FreeBit Co., Ltd.
3843 Tokyo Stock Exchange First Section

12-Aug.-16

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FISCO Ltd. Analyst
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Aiming to achieve net sales of ¥50bn and operating income of ¥5bn in FY4/20 through growing existing businesses and expanding new businesses, centered on "Health Tech"

FreeBit Co., Ltd. <3843> (hereafter, also "the Company") provides a variety of Internet services to corporations and individuals, from infrastructure through to consulting and solutions. In addition to the provision of infrastructure for Internet service providers (ISP), the businesses the Company's Group are involved in include providing support for entering into MVNO*1 as an MVNE (Mobile Virtual Network Enabler), Web marketing services, Internet-related services for individuals and collective housing (condominiums), and the provision of Cloud infrastructure, particularly virtual data centers (VDC)*2. Also, toward the growth of its smartphone business that utilizes the Group's business expertise, in 2015 it established Tone mobile inc., a joint venture with Culture Convenience Club Co., Ltd. (hereafter, "CCC"), and is currently focusing on expanding its businesses, including through the provision of its proprietary smartphone TONE.

In the FY4/16 consolidated results announced on June 10, net sales increased 32.2% year-on-year (y-o-y) to ¥28,389mn, operating income rose 52.9% to ¥1,902mn, and net income attributable to the owners of parent declined 46.1% to ¥553mn, but achieving record highs for both net sales and operating income. In addition to the strong performances of the Mobile Business, including the "freebit MVNO Pack,"*3, and the Ad Technology Business of Full Speed Inc.<2159>, the positive results were due to the expansion of the Internet service for collective housing provided by GIGAPRIZE Co., Ltd.<3830> in the Broadband Business. Net income declined as a reaction to temporary factors in the previous fiscal year, including the recording of deferred tax assets.

At the same time as the results announcement, the Company announced SiLK VISION 2020, its medium-term business policy up to FY4/20. The policy describes the consolidated results targets for FY4/20 of net sales of ¥50bn and operating income of ¥5bn from the FreeBit Group's commitment to its external markets. This basic policy outlines the goal of achieving business expansion in the medium to long term by aiming to realize growth through strengthening its existing Mobile and Ad Technologies businesses; launching new businesses in the three fields the Company cited in SiLK VISION 2016, of "Health Tech," "IoT," and "Real Estate Tech" within the "Life Revolution" area; and leveraging synergies through Group coordination.

The Company's targets for the FY4/17 results are for a double-digit increase in sales, a single-digit increase in operating income, but a decline in net income, with net sales forecast to rise 23.3% to ¥35,000mn, operating income to grow 5.1% to ¥2,000mn, but net income attributable to the owners of the parent company to fall 54.8% to ¥250mn. The reason why operating income will only increase by a single digit is because the forecast incorporates the prior investment of ¥500mn to ¥600mn described in the medium-term business policy in order to launch the new businesses, centered on "Health Tech." In addition, the major decline in net income is due to the fact that the temporary factors that occurred in the previous fiscal year, including a gain on the sale of a business, are not expected in this fiscal year, and also because of an increase in income tax from the strong results recorded by the subsidiaries, and as net income attributable to the non-controlling shareholders of GIGAPRIZE and Full Speed will be recorded.

The contribution to profits of the Company's subsidiaries is high, and compared to operating income and ordinary income, net income tends to decline. Therefore, the Company as a whole is aware that increasing profits is an issue to be addressed in the medium to long term.

*1 A virtual mobile communications businesses that involves conducting an independent communication business by borrowing the lines from communication businesses with a wireless communication infrastructure, such as NTT DOCOMO, INC. <9437>, KDDI CORPORATION <9433>, and SoftBank Corp.

*2 A mechanism or service for virtually building the functions of a data center so they can be used over the Internet.

*3 A package service that can commercialize MVNO at low cost and low risk in a short period of time that the Company provides to various businesses.

