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Japan's first listed pachinko hall operator, after listing in Hong Kong

Dynam Japan Holdings is the top operator of pachinko and pachinko slot (pachislot) halls in Japan in terms of the number of halls operated and the second largest operator in terms of operating revenue. In August 2012, it became Japan's first operator of pachinko halls to list its shares, doing so on the Hong Kong Stock Exchange.

The operating environment for the pachinko/pachislot hall industry in Japan is challenging, but the company is aggressively opening new halls to grow while maintaining high profitability through merits of scale. By the end of the fiscal year ending in March 2023, i.e., by the end of FY3/23, the company aims to have 1,000 halls in operation and to hold a 10% share of the Japanese market.

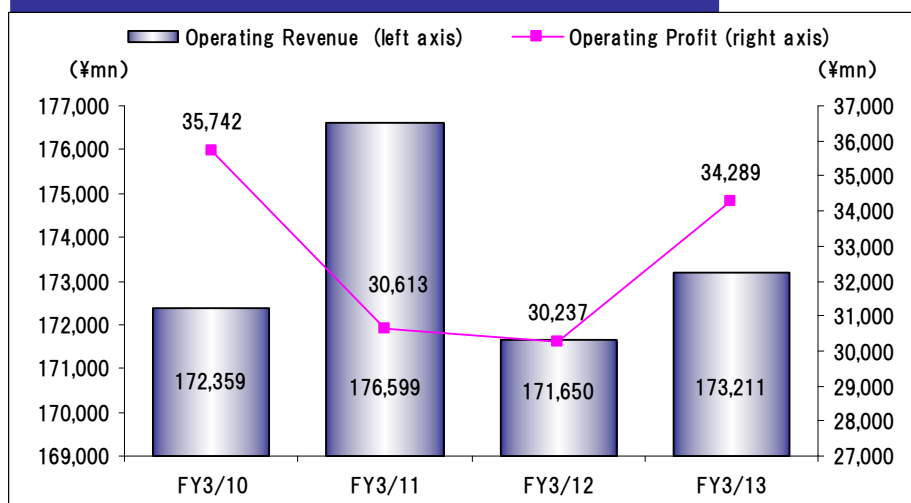
The company may be able to achieve this goal because of its efficient management based on chain store management. Impressed by the distribution revolution in Japan several years ago, the company's top manager successfully applied chain store management principles to the operation of pachinko/pachislot halls.

Success in the pachinko hall industry depends on many factors, including the opening of new halls, the provision of pachinko machines with low playing cost, the introduction of private brands of pachinko machines, and the introduction of personal systems. The company therefore has many options to pursue growth in a shrinking industry.

Check Points

- The top operator of pachinko and pachislot halls in Japan in terms of the number of halls operated
- The company targets 1,000 halls in operation and a 10% market share in 10 years
- It intends to raise its dividend payout ratio to 45-50%, indicating its concern for shareholder returns

Operating Revenue and Operating Profit, FY3/10-FY3/13



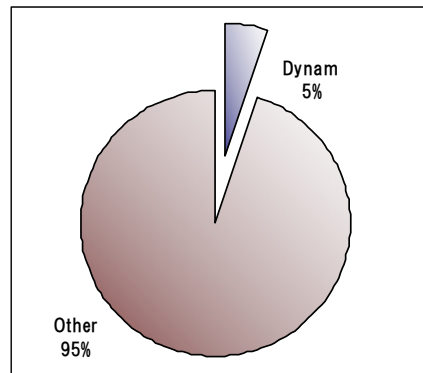
Company Overview

The top operator of pachinko and pachislot halls in Japan in terms of the number of halls operated

Description

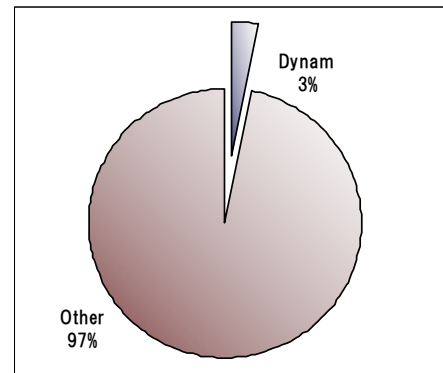
At the end of September 2013, Dynam Japan Holdings operated 363 pachinko and/or pachislot halls in Japan, the highest number of any operator. In FY3/13, the company's revenue from renting pachinko balls and pachislot tokens totaled ¥929.2bn, which was the second largest such revenue in the industry, behind Maruhan. This revenue is also called gross revenue. Dynam Japan Holdings is the only listed Japanese operator of pachinko halls. Its shares are listed on the Hong Kong Stock Exchange.

Share of the Japanese Pachinko Hall Market in Terms of Ball or Token Rental Revenue in FY3/13



Sources: Company, Leisure White Paper by the Japan Productivity Center

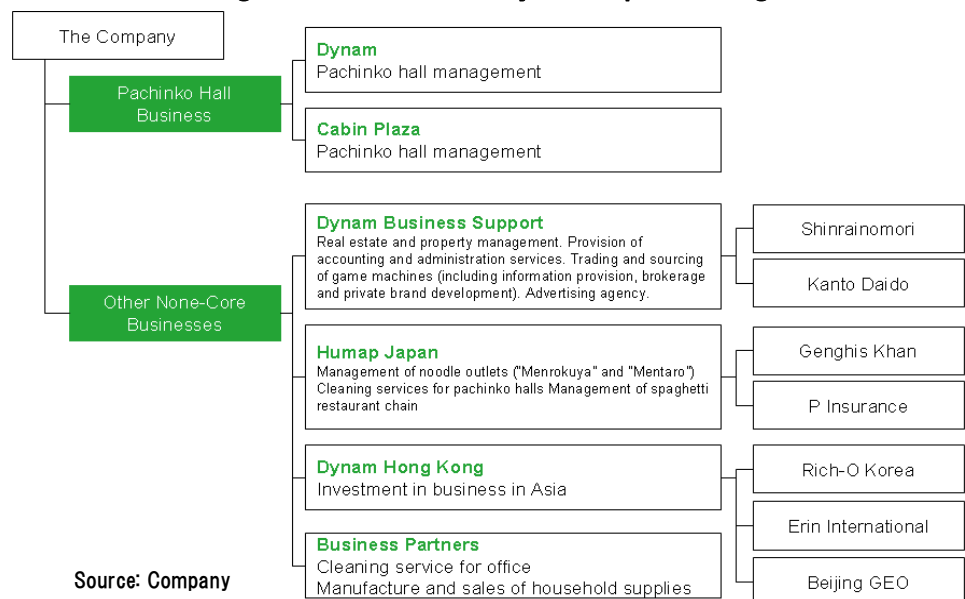
Share of the Japanese Pachinko Hall Market in Terms of Number of Halls in Operation at the end of 2012



