500	24,500	25,500	26,500
Middle East & Africa	7,718	5,545	7,356	12,858	5,500	4,000	9,000	13,500	24,188	29,081	33,477	32,000	33,500	35,000	36,500	38,000
Other region	6,108	4,610	5,552	7,377	7,500	6,500	8,000	9,000	20,038	21,086	23,647	31,000	36,000	41,000	46,000	51,000
IT & Devices	4,677	8,320	6,147	16,820	4,500	9,500	6,500	16,500	22,006	26,856	35,964	37,000	39,000	35,000	25,000	22,000
IT Systems	2,264	6,191	4,585	14,886	2,400	7,400	4,400	14,300	11,341	16,379	27,926	28,500	30,500	26,500	16,500	13,500
Electronic devices	2,413	2,128	1,561	1,936	2,100	2,100	2,100	2,200	10,664	10,476	8,038	8,500	8,500	8,500	8,500	8,500
Others	411	453	412	360	400	400	400	400	3,536	2,157	1,636	1,600	1,600	1,600	1,600	1,600
Total	47,411	48,359	36,831	76,565	50,900	53,900	49,900	80,900	182,104	203,548	209,166	235,600	250,600	260,100	263,600	274,100
YoY																
Air-conditioners	-21.2%	-4.9%	2.1%	19.9%	8.7%	11.2%	42.0%	7.8%	12.5%	11.5%	-1.7%	14.8%	6.6%	6.4%	6.0%	5.7%
IT & Devices	-0.6%	25.6%	28.2%	56.7%	-3.8%	14.2%	5.7%	-1.9%	-1.7%	22.0%	33.9%	2.9%	5.4%	-10.3%	-28.6%	-12.0%
Others	-38.6%	-33.8%	-2.6%	-5.5%	-2.7%	-11.7%	-2.9%	11.1%	36.5%	-39.0%	-24.2%	-2.2%	0.0%	0.0%	0.0%	0.0%
Total	-19.8%	-1.2%	5.6%	26.3%	7.4%	11.5%	35.5%	5.7%	10.9%	11.8%	2.8%	12.6%	6.4%	3.8%	1.3%	4.0%
OP																
Air-conditioners	4,214	658	-1,530	3,793	1,100	500	300	6,200	7,416	9,586	7,135	8,100	9,600	11,100	12,600	14,100
IT & Devices	273	1,416	969	5,145	300	1,200	1,000	5,000	2,357	3,361	7,803	7,500	8,000	7,000	3,500	2,500
Others	100	139	109	-167	100	100	100	100	1,255	370	181	400	400	400	400	400
Total	4,587	2,213	-452	8,771	1,500	1,800	1,400	11,300	11,028	13,317	15,119	16,000	18,000	18,500	16,500	17,000
OPM																
Air-conditioners	10.0%	1.7%	-5.1%	6.4%	2.4%	1.1%	0.7%	9.7%	4.7%	5.5%	4.2%	4.1%	4.6%	5.0%	5.3%	5.6%
IT & Devices	5.8%	17.0%	15.8%	30.6%	6.7%	12.6%	15.4%	30.3%	10.7%	12.5%	21.7%	20.3%	20.5%	20.0%	14.0%	11.4%
Others	24.3%	30.7%	26.5%	-46.4%	25.0%	25.0%	25.0%	25.0%	35.5%	17.2%	11.1%	25.0%	25.0%	25.0%	25.0%	25.0%
Total	9.7%	4.6%	-1.2%	11.5%	2.9%	3.3%	2.8%	14.0%	6.1%	6.5%	7.2%	6.8%	7.2%	7.1%	6.3%	6.2%

Source: Company data, Citi Research.