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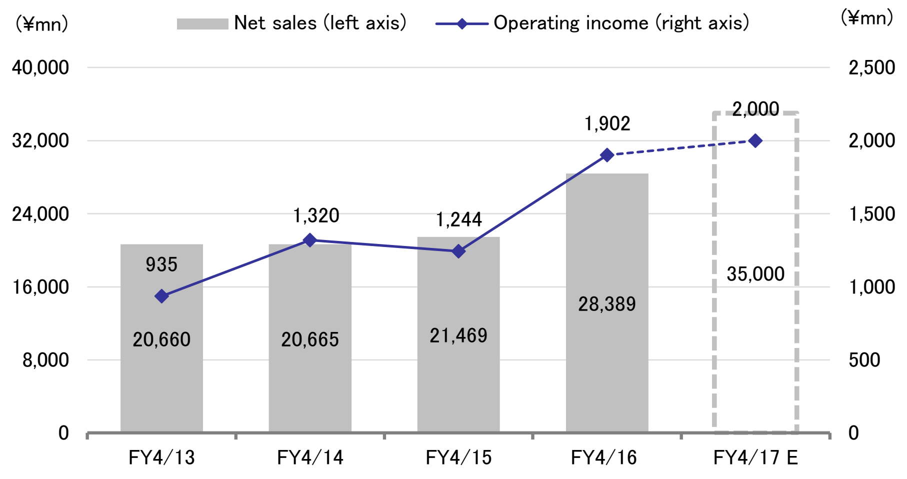
Check Point

- Achieved record highs in net sales and operating income in FY4/16 from the strong performances of the Mobile and Ad Technology businesses
- Planning prior investment of ¥500mn to ¥600mn in FY4/17 to launch new businesses, centered on "Health Tech"
- Is aiming for net sales of ¥50bn and operating income of ¥5bn as its FY4/20 consolidated results targets

Results trends



Company Profile and History

Infrastructure provider based on the Internet, expanding its business through active M&As

(1) Company Profile

Based on its corporate philosophy of "Being the NET Frontier! (expand the Internet, contribute to society)" and its mission of "Creating New Products from Zero," the Company leverages its strength of accumulating technological capabilities, of the development of Internet-related core technologies and the management of large-scale systems, to provide a variety of Internet-related services to corporations and individuals. These proprietary network services that combine cutting-edge technologies, including patented technologies and marketing that anticipates market needs, enable it to provide solutions that create new value based on the keywords of "Monozukuri (craftsmanship) in the IT age."

*1 Rather than developing the Web like a cobweb as it had been developed in the US, the Company aims to create SiLK as a "smooth and soft Internet," with the word SiLK expressing the Japanese style of Internet service.

*2 As SiLK VISION 2010 progressed better than anticipated and the initial targets were achieved one year ahead of schedule, the Company formulated SiLK VISION 2012 (FY4/10 to FY4/12) and announced it in April 2009. Subsequently, taking into account the effects of the execution of M&As and other factors, in August 2010 it announced SiLK VISION 2012 ver.2 (FY4/10 to FY4/13) that extended the plan's period by one year.

(2) Company history

The predecessor of the Company, FreeBit.com Co., Ltd., was founded in May 2000 (name changed to FreeBit Co., Ltd. in December 2002) by Atsuki Ishida, chairman of the board, who was involved in the founding of DREAM TRAIN Internet INC. (hereafter, "DTI"), which is a subsidiary of Mitsubishi Electric Information Network Corporation; Nobuaki Tanaka, president and member of the board; and Takashi Shimizu, vice president and director. Based on its independently developed proprietary technologies, it deployed Internet business support operations, such as providing infrastructure and technology for companies managing ISP and its sales grew. It listed on the Tokyo Stock Exchange (TSE) Mothers Market in March 2007.

After it listed, the Company developed its strategy based on its Medium-Term Management Plan. At the same time as expanding its business area and scale through actively conducting M&As, it implemented business-structure reforms targeting selection and concentration, which brings it up to the present day. This stage, from its foundation up to the present day, can be divided according to the three Medium-Term Management Plans, of SiLK*1 VISION 2010, SiLK VISION 2012 & 2012 ver.2*2, and SiLK VISION 2016.

a) SiLK VISION 2010 (FY4/08 to FY4/10)

The Company developed a hybrid strategy based on the Medium-Term Management Plan SiLK VISION 2010 it announced in June 2007 (aiming to acquire ISPs, integrate them with DTI, and increase user numbers. At the same time, aiming to differentiate itself by providing proprietary services utilizing its own technologies). After DTI was consolidated in August of the same year, in March 2009 Media Exchange Co., Ltd. (name changed to FreeBit Cloud Co., Ltd. in September 2010. Merged with DTI in February 2014) and its subsidiary GIGAPRIZE Co., Ltd. were consolidated. In this way, the Company has been conducting M&As and integrating ISP operators.

b) SiLK VISION 2012 & 2012 ver.2 (FY4/10 to FY4/13)