Sources: Company, Nichiyukyo (Japan Association of Recreation Businesses)

The main business of Dynam Japan Holdings is the operation of pachinko/pachislot halls. Its other businesses are related to the operation of these halls and include managing the property on which halls are erected, cleaning the halls, and providing food and beverages in the halls. The company has a subsidiary in Hong Kong which looks for investment opportunities in Asia. It also has a subsidiary that acts as a travel agency for trips to Mongolia and sells real estate in Mongolia.

Organization Chart for Dynam Japan Holdings



Source: Company



Leading the industry by undertaking revolutionary challenges

History

Dynam Japan Holdings originated as Sawa Shoji Co., Ltd, which was established in 1967 by the father of the company's current Chairman, Yoji Sato. In 1968, the founder passed away, so his eldest son, Yoji Sato, who had been working for the supermarket chain operator Daiei (8263), assumed leadership of Sawa Shoji at the age of 24.

Throughout the company's history, it has sought new challenges and introduced new practices and products to lead the pachinko industry. Among its innovations were the employment of university graduates, the development of low operation cost and suburban halls, the establishment of a company union for its employees, and the introduction of pachinko machines with low playing cost. However, the two most distinctive traits of the company have been 1) its development and operation of pachinko/pachislot halls according to the principles of chain store operations, as shown by its membership in the Pegasus Club, and 2) its early intent to list its shares, as shown by its regular meetings with securities analysts and its attainment of an investment rating in 1997, which it no longer holds.

A chain store operational style is revealed in many aspects of company management, and this style explains the significance of its activities. Its model for opening pachinko/pachislot halls, described in greater detail below, is representative of this style.

Chairman Yoji Sato is primarily responsible for the introduction of the company's chain store operational style. While a university student, he was impressed by the revolution that was taking place in Japan's distribution system at the time. Upon graduation, he entered the supermarket chain operator Daiei, where he quickly began offering reports and recommendations to his superiors on ways to improve store management. He even impressed Daiei founder Isao Nakauchi. Yoji Sato subsequently joined Sawa Shoji, but he remains active in Japan's chain store industry as a member of the Pegasus Club, a group of executives of top chain stores in Japan that analyzes chain store management. Yoji Sato helped establish the corporate culture at Dynam Japan Holdings that underlies the company's success.

Dynam Japan Holdings has prepared to list its shares for more than 20 years. Toward this end, it established a compliance department long before most other Japanese companies had such a department. Through strict adherence to the law, the company aimed to overcome the stigma of gambling attached to the pachinko industry. Today, its legal, risk management and internal audit department employs more than 100 professionals.

The company has worked to benefit all the stakeholders in its business. For example, it was the first company in the industry to establish a labor union. It aims to operate 1,000 pachinko/pachislot halls and to hold a 10% share of the Japanese market 10 years from now. Thus, it is currently in a rapid growth phase. Normally, companies in this stage forego dividends to invest in expansion, allowing shareholders to reap capital gains on their investment. However, Dynam Japan Holdings plans to achieve a dividend payout ratio of 45-50% while growing rapidly. This demonstrates management's commitment to shareholders.

Company History

July	1967	Established as Sawa Shoji Co., Ltd., with pachinko halls in Kameari and Kanamachi, Tokyo
November	1987	Company name changed to Dynam Co., Ltd.
April	1989	Hired first employees who had just graduated from universities
October	1989	Opened company's first suburban pachinko hall in Shibata, Niigata Prefecture
October	1993	Became a corporate member of the Pegasus Club, an organization that analyzes chain store operations
August	1994	Opened company's first low playing cost pachinko hall made of wood, in Ebetsu, Hokkaido
July	1997	Held first meeting with securities analysts
December	1997	Received the first investment rating ever awarded to a pachinko hall operator in Japan
April	1998	Established a labor union called Dynam Union, the first such union in the industry
December	2006	Opened the first pachinko hall offering low playing costs (¥2 per pachinko ball and ¥10 per pachislot token), in Ebetsu, Hokkaido
May	2007	Began full-scale development of Dynam Yuttari Kan pachinko halls, which rent pachinko balls at a price of ¥1 each
March	2009	Announced the concept of Shinrai no Mori pachinko hall and opened the first such hall in Takanosu, Akita Prefecture
September	2011	Dynam Japan Holdings Co., Ltd. established through a split up of Dynam Holdings Co., Ltd.
August	2012	Shares listed on the Hong Kong Stock Exchange
January	2013	Established subsidiary Dynam Hong Kong Co., Ltd.
May	2013	Announced investment in the Erin Town Project, a real estate development in Mongolia
June	2013	Announced the investment of US\$35mn in Macao Legend Development Ltd.
October	2013	Announced the investment of US\$15mn in IGG Inc., of Singapore