Figure 14. Fujitsu General: Balance sheet and cash flow statements

(¥mn)	3/11 FYA	3/12 FYA	3/13 FYA	3/14 FYE	3/15 FYE	3/16 FYE	3/17 FYE	3/18 FYE
Balance sheet								
Current Assets	82,497	82,843	109,005	116,615	123,628	129,951	133,389	142,492
Cash & Cash Equivalents	5,709	4,639	5,935	7,363	8,256	10,703	23,257	28,496
Notes and Accounts Receivable	47,583	53,621	75,719	80,104	85,204	88,434	79,080	82,230
Inventories	18,973	15,347	14,223	16,021	17,041	17,687	17,925	18,639
Other Current Assets	10,231	9,235	13,127	13,127	13,127	13,127	13,127	13,127
Fixed Assets	37,905	38,642	40,176	46,176	46,676	46,676	46,676	46,676
Tangible Assets	29,277	28,889	29,151	35,151	35,651	35,651	35,651	35,651
Intangible Assets	2,071	2,162	2,155	2,155	2,155	2,155	2,155	2,155
Investments in Securities	1,631	2,008	3,545	3,545	3,545	3,545	3,545	3,545
Other Fixed Assets	4,925	5,582	5,324	5,324	5,324	5,324	5,324	5,324
Total Assets	120,402	121,486	149,182	162,793	170,306	176,629	180,067	189,169
Current Liabilities	64,810	67,407	84,275	89,295	87,143	83,947	79,612	80,441
Notes and Accounts Payable	34,544	30,295	39,720	44,740	47,588	49,392	50,057	52,051
Short-term Borrowings	15,212	17,525	16,165	16,165	11,165	6,165	1,165	0
Other Current Liabilities	15,054	19,587	28,390	28,390	28,390	28,390	28,390	28,390
Fixed Liabilities	26,118	19,351	16,403	16,403	16,403	16,403	16,403	16,403
Long-term Debts	11,817	5,201	1,135	1,135	1,135	1,135	1,135	1,135
Other Fixed Liabilities	14,301	14,150	15,268	15,268	15,268	15,268	15,268	15,268
Total Liabilities	90,929	86,759	100,679	105,698	103,547	100,351	96,015	96,844
Minority Interests	1,742	1,643	1,794	2,094	2,394	2,694	2,994	3,294
Shareholders' equity	27,310	31,833	43,967	52,259	61,623	70,842	78,316	86,289
Total Net Assets	29,472	34,727	48,503	57,095	66,759	76,278	84,052	92,325
Liabilities & Net Assets	120,402	121,486	149,182	162,793	170,306	176,629	180,067	189,169
Cash flow statement								
Cash Flow from Operating Activities								
Net Income	4,848	5,174	13,009	9,600	11,000	11,400	10,200	10,700
Depreciation	3,442	3,182	3,275	4,000	4,500	5,000	5,000	5,000
Increase or Decrease in Working Capital	1,103	-6,665	-9,206	-1,163	-3,272	-2,072	9,781	-1,870
Other	381	6,149	4,240	300	300	300	300	300
Total	9,774	7,841	11,318	12,737	12,528	14,628	25,281	14,130
Cash Flow from Investment Activities								
Capital Expenditure	-3,981	-2,229	-2,373	-10,000	-5,000	-5,000	-5,000	-5,000
Other	538	-870	-523	0	0	0	0	0
Total	-3,443	-3,099	-2,896	-10,000	-5,000	-5,000	-5,000	-5,000
Cash Flow from Financial Activities								
Increase or Decrease in Interest-bearing debt	-4,716	-4,412	-6,340	0	-5,000	-5,000	-5,000	-1,165
Increase or Decrease in Capital & Legal Reserve	0	0	0	0	0	0	0	0
Dividends	-651	-651	-869	-1,309	-1,636	-2,181	-2,726	-2,726
Others	-444	-462	-430	0	0	0	0	0
Total	-5,811	-5,525	-7,639	-1,309	-6,636	-7,181	-7,726	-3,892
Effect of Change in Exchange Rate on Cash & Cash Equivalents	-234	-285	513	0	0	0	0	0
Net Increase or Decrease of Cash	284	-1,069	1,296	1,429	893	2,447	12,554	5,238
Net Increase or Decrease of Cash by New Consolidation	0	0	0	0	0	0	0	0
Cash & Cash Equivalents at the Beginning of the Term	5,424	5,709	4,639	5,935	7,363	8,256	10,703	23,257
Cash & Cash Equivalents at the Term End	5,709	4,639	5,935	7,363	8,256	10,703	23,257	28,496

Source: Company data, Citi Research.

Fujitsu General

Investment strategy

We initiate coverage of Fujitsu General with a Buy (1) rating and a ¥1,330 target price. We do so because 1) we see substantial growth potential, particularly in emerging economies, for mainstay room air-conditioners, and 2) IT & electronic device earnings are steady and wireless emergency management systems are benefitting from extraordinary demand. The shares look undervalued on an FY3/14E PER of 12x and FY3/15E PER of 11x.