For the period from 2010 onwards, the Company formulated and announced in April 2010 the subsequent Medium-Term Management Plan SiLK VISION 2012, which was centered on the Smart Infra strategy. Under this strategy, it aimed to utilize its proprietary technologies, such as network virtualization and transitioning to IPv6, to convert the global Internet infrastructure to "Smart Infra: a light and smart infrastructure." Based on this strategy, from August 2010 it made consolidated subsidiaries of the Internet advertising agency Full Speed Inc., FORiT Inc. that operates an affiliate advertising business and provides its proprietary program Affiliate B, and BEKKOAME INTERNET INC. that operates an IT platform business. Aiming to make its services multi-layered, at the same time as entering into the Cloud business, MVNE and MVNO business, and Ad Technology Business, the Company has been conducting structural reforms and technological integration in the companies it has acquired, and it has become a corporate group possessing a complete set of components relating to Internet services.

c) SiLK VISION 2016 (FY4/14 to FY4/16)

The Company next developed its strategy of aiming to expand its main business areas based on its Medium-Term Management Plan SiLK VISION 2016 announced in March 2013 (the vertical integration of the components built up to FY4/13 (multi-layered services), and the horizontal development of the 3 revolution areas of Mobile Revolution, Life Revolution, and Production Revolution).

In the Mobile Business, FreeBit Mobile Inc. was established in January 2015 to operate the smartphone carrier business. In February of the same year in this business, the Company formed a strategic alliance with CCC, and then in March changed the corporate name of FreeBit Mobile to Tone mobile inc., and it became the Company's equity method affiliate (the Company's capital contribution ratio is 49%). On the other hand in the Ad Technology Business, in October of the same year, Full Speed took over the ad network business for smartphones of Liveaid Inc., and in addition, collaborated with IREP Co., Ltd., which is the largest SEM management company in the industry, and founded the joint venture company THINKS Co., Ltd.

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Company History

	History
May 2000	Founded as FreeBit.com Co., Ltd. in Shibuya Ward, Tokyo, to provide Internet business support
June 2000	Started providing services to ISP (communication operators)
December 2002	Changed its corporate name from FreeBit.com Co., Ltd., to FreeBit Co., Ltd.
December 2003	Launched the FreeBit OfficeOne IP Business Phone, an IPv6 compliant IP telephone service for corporations
May 2004	Announced and launched the OverLay Internet technology Emotion Link
May 2006	Launched the VPN service MyVPN for multi-sites and multi-stores
March 2007	FreeBit Co., Ltd. was listed on the TSE Mothers market
August 2007	Made a consolidated subsidiary of DTI that operates an ISP business for individuals
April 2008	Officially launched operations of Karatsu SiLK Hotlines as a call center business
March 2009	Made a consolidated subsidiary of Media Exchange Co., Ltd. (currently merged into DTI), and at the same time, made a consolidated subsidiary of Media Exchange's subsidiary GIGAPRIZE Co., Ltd., which operates a condominiums ISP business
March 2010	Launched the virtual data center service (IaaS) FreeBit CloudVDC (formerly: MeX VDC ENTERPRISE-FARM)
August 2010	Made consolidated subsidiaries of the Internet advertising agency Full Speed Inc., FORiT Inc. that operates an affiliate advertising business and provides its proprietary program Affiliate B, and BEKKOAME INTERNET INC. that operates an IT platform business
November 2010	GIGAPRIZE Co., Ltd. launched the service RentAgent for people renting an apartment
December 2012	Full Speed Inc. launched the advertising management integration program AdMatrix series
July 2013	FreeBit Co., Ltd. launched the MVNE service FreeBit MVNO Pack (formerly: YourNet MVNO Pack) for MVNO through an LC connection with NTT DOCOMO, INC.
November 2013	With the aim of improving efficiency, incorporated the SiLK Hotlines call center business within FreeBit Co., Ltd. and founded Freebit Smart Works Inc.
October 2014	With the aim of improving efficiency in its Internet connection-related business, transferred GIGAPRIZE Co., Ltd. to be a direct subsidiary of FreeBit Co., Ltd.
January 2015	Founded Freebit mobile, inc. to operate an MVNO business
February 2015	FreeBit Co., Ltd. implemented a strategic alliance with the Culture Convenience Club Group
March 2015	Changed the corporate name of FreeBit mobile, inc. to Tone mobile inc. In conjunction with the implementation of a third-party allocation of shares to Culture Convenience Club Co., Ltd, Tone mobile inc. became an equity method affiliate of FreeBit Co., Ltd.
April 2015	Founded freebit investment inc. with the objective of conducting investments for business expansion
October 2015	GIGAPRIZE Co., Ltd. made an equity method affiliate of For Members Co., Ltd., which is a developing a franchise of AEON Housing, the real estate intermediary business of AEON MALL
October 2015	Full Speed Inc. took over the ad network (AID) business for smartphones of Liveaid Inc.
November 2015	Full Speed Inc. collaborated with IREP Co., Ltd., the largest SEM management company in the industry, to found the joint venture company THINKS Co., Ltd., (Full Speed's capital contribution ratio is 49%) and made it an equity method affiliate

Source: prepared by FISCO with reference to the Company's securities reports, homepage, etc.