■ Japan's Pachinko Industry

Proportion of low playing cost halls rising in response to consumer demand

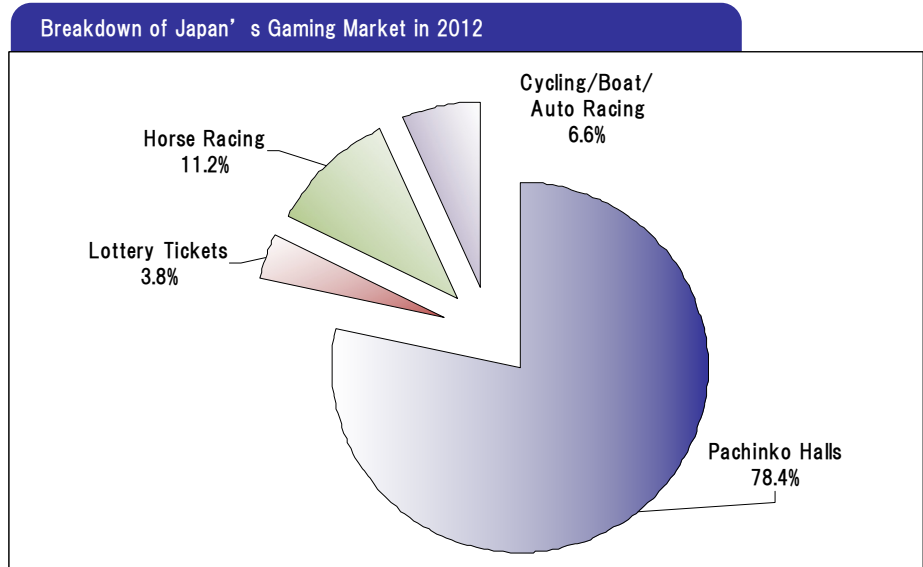
The two dominant characteristics of Japan's pachinko industry are 1) shrinkage as the number of customers falls, and 2) an increase in the number of low playing cost halls.

Market trends

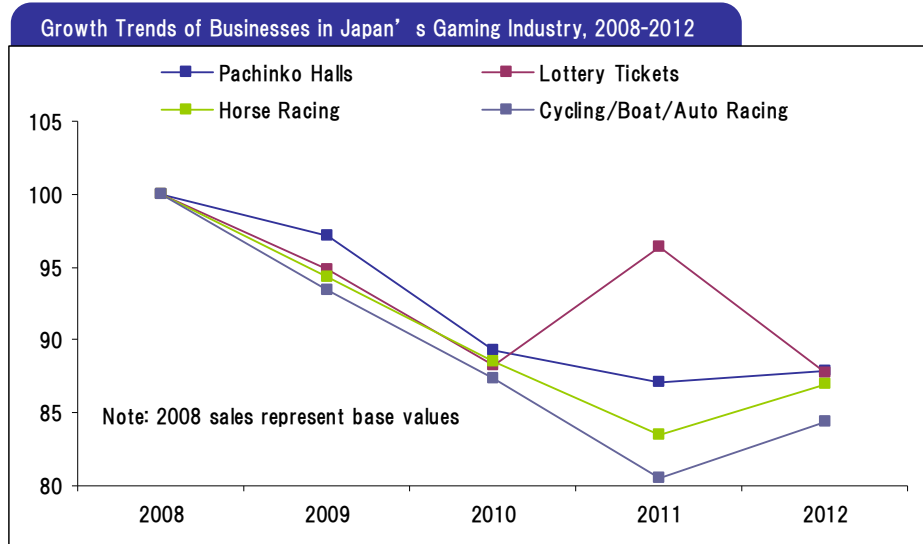
Pachinko halls constitute 78% of Japan's gaming market, but like the markets for other gaming industries, the market for pachinko halls is shrinking. Thus, the operation of pachinko halls is becoming more difficult.

Pachinko industry sales, i.e., revenues from renting pachinko balls, peaked in 1995 at ¥30.9 trillion and declined steadily to ¥18.9 trillion in 2011, when the market was also adversely affected by the Great East Japan Earthquake of March 11, 2011. In 2012, industry sales recovered to ¥19.1 trillion, but this was not a wholehearted recovery. The number of pachinko hall customers fell to 11.1 million in 2012 from 12.6 million in 2011, and the number of pachinko halls remained depressed.

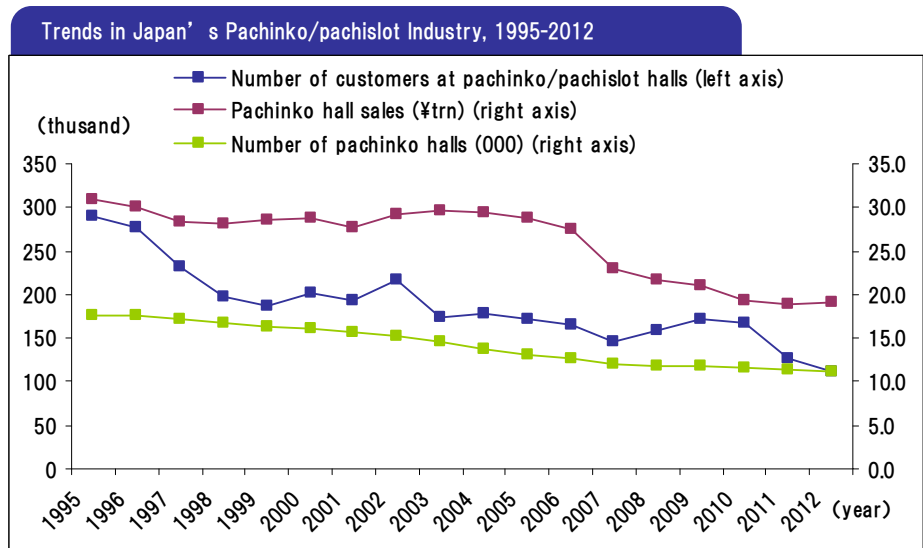
Japan's Pachinko Industry



Source: Leisure White Paper, Japan Productivity Center



Source: Leisure White Paper, Japan Productivity Center



Source: Prepared by FISCO Ltd. based on the Leisure White Paper by the Japan Productivity Center and on materials from Nichiyukyo (Japan Association of Recreation Businesses)