The mainstay air-conditioner business boasts a strong product line-up backed by leading technology as well as global sales channels, and with continued growth both in Japan and overseas Fujitsu General looks like an unheralded blue-chip. We see air-conditioners as a growth industry with expansion likely in both developed and developing markets. As Fujitsu General is highly competitive in room air-conditioners we think it is well-positioned to benefit from market expansion.

Since the 2000s it has moved forward with restructuring, such as withdrawing from unprofitable businesses like PDP TVs and refrigerators and focusing management resources on the growing air-conditioner business. Japan's electronics firms are in the midst of restructuring at present, but as Fujitsu General restructured ahead of its peers we see it as a role model for the revival of Japan's electronic equipment industry.

Valuation

Our ¥1,330 target price is based on a DCF-derived theoretical price, and we also reference the average PER for global household appliance majors.

Our DCF-based theoretical price assumes a risk-free rate of 1%, an equity premium of 6%, a terminal growth rate of 0%, a beta of 1.1, and a tax rate of 30%, resulting in WACC of 6.6%. We also use earnings forecasts for FY3/14-FY3/18. The theoretical price derived from this is ¥1,240. Applying a PER of 14x (the average for global household appliance firms) to our FY3/15 EPS forecast of ¥101 results in a theoretical share price of ¥1,410.

In light of the theoretical prices we derive we set our target price at ¥1,330.

Risks

Risks to our target price include 1) weak demand for air-conditioners due to a global economic slowdown, 2) a decline in sales share in Japan and overseas, 3) an increase in marketing costs due to a rise in competition over sales; 4) a rise in costs via higher material prices, 5) lower earnings due to continued yen weakening, and 6) a shift to other cyclical stocks due to economic recovery. As Fujitsu General manufactures air-conditioners overseas and imports them into Japan, one should keep in mind that yen weakness and/or strength for developing market currencies is negative for OP.

Appendix A-1

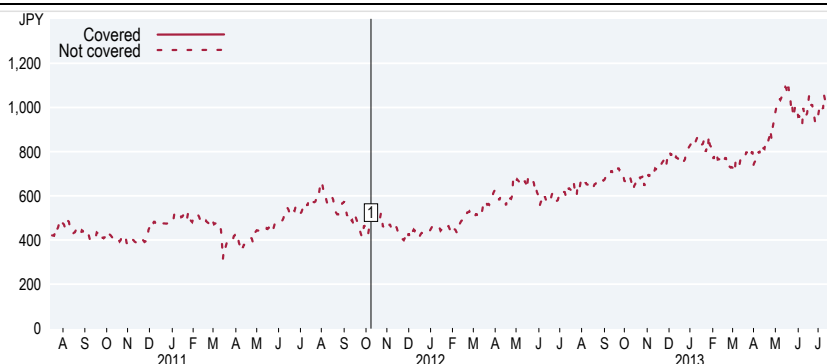
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IMPORTANT DISCLOSURES

Fujitsu General (6755)

Ratings and Target Price History
Fundamental Research



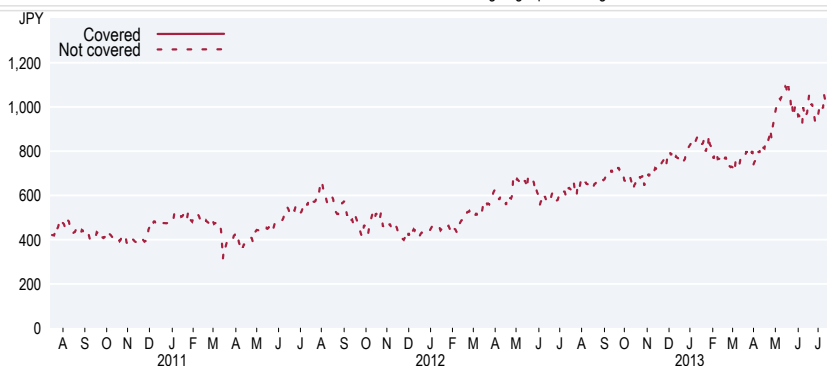
	Date	Rating	Target Price	Closing Price
1	8-Oct-11	Stock rating system changed		

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

Fujitsu General (6755)

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



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