■ Business descriptions

Provides a wide range of Internet-related services, from infrastructure to consulting and solutions

(1) Group conditions

In addition to the Company, the Company Group is comprised of 11 consolidated subsidiaries, such as DTI, GIGAPRIZE and Full Speed, and 4 equity method affiliates, including Tone mobile.

Overview of the main subsidiaries and affiliates

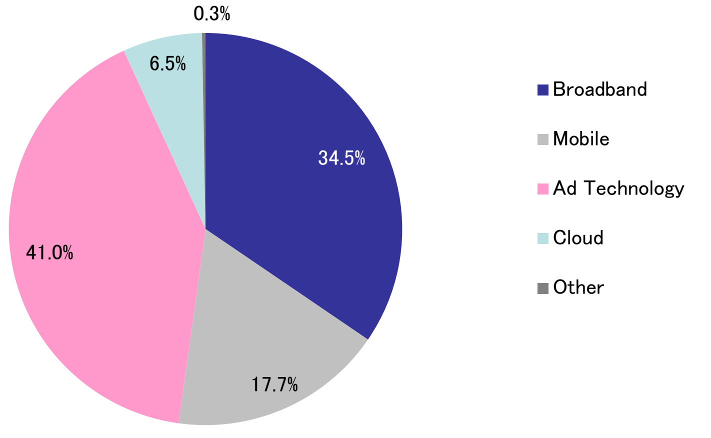
Consolidated subsidiaries	Description of main business
DREAM TRAIN Internet INC.	Internet connection services, Cloud services, services to provide an Internet server environment, high speed mobile communications services
GIGAPRIZE Co., Ltd.	Internet connection services for collective housing (condominiums)
Full Speed Inc.	Internet marketing business, Ad Technology Business
BEKKOAME INTERNET INC.	Platform business (housing service, hosting service, etc.), SaaS (ASP) business (video delivery service, email delivery service, etc.)
FORiT Inc.	Internet advertising agency business, affiliate business, ad network business
freebit investment inc.	New businesses planning, start-up investment, and M&As
Equity method affiliate	
Tone mobile inc.	Smartphone carrier business

Source: prepared by FISCO based on the Company's securities report, homepage, etc.

(2) Business descriptions

In terms of the businesses the Company is involved in, since FY4/16, with the objective of clarifying the future trends in its main businesses, it changed its business segments to the Broadband Business (FY4/16 sales ratio, 34.5%), the Mobile Business (17.7%), the Ad Technology Business (41.0%), the Cloud Business (6.5%), and Other businesses (0.3%).

Percentages of net sales by segment (FY4/16)



a) Broadband Business
The Company, GIGAPRIZE, and DTI conduct this business. Targeting the approximately 300 ISPs nationwide in Japan, the Company provides a high-speed Internet backbone over fixed lines and ISP services to support ISPs' shift to broadband. Also, DTI provides an Internet connection service to individuals, while GIGAPRIZE is developing a business of providing a unified ISP service for condominiums, from the technical survey and design specifications through to maintenance.

In the context of the expansion of the Internet business for condominiums, GIGAPRIZE is aiming to strengthen its provision of a total IT solutions service for the real estate industry. Toward this, in October 2015, it formed a capital and business alliance with For Members Co., Ltd., which is developing a franchise of AEON Housing, the real estate intermediary business of AEON MALL Co., Ltd. <8905> and For Members was made an equity method affiliate (capital contribution ratio of 19.98%). Further, in February 2016, it entered into an OEM agreement with Mitsuuroko Co., Ltd. (an operating subsidiary of Mitsuuroko Group Holdings <8131>), and will start to provide its “Mitsuuroko net” Internet connection service to the Mitsuuroko Group's energy customers of approximately 1 million households, and also to Mitsuuroko's 1,600 corporate members nationwide (both figures are as of the end of January 2016), with the aim of introducing the service into 30,000 households in the first fiscal year.