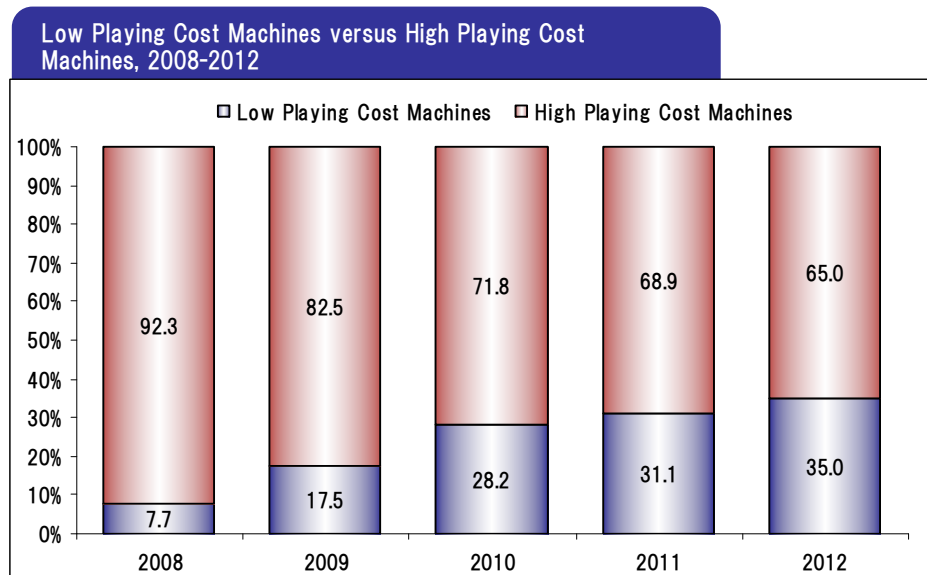


■ Japan's Pachinko Industry

Increase in the number of low playing cost halls

Japan's pachinko market is shrinking for many reasons: Japan's economy has been weak for most of the past 30 years, games played on mobile devices have become popular, and the regulation of consumer loans has been tightened substantially. Another major reason is the spread of pachinko halls that charge rental fees of only ¥1-2 per pachinko ball, whereas the standard rental fee is ¥4. It is difficult to determine whether the spread of these low playing cost halls has caused the industry to shrink or has resulted from industry shrinkage, but the number of such halls has increased steadily.

Regulations set the upper limit on the rental fee for a pachinko ball at ¥4, but there is not lower limit. The standard pachinko machine releases 100 balls per minute. At a rental fee of ¥4 per ball, a machine can generate up to ¥24,000 of sales per hour, but at a rental fee of ¥1 per ball, it can generate maximum sales of ¥6,000 per hour. For this reason, many operators of pachinko parlors have been reluctant to introduce low playing cost machines, but more operators have introduced them in response to consumer demand, and the proportion of all machines accounted for by low playing cost machines has risen steadily, as shown in the following bar chart.



Source: Japan Productivity Center

■ **Dynam's Pachinko Business**

Regaining revenue and profit growth in a shrinking industry

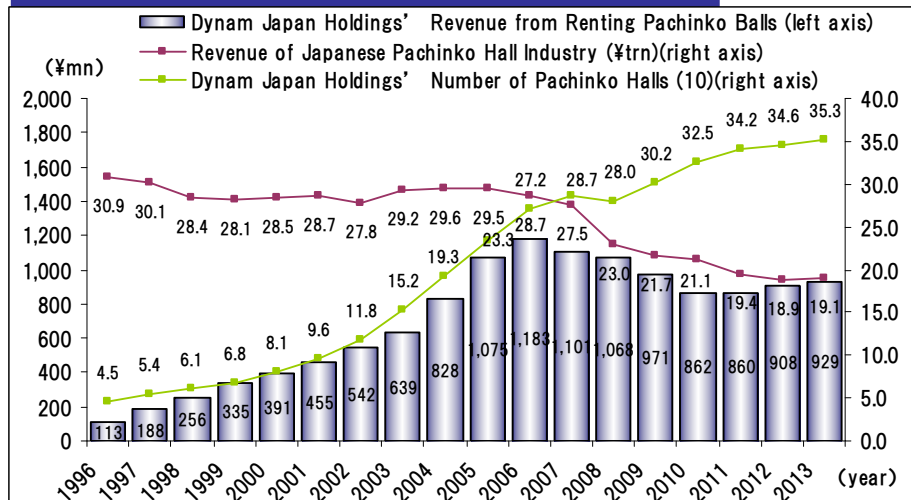
Past performance

As Japan's pachinko hall industry has contracted, Dynam Japan Holdings has expanded its revenue from renting pachinko balls, except for four years, from 2005 to 2009. In 2006-2007, its revenue fell, due in part to a change in the structure of demand, and revenue declines in 2008 - 2009 reflected the company's rapid expansion of low playing cost halls. In 2010, the company's revenue from renting pachinko balls was basically unchanged year-on-year (y-o-y), and since then, it has increased, reflecting the company's steady expansion of low playing cost halls, its policy of presenting ideal playing environments for its customers, and its increase in the total number of halls in operation.



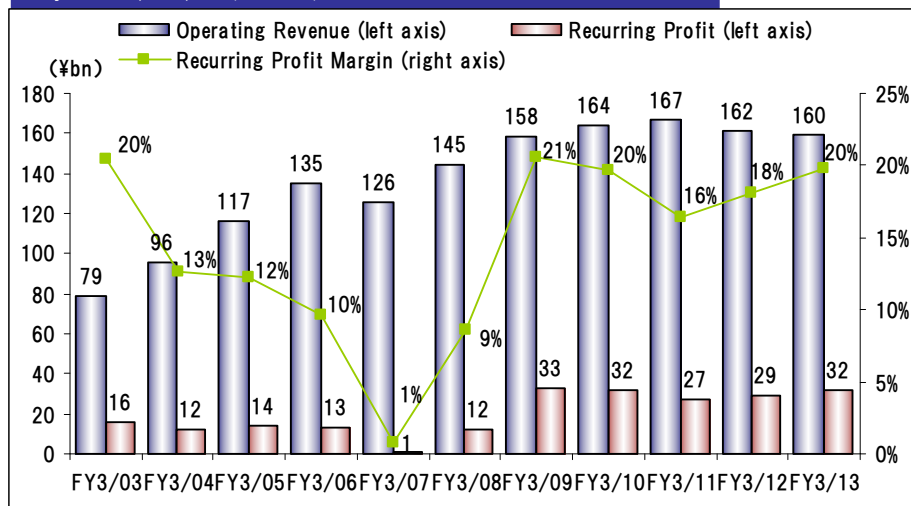
■Dynam' s Pachinko Business

Dynam Japan Holdings' Revenue from Renting Pachinko Balls and Number of Pachinko Halls versus Revenue from Renting Pachinko Balls of Japan' s Pachinko Hall Industry, 1996-2013



Dynam Co., Ltd., the main subsidiary of Dynam Japan Holdings, has fared well despite the downturn in Japan' s pachinko industry. In FY3/13, its operating revenue, i.e., its revenue from renting pachinko balls minus its cost of prizes, plus other income, such as sales of food and beverages, fell by 1% y-o-y to ¥159.5bn, but its recurring profit grew by 7.6% y-o-y to ¥31.6bn, close to the company' s all-time high recurring profit, for a recurring profit margin of 19.8%.

Operating Revenue, Recurring Profit, and Recurring Profit Margin of Dynam Co., Ltd., FY3/03-FY3/13



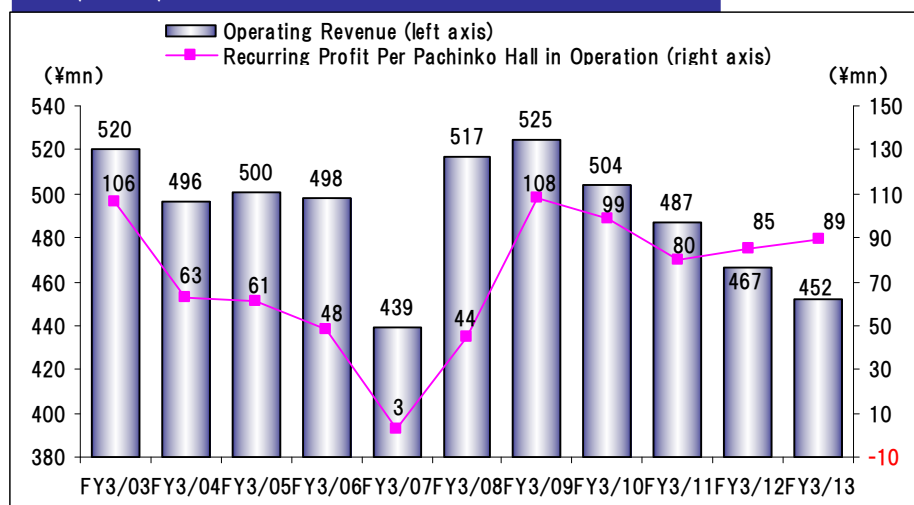
Source: Operating revenue comes from renting pachinko balls minus its cost of prizes

However, Dynam Co.' s operating revenue per pachinko hall declined by 13.2% from FY3/03 to FY3/13. Since most of the company' s operating revenue comes from renting pachinko balls minus its cost of prizes, the company' s shift towards low playing cost halls was a main cause of the decline in operating revenue per pachinko hall. A fall in the number of customers per hall and a drop in average spending per customer also contributed to the decline in operating revenue per pachinko hall. By introducing personal systems and private brand pachinko machines to control costs, Dynam Co. reversed a temporary decline in its recurring profit per pachinko hall.



■Dynam' s Pachinko Business

Dynam Co., Ltd.' s Operating Revenue and Recurring Profit Trends, FY3/03-FY3/13



Higher than industry average profitability reflects aggressive investment in low playing cost halls

One measure of business performance in the pachinko industry is the pachinko/pachislot machine utilization rate, which is the average number of pachinko balls or pachislot tokens released per machine per day. In H1 FY3/14, the average utilization rate for Dynam Japan Holdings was 24,570, which was about 3,500 more than the average utilization rate for the pachinko hall industry. Over the past three years, Dynam Japan Holdings' machine utilization rate has exceeded the industry average utilization rate by 3,000-4,000 per year, illustrating the group' s superior ability to generate profit.

One reason that Dynam Co. has a high pachinko machine utilization rate is that it has a high proportion of pachinko machines with low playing cost. At the end of March 2012, about 35% of all the pachinko/pachislot machines in Japan were low playing cost machines, whereas Dynam Co.' s ratio was 52.3%. For pachinko machines alone, Dynam Co.' s ratio was 58.9%. At the end of September 2013, 62.3% of Dynam' s pachinko machines were low playing cost machines.

At the end of September 2013, Dynam Japan Holdings operated 363 pachinko halls, including 9 operated by subsidiary Cabin Plaza. Of these, 174 halls were traditional halls offering high playing cost machines, i.e., machines charging a rental fee of ¥4 per pachinko ball and ¥20 per pachislot token, 155 halls were Yuttari Kan halls, which specialize in low playing cost machines, and 34 were Shinrai no Mori halls based on the concept of time consuming leisure and which offer mainly low playing cost machines. The Yuttari Kan halls allow smoking anywhere, whereas the Shinrai no Mori halls strictly segregate smoking areas. The traditional halls provide much more revenue from hall operations than the other two types of hall. However, in terms of net revenue (revenue from renting pachinko balls minus the cost of prizes), the contributions are more similar. Net revenue as a proportion of revenue from renting balls is considered to be the gross profit margin. For traditional halls, the gross profit margin was 15.0% in H1 FY3/14, whereas the average gross profit margin for Yuttari Kan halls and Shinrai no Mori halls was 24.1%.

■Dynam's Pachinko Business

In terms of absolute profit contribution, traditional halls provide the most because personnel expense varies little by type of hall, and since Yuttaki Kan halls and Shinrai no Mori Halls still provide relatively small net revenues, their profits are depressed by personnel costs.

Nonetheless, the company plans to open only low playing cost Yuttari Kan halls hereafter, because consumers demand such halls. To improve profitability while opening low playing cost halls, the company intends to reduce the cost of opening new halls and to introduce private brand machines and personal systems to lower operating costs.