Its performance for introducing ISP into its main customers of collective housing was 142,228 homes at the end of March 2016 (100,829 homes at the end of March 2015). Its competitors include Internet Initiative Japan Inc. <3774> (hereafter, IIJ) for corporations, and Asahi Net, Inc. <3834>for individuals.

b) Mobile Business
The Company, DTI, and the equity method affiliate Tone mobile conduct this business. As an MVNE, the Company provides “freebit MVNO Pack” as a support package for MVNO entrant businesses. It also sells pre-paid SIM cards and rental routers to foreign tourists visiting Japan, and additionally conducts a smart device business that provides smartphones to Tone mobile. Other than these services, DTI provides the mobile high-speed data communication service DTI SIM, which realizes the most inexpensive plan in the industry.

The freeBit MVNO Pack bandwidth at the end of May 2016 had expanded at a pace of 4.1 times compared to 1 year earlier, due to the growth in the number of users that occurred in conjunction with the increase in the number of companies introducing it. Competitors include Japan Communications Inc. <9424> and IIJ.

Conversely, Tone mobile*1, which is the joint venture company of the Group and CCC, conducts a smartphone career business, mainly providing smartphones to individuals as an MVNO. In November 2015, the Company launched sales of the LTE compliant new terminal TONE (m15) that it developed with the concept of "Quality to provide peace of mind to everyone" (terminal price, ¥29,800; monthly usage fee, ¥1,000) at Futako Tamagawa TSUTAYA ELECTRICS and Daikanyama TSUTAYA BOOKS, and it is expanding the sales network to TSUTAYA directly-managed stores and franchise stores.*2

c) Ad Technology Business
This business is conducted by consolidated subsidiary Full Speed and FORiT, the subsidiary of Full Speed. They utilize the marketing platform AdMatrix*3 series developed in-house by Full Speed, and also Affiliate B*4, a program developed by FORiT to provide highly original Internet advertising solutions services, including for SEO, listing advertising, social media marketing, display advertising, and affiliate advertising.

In October 2015, Full Speed formed a strategic business alliance with IREP <2132> with the objectives of improving the expertise of managed advertising and strengthening the structure for providing services at the highest level in the industry, and they founded the joint venture company THINKS (Full Speed's capital contribution ratio is 49%). Additionally, it is bolstering the Ad Technology Business, including by taking over businesses, such as the ad network business for smartphones of Liveaid.

The main users are around 1,500 companies with no bias toward any particular industry. There are many competitors, including MicroAd, Inc. in the CyberAgent, Inc. <4751> Group, the VOYAGE GROUP, Inc. <3688>, FreakOut, Inc. <6094>, and UNITED, Inc. <2497>.

d) Cloud Business
This business is conducted by the Company, BEKKOAME INTERNET, DTI and GIGAPRIZE. They utilize the data center management expertise cultivated in broadband infrastructure management to provide a wide range of Cloud services, including IaaS*5, SaaS*6, and VPN, and also to provide virtual cyber services and large-scale email systems that utilize the Cloud to the greatest possible extent.

The main users of the virtual data center (VDC) service are corporations, including game companies and TV stations. Conversely, the main users of the Cloud services are both corporations and individuals. In addition to IIJ, competitors include SAKURA Internet Inc. <3778> and Bit-isle Equinix Inc. <3811>.

e) Other businesses
It corresponds to the SI businesses providing services not described above.

Strengths and business risk

One of only a few companies that possess the high-level technological development capabilities and application capabilities to provide a one-stop Internet service

(1) The Company's strength

The Company's strength is that it is one of only a few companies that can provide a one-stop service by offering a variety of multi-layered Internet-related services based on its proprietary technologies. This strength is built on three points: 1) the Company possesses many proprietary technologies that it developed independently, 2) it has the application technological capabilities that enable it to turn these technologies into core component API*7, and 3) it has a business model in which 90% of earnings are from continuous billing.

(2) Business and other risks

Recently, the Company has focused on expanding its Mobile Business and Ad Network Business. Therefore, we think that the risks in these businesses could constitute the greatest risk factors.

*1 It was founded in February 2015 through a capital and business alliance with the CCC Group in order to strengthen its planning and sales force toward capturing 1 million users in the mobile area. Its predecessor was FreeBit Mobile Inc. (founded January 2015), which was based on the Group's smartphone carrier business that it entered-into in November 2013. Its corporate name was changed in March 2015, and following a third-party allocation of shares to CCC, it became the Company's equity method affiliate (the Company's capital contribution ratio is 49%).

*2 It has launched a deployment in stores nationwide, starting with 14 TSUTAYA stores. It is currently expanding this deployment with the aim of opening stores in 200 TSUTAYA stores nationwide by FY3/17.

*3 The advertising management integration platform provided by Full Speed. It maximizes advertising through the integrated management of all marketing phases, from awareness of the advertising among site users through to applications and purchases.