Dynam Co., Ltd. Revenues from Renting Pachinko Balls (Gross Revenue), Net Revenue, Personnel Cost, and Operating Profit (¥mn) by Type of Pachinko Hall, FY3/13 - H1 FY3/14
(Unit: ¥mn)

			FY3/12			FY3/14
			H1	H2	Total	H1
Revenue from Renting Pachinko Balls	Total	Total	467,263	461,895	929,158	470,532
	Traditional Halls		364,457	352,385	716,842	343,925
	Yuttari Kan Halls		80,575	87,668	168,243	107,249
	Shinrai no Mori Halls		22,231	21,842	44,073	19,358
Net Revenue	Total	Amount	82,060	81,901	163,961	82,159
		Ratio to Revenue from Renting	17.6%	17.7%	17.6%	17.5%
	Traditional Halls	Amount	53,823	53,484	107,307	51,597
		Ratio to Revenue from Renting	14.8%	15.2%	15.0%	15.0%
	Yuttari Kan Halls	Amount	22,433	23,006	45,439	25,890
		Ratio to Revenue from Renting	27.8%	26.2%	27.0%	24.1%
	Shinrai no Mori Halls	Amount	5,804	5,411	11,215	4,672
		Ratio to Revenue from Renting	26.1%	24.8%	25.4%	24.1%
Hall Personnel Cost	Total	Amount	23,142	22,613	45,755	22,582
		Ratio to Net Revenue	28.2%	27.6%	27.9%	27.5%
	Traditional Halls	Amount	14,643	14,095	28,738	13,611
		Ratio to Net Revenue	27.2%	26.4%	26.8%	26.4%
	Yuttari Kan Halls	Amount	6,656	6,759	13,415	7,536
		Ratio to Net Revenue	29.7%	29.4%	29.5%	29.1%
	Shinrai no Mori Halls	Amount	1,843	1,759	3,602	1,435
		Ratio to Net Revenue	31.8%	32.5%	32.1%	30.7%
Hall Operating Profit	Total	Amount	15,489	14,568	30,057	14,003
		Ratio to Net Revenue	18.9%	17.8%	18.3%	17.0%
	Traditional Halls	Amount	12,113	13,726	25,839	11,019
		Ratio to Net Revenue	22.5%	25.7%	24.1%	21.4%
	Yuttari Kan Halls	Amount	3,158	1,435	4,593	2,745
		Ratio to Net Revenue	14.1%	6.2%	10.1%	10.6%
	Shinrai no Mori Halls	Amount	218	-592	-374	239
		Ratio to Net Revenue	3.8%	-10.9%	-3.3%	5.1%

■ Medium-term Growth Scenario

The company targets 1,000 halls in operation and a 10% market share in 10 years

Summary

For the business of operating pachinko halls, Dynam Japan Holdings aims to operate 1,000 halls and to hold a 10% share of the Japanese market 10 years from now. The company intends to achieve these goals through the orthodox strategy of expanding its share of a shrinking market, thereby supporting sales and profit growth. However, these are ambitious targets. The most challenging will probably be the operation of 1,000 halls. At the end of FY3/13, Dynam Japan Holdings operated 362 halls, of which, 353 were operated by Dynam Co. and 9 were operated by subsidiary Cabin Plaza. Over the next three years, the company targets 40 new halls per year. After that, or possibly in conjunction with this expansion, the company plans to acquire smaller operators of pachinko halls to increase the number of its halls.

It is difficult to forecast the shrinkage of Japan's pachinko hall market 10 years from now. In fact, the market may expand again. Other forms of entertainment, such as casinos, may gain popularity at the expense of the pachinko hall industry. Furthermore, Dynam Japan Holdings may reduce its industry-leading operating efficiency by acquiring smaller pachinko hall operators. This threat has convinced many companies to eschew mergers and acquisitions in favor of organic growth. The company aims to overcome these challenges by adhering to its model for opening new halls and by introducing more private brand (PB) pachinko and pachislot machines, thereby lowering its operating costs substantially.

Model for opening new halls

The company plans to concentrate on opening new Yuttari Kan pachinko halls in suburban areas, with each hall housing about 480 machines. It will rent plots of land about 11,666 square meters in area each and invest about ¥452mn to construct a hall and install equipment other than pachinko and pachislot machines in each hall. The cost of installing pachinko and pachislot machines will be expensed in the first year of operation. Thus, each new hall will suffer an operating loss in its first year, but each should be profitable from the second year, providing an average operating profit of ¥130mn per year over the first 10 years.

The company began opening new halls according to this model in FY3/12, when it budgeted ¥600mn to construct a hall and install equipment other than pachinko and pachislot machines in it. Over the past two fiscal years, it discovered that it could lower this initial investment to about ¥450mn per hall. By introducing personal systems into its halls, the company reduced the number of employees per hall to 6 - 7 regular employees and about 20 part-time employees.

Introduction of more private-brand machines

Operators of pachinko halls must reduce the cost of renewing pachinko and pachislot machines to profit. Over the next four years, Dynam Japan Holdings plans to install more private-brand machines to lower its costs. The company calculates that a private-brand machine costs about ¥100,000 less than a comparable national-brand machine. Thus, it could lower costs substantially by using more private-brand machines.

■ Medium-term Growth Scenario

However, this strategy could backfire if consumers are not attracted to private-brand machines. Thus, the company may install used national-brand machines as well as private-brand machines. The use of more private-brand machines will succeed only if the company or a contracted manufacturer of pachinko machines develops private-brand machines that appeal to consumers. As the company lacks experience in developing machines, it would be hasty to place too much expectation on the impact of using more private-brand machines.

Cash flow analysis

In recent years, Dynam Japan Holdings has maintained a stable cash flow. Its pretax profit has averaged about ¥30bn per year, its depreciation expense has averaged about ¥10bn per year, and its taxes paid have averaged about ¥12bn per year. Thus, its cash flow from operations has averaged about ¥30bn per year.

The acquisition of fixed assets, primarily new pachinko halls, has accounted for about half of the company's cash flow from investments.

As noted earlier, the company plans to open about 40 new halls per year over the next three years. Its ability to do so will depend on such factors as the availability of suitable land sites and the terms of lease applying to these sites. Assuming the company can open 40 new halls per year at an average cost of ¥452mn per hall, its capital investment would average about ¥18bn per year, or about 60% of its cash flow from operations.

While the company invests heavily in new halls, it plans to maintain a dividend payout ratio of 45—50%. In FY3/13, the company paid a full-year dividend of ¥13.0 per share. Thus, its total dividend payments came to about ¥9.7bn. For H1 FY3/14, the company paid a dividend of ¥7.0 per share. It has not decided on its year-end dividend for FY3/14, but if it matches its year-end dividend for FY3/13 of ¥7.25 per share, it will pay a full-year dividend of ¥14.25 per share for FY3/14. As it has 742.85mn shares outstanding, its dividend payments would total about ¥10.6bn for FY3/14.

If Dynam Japan Holdings continues to generate about ¥30bn of cash flow from operations each year, it should be able to open 40 new halls per year and maintain a dividend payout ratio of 50%.

Cash Flow Statement (¥mn), FY3/10-FY3/13

(Unit: ¥mn)

	FY3/10	FY3/11	FY3/12	FY3/13
Cash flow from operations				
Pretax profit	33,300	28,476	28,404	33,436
Depreciation cost	11,402	11,462	10,804	10,507
Taxes paid	-20,429	-6,975	-12,360	-12,511
Other items	-5,044	436	5,058	-3,102
Total	19,229	33,399	31,906	28,330
Cash flow from investments				
Increase in fixed assets	-11,133	-6,152	-7,471	-10,723
Other items	1,080	-11,096	18,469	-176
Total	-10,053	-17,248	10,998	-10,899
Cash flow from financing				
Increase in bank borrowings	43,098	13,850	22,000	15,500
Repayment of bank borrowings	-43,305	-30,527	-37,453	-33,191
New share issuance	0	0	-	15,884
Dividend payments	-7,242	-4,295	-4,885	-4,271
Other items	-111	194	-11,502	-1,950
Total	-7,560	-20,778	-31,840	-8,028
Gain or loss on translation of foreign currency cash and cash equivalents	0	0	-	3,539
Change in cash and cash equivalents	1,616	-4,627	11,064	12,942
Cash and cash equivalents at start of term	20,471	22,087	17,460	28,524
Cash and cash equivalents at end of term	22,087	17,460	28,524	41,466

Business Trends

With greater contributions by Yuttari Kan halls, sales and profits grew y-o-y

H1 FY3/14 Results

In H1 FY3/14, Dynam Japan Holdings increased its operating revenue by 0.8% y-o-y to ¥85,757mn, its operating profit by 2.4% y-o-y to ¥15,888mn, and its net profit by 6.2% y-o-y to ¥9,898mn.

Revenue from renting pachinko balls, or gross revenue, grew by 0.7% y-o-y to ¥470,532mn, while the cost of prizes increased by 0.8% y-o-y to ¥388,373mn, so net revenue rose by only 0.1% y-o-y to ¥82,159mn. The company invested mainly in installing more low playing cost pachinko machines, so it opened only one new pachinko hall in H1 FY3/14. This minimal increase in the number of pachinko halls contributed to the slow rates of revenue growth. At the end of H1 FY3/14, the company had seven more halls in operation than it did a year earlier.

Net revenue from traditional pachinko halls fell by 4.1% y-o-y to ¥51,598mn in H1 FY3/14, while net revenue from Yuttari Kan pachinko halls grew by 15.4% y-o-y to ¥25,889mn, and net revenue from Shinrai no Mori pachinko halls dropped by 19.5% y-o-y to ¥4,671mn. The fall in net revenue from traditional halls and the rise in net revenue from Yuttari Kan halls reflected a shift in consumer preference to low playing cost halls. As a result of this shift, the utilization rate of machines charging rental fees of ¥4 per ball declined. Net revenue from Shinrai no Mori pachinko halls declined because 10 of these halls were converted into Yuttari Kan pachinko halls in H1 FY3/14.

Operating costs were limited to 0.4% y-o-y growth. Therefore, operating profit increased by 2.4% y-o-y.

Summary Income Statement (¥mn), FY3/10 - H1 FY3/14

(Unit: ¥mn)

Revenues	FY3/10	FY3/11	FY3/12			FY3/13			FY3/14
			H1	H2	Yr	H1	H2	Yr	H1
Gross revenue	862,023	859,882	444,584	463,725	908,309	467,263	461,895	929,158	470,532
y-o-y	--	-0.2%	--	--	5.6%	5.1%	-0.4%	2.3%	0.7%
Cost of prizes	696,562	690,245	364,288	378,943	743,231	385,203	379,994	765,197	388,373
y-o-y	--	-0.9%	--	--	7.7%	5.7%	0.3%	3.0%	0.8%
Net revenue	165,461	169,637	80,296	84,782	165,078	82,060	81,901	163,961	82,159
y-o-y	--	2.5%	--	--	-2.7%	2.2%	-3.4%	-0.7%	0.1%
Other revenue	6,898	6,962	3,588	2,984	6,572	3,029	6,221	9,250	3,598
Total operating revenue	172,359	176,599	83,884	87,766	171,650	85,089	88,122	173,211	85,757
y-o-y	--	2.5%	--	--	-2.8%	1.4%	0.4%	0.9%	0.8%
Costs									
Pachinko hall operating costs	134,787	144,239	69,052	69,733	138,785	66,571	67,333	133,904	68,156
y-o-y	--	7.0%	--	--	-3.8%	-3.6%	-3.4%	-3.5%	2.4%
SGA costs	642	934	625	1,129	1,754	1,759	1,353	3,112	1,474
y-o-y	--	45.5%	--	--	87.8%	181.4%	19.8%	77.4%	-16.2%
Other operating costs	1,188	813	311	563	874	1,238	668	1,906	239
Total operating costs	136,617	145,986	69,988	71,425	141,413	69,568	69,354	138,922	69,869
y-o-y	--	6.9%	--	--	-3.1%	-0.6%	-2.9%	-1.8%	0.4%
Operating profit	35,742	30,613	13,896	16,341	30,237	15,521	18,768	34,289	15,888
y-o-y	--	-14.4%	--	--	-1.2%	11.7%	14.9%	13.4%	2.4%
Net financial cost	2,442	2,137	1,287	546	1,833	393	460	853	402
Pretax profit	33,300	28,476	12,609	15,795	28,404	15,128	18,308	33,436	15,486
y-o-y	--	-14.5%	--	--	-0.3%	20.0%	15.9%	17.7%	2.4%
Tax expense	13,086	12,285	5,147	7,359	12,506	5,804	6,707	12,511	5,588
Net profit	20,214	16,191	7,462	8,436	15,898	9,324	11,601	20,925	9,898
y-o-y	--	-19.9%	--	--	-1.8%	25.0%	37.5%	31.6%	6.2%
EPS	32.0	25.7			25.2	14.0		29.7	13.4
Dividend per share (¥)	9.60	5.70			4.40	5.75	7.25	13.00	7.00