*4 Affiliate refers to an advertising system in which the site manager can receive remuneration in accordance with the results achieved from the listing of client's ads on its sites (homepages, blogs, newsletters, etc.) Affiliate B creates a network from the approximately 550,000 partner sites, and it is being developed for PCs, tablets, smartphones, and other mobile devices.

*5 Infrastructure, such as the equipment and lines needed to operate the information system, which enables services to be used remotely over the Internet.

*6 A mechanism that enables the user to call for and use the software when they need it, such as over the Internet.

*7 A key component. The Company focuses on the development of core components that will become the foundation of its services. It is able to provide a variety of services through combining these component API.

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First, with regards to the Mobile Business, the risks that can be cited are the reduction in mobile phone charges and the launch of Tone mobile. With regards to the reduction in mobile phone charges, when a price reduction by a major communicator operator, such as NTT DOCOMO, is considerable, it has a negative impact on the Company, as its share of MVNO users will decline, causing its results to worsen. But under the current situation, the impact is expected to be limited to the point where sales in which the terminal is free will not be possible, so it is difficult to imagine that a full-fledged price war will develop. So for MVNO, it is highly likely that this will instead have a positive effect, which is why we think it will not be a risk.

With regards to the launch of Tone mobile, its results may fluctuate depending on the progress made in store development and the scale of the investment in advertising expenses. Specifically, while advertising will be conducted in conjunction with the period for store expansion, if the progress made by CCC in its store development is slower than anticipated, the acquisition of users will fall below the target, which will have an adverse effect on sales of terminals and communication services.

On the other hand, the risks for the Ad Technology Business can be considered to be the acquisition of clients for the main products, such as AdMatrix, falling below the target.

Results trends

Achieved record net sales and operating income from the expansions of the Mobile and Ad Technology businesses

(1) FY4/16 consolidated results

In the FY4/16 consolidated results, net sales increased 32.2% year-on-year (y-o-y) to ¥28,389mn, operating income rose 52.9% to ¥1,902mn, and net income attributable to the owners of parent declined 46.1% to ¥553mn, while both net sales and operating income were record highs. The reasons why net income declined despite the record highs was as a reaction to temporary factors in FY3/15, including the recording of gains on a business transfer and from changes in equity, and also because of a rise in net income attributable to non-controlling shareholders.

Overview of the FY4/16 consolidated results

(Unit: ¥mn)

	FY4/14		FY4/15			FY4/16		
	Result	Relative to sales	Result	Relative to sales	% change y-o-y	Result	Relative to sales	% change y-o-y
Sales	20,665	-	21,469	-	3.9%	28,389	-	32.2%
Cost of sales	12,667	61.3%	13,909	64.8%	9.8%	20,177	71.1%	45.1%
Gross profit	7,998	38.7%	7,560	35.2%	-5.5%	8,212	28.9%	8.6%
SG&A expenses	6,677	32.3%	6,315	29.4%	-5.4%	6,309	22.2%	-0.1%
Operating income	1,320	6.4%	1,244	5.8%	-5.8%	1,902	6.7%	52.9%
Ordinary income	1,219	5.9%	982	4.6%	-19.5%	1,322	4.7%	34.6%
Net income attributable to the owners of parent	235	1.1%	1,025	4.8%	335.1%	553	1.9%	-46.1%

Source: Prepared by FISCO based on the Company's financial results summary and financial results briefing materials

Net sales recorded high-level growth in excess of 30% y-o-y, driven by the continuous growth of the Mobile Business and Full Speed's Ad Technology Business. Gross profit rose 8.6% to ¥8,212mn alongside the increase in net sales. But communication costs grew due to the rise in costs to purchase bandwidth in conjunction with the higher sales in the Mobile Business, and also due to the rise in fixed network communication costs. Consequentially, network-related costs increased, so the gross profit margin fell by 6.3 percentage points to 28.9% from 35.2% in the previous fiscal year. Conversely, advertising costs and sales promotions costs fell due to the FreeBit Mobile company split and the reduction in incentives to acquire fixed network customers, and therefore SG&A expenses declined 0.1% to ¥6,309mn (the SG&A expenses ratio was 22.2%, a fall of 7.2 percentage points). As a result of the above, operating income greatly increased and the operating margin rose by 0.9 of a percentage point to 6.7%.

* GIGAPRIZE's FY3/16 consolidated results were net sales of ¥2,928mn (up 34.4% y-o-y) and operating income of ¥463mn (up 29.5%).