Company aims to grow by opening new halls in the shrinking market, thereby raising its market share

Growth Prospects

As stated previously, the company's strategy is to grow by increasing the number of pachinko halls it operates and its share of a shrinking market. Thus, its pace of opening new halls is an important gauge of its growth potential.

It will also be necessary to increase revenue and cut costs at traditional Dynam brand pachinko halls and to generate greater revenue from the Yuttari Kan pachinko halls. Yuttari Kan pachinko halls provide low playing cost machines and yield a higher gross profit margin than traditional Dynam brand pachinko halls, but their absolute revenue remains relatively small because most of the machines in these halls charge a rental fee of only ¥1 per ball. These machines enable long-term play, but they offer low returns in terms of prizes. Therefore, consumers have recently shown greater interest in playing machines that charge a rental fee of ¥2 per ball, as these machines offer more attractive prizes than machines that charge a rental fee of ¥1 per ball. Dynam Japan Holdings would benefit from an expansion of this trend.

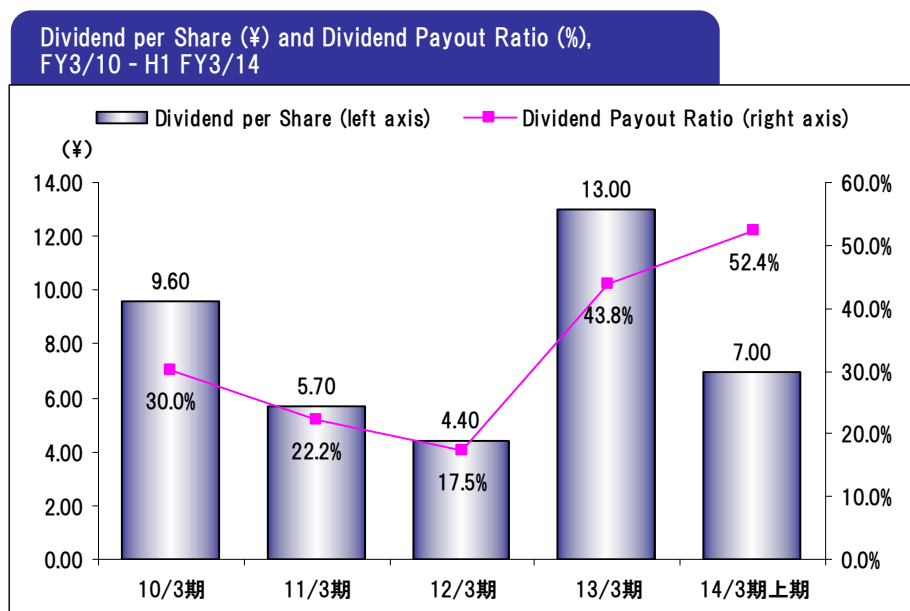
To cut costs, in addition to adding more private-brand pachinko machines, as discussed above, the company is installing more personal systems in its pachinko halls. These systems allow customers to change pachinko machines without carrying their pachinko balls. Thus, hall corridors remain uncluttered with boxes for carrying balls, and it is easier to monitor the number of balls outstanding, enabling the company to reduce the number of employees per hall. These systems cost about ¥50mn each, but they allow large reductions in staff cost. By the end of H1 FY3/14, the company had installed personal systems in 221 of its pachinko halls, and it will probably continue to install these systems.

Thus, the growth potential of Dynam Japan Holdings depends on many factors, including the pace of opening new halls, an increase in the number of low playing cost halls, an increase in the number of private-brand pachinko machines, and a further use of personal systems. With this many options to pursue, the company should be able to grow despite industry contraction.

■ Shareholder Return Policy

Company intends to raise its dividend payout ratio to 45 – 50%, indicating its concern for shareholder returns

As a listed company, Dynam Japan Holdings is mindful of its obligations to its shareholders. Consequently, it intends to realize a dividend payout ratio of 45-50% even as it invests heavily in growth.



■ Response to Japan's Possible Permission of Casinos

Hong Kong subsidiary plays the important role of gathering information on the casino industry

The Japanese government is trying to make Japan more attractive to international tourists. Tokyo will host the Olympic Games in 2020, and many parties are promoting the development of integrated resorts in Japan, which would include casinos, which are currently banned in Japan. A multi-party commission in the Diet is preparing a law to legalize casinos. Many makers of pachinko machines are interested in manufacturing casino equipment, but no Japanese company has the knowhow to operate a casino. If casinos were legalized, Dynam Japan Holdings and other operators of pachinko halls would naturally be interested in learning to operate casinos.

Improve information gathering ability through Hong Kong subsidiary

Dynam Japan Holdings' subsidiary in Hong Kong has been gathering information on opportunities for the company to ally with operators of casinos overseas, especially in Macao. The company continues to gather information and knowhow about this business to prepare for possible entry if casinos are legalized in Japan.

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