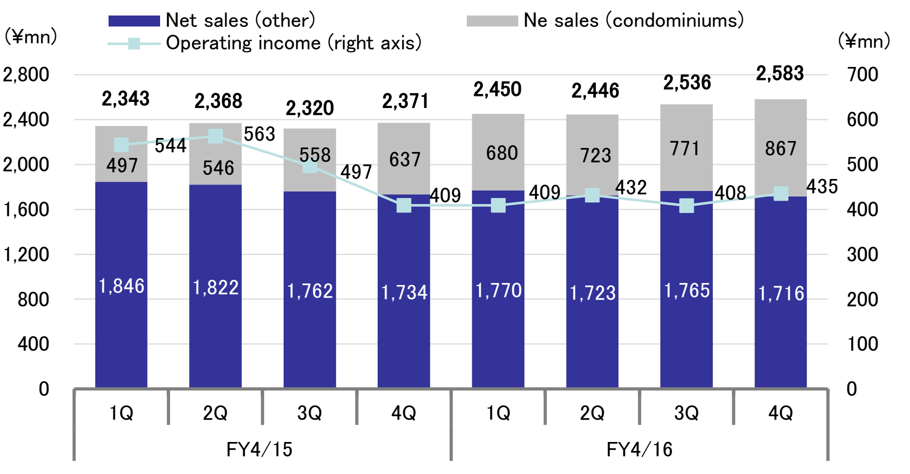
The conditions according to segment are as follows.

a) Broadband Business

Net sales increased 6.5% y-o-y to ¥10,017mn, but segment income decreased 16.3% to ¥1,685mn, for higher sales but lower profits. The main factors behind the increase in sales were the steady expansion of the GIGAPRIZE* Internet service for condominiums (from 100,829 homes in FY3/15 to 142,228 homes in FY3/16, an increase of 41.1% y-o-y) and also the smooth rise in the number of users of DTI Hikari, DTI's Internet service for individuals (user numbers increased by approximately 9.8 times in 1 year). The reasons for the decline in profits despite these higher sales were the impact of negative factors like the lower profits from the fall in sales of the fixed network connection service, and the higher network-related costs following the rise in traffic due to the increase, for example, of viewing of videos via fixed lines.

However, looking on a quarterly basis, it is clear that excluding condominium Internet net sales, the declines in net sales and segment income have both bottomed-out, that the higher condominium Internet sales are covering for the declines in sales and profits in the other areas, and that a return to profitability is in sight.

Trends in the Broadband Business, net sales and segment income



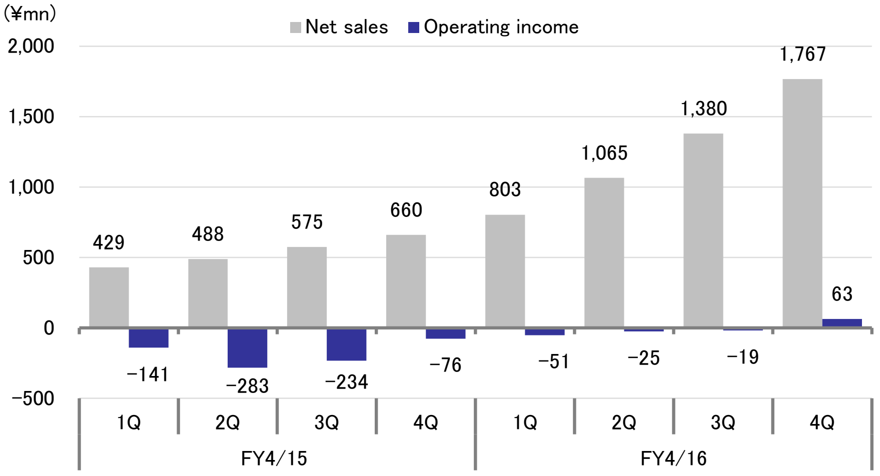
Source: prepared by FISCO based on the Company's financial results briefing materials

b) Mobile Business

Net sales increased 132.9% y-o-y to ¥5,016mn, while the segment loss was reduced to ¥33mn (compared to a loss of ¥736mn in the previous fiscal year). The factors behind this were as follows: the steady acquisition of business subscribers for the provision of the "freebit MVNO Pack," the MVNO package service (as of May 2016, the "freebit MVNO Pack" bandwidth had increased by around 4.1 times compared to the same month in the previous fiscal year); the strong performance of prepaid SIM cards (cumulative sales from February 2015 have exceeded 310,000 SIM cards); in DTI, the significant expansion in the number of contracts (increased by around 4 to 5 times compared to Q2) for "DTI SIM," a mobile high-speed data communication service launched in September of last year; and in the smartphone business, the launch of shipments of "TONE m15" (established a supply system on a scale of hundreds of thousands of units).

■ Results trends

Trends in Mobile Business net sales and segment income



Source: prepared by FISCO based on the Company's financial results briefing materials

c) Ad Technology Business

Net sales rose 44.9% y-o-y to ¥11,691mn and segment income grew 54.5% to ¥908mn, for major increases in both sales and profits. Full Speed recorded significant increases in both sales and profits*1 mainly due to factors including 1) it is focusing on business expansion and is steadily increasing sales of the "AdMatrix" series, a proprietary advertising management comprehensive platform, and 2) its other services, of affiliate advertising and social media marketing, are also trending strongly. Another positive factor was that FORiT increased user numbers to improve its revenue situation, of high in summer but low in winter, and it was able to secure an upward trend in its results.

d) Cloud business

Net sales declined 1.9% y-o-y to ¥1,997mn and segment income fell 21.4% to ¥85mn, to continue the trend of a double-digit fall in profits. The main reason for this was the decline in sales of the legacy services, centered on the housing and hosting services, provided by BEKKOAME INTERNET. However, the new services, of the SaaS*2 backup service "FreeBit Cloud Backup Orchestra"*3 and the IaaS*4 private Cloud service "FreeBit Cloud VDC Private"*5, have been launched and a system is being established to cover the decline in sales from legacy services.

*1 Full Speed's FY4/16 consolidated results were net sales of ¥15,061mn (up 26.4% y-o-y), and operating income of ¥955mn (up 67.9%).

*2 A mechanism that enables the user to call for and use the software when they need it, such as over the Internet.

*3 A backup service for corporations that combines the engine of Acronis of the United States and the Company's technologies to make possible services from daily backup to DR countermeasures.

*4 Infrastructure, such as the equipment and lines needed to operate the information system, that enables services to be used remotely over the Internet.

*5 A service in which the IaaS (Infrastructure as a Service) "FreeBit Cloud VDC" developed by the Company is built not in the FreeBit Cloud environment, but on a private Cloud within the user environment.

Segment net sales and profits

(¥mn)

	FY4/15		FY4/16					FY4/17		
	Result	Relative to sales	Target	Result	Relative to sales	% change y-o-y	% change vs. target	Target	Relative to sales	% change y-o-y
Total net sales	21,469	-	27,000	28,389	-	32.2%	5.1%	35,000	-	23.3%
Broadband	9,405	43.8%	9,675	10,017	35.3%	6.5%	3.5%	11,041	31.5%	10.2%
Mobile	2,154	10.0%	5,273	5,016	17.7%	132.9%	-4.9%	8,451	24.1%	68.5%
Ad Technology	8,069	37.6%	10,305	11,691	41.2%	44.9%	13.5%	14,099	40.3%	20.6%
Cloud	2,037	9.5%	1,891	1,997	7.0%	-1.9%	5.7%	1,899	5.4%	-5.0%
Other businesses	175	0.8%	102	81	0.3%	-53.5%	-20.0%	-	-	-
Adjusted amount	-372	-	-246	-415	-	-	-	-	-	-
Operating income	1,244	5.8%	1,500	1,902	6.7%	52.9%	26.9%	2,000	5.7%	5.1%
Broadband	2,014	21.4%	1,367	1,685	16.8%	-16.3%	23.3%	1,493	13.5%	-11.4%
Mobile	-736	-34.2%	44	-33	-0.7%	-	-	92	1.1%	-377.2%
Ad Technology	588	7.3%	850	908	7.8%	54.5%	6.9%	1,110	7.9%	22.1%
Cloud	108	5.3%	6	85	4.3%	-21.4%	1322.9%	78	4.1%	-8.6%
Other businesses	-90	-51.8%	-149	-147	-181.1%	-	-	-	-	-
Adjusted amount	-639	-	-618	-596	-	-	-	-	-	-

Note: segment net sales are before the elimination of internal transactions
Source: prepared by FISCO based on the Company's financial results summary and briefing materials

Steady accumulation of net assets

(2) Financial position

At the end of March 2016, total assets had increased ¥2,607mn from the end of the previous fiscal year to ¥21,931mn. Breaking this down, current assets rose ¥3,392mn to ¥15,989mn. This was mainly due to increases in cash and deposits of ¥927mn, notes and accounts receivable-trade of ¥1,307mn, and merchandise and finished goods of ¥615mn. In contrast, non-current assets declined ¥784mn to ¥5,942mn, due to factors like a reduction in intangible non-current assets of ¥322mn, including a ¥534mn decrease in goodwill, and a decline in investments and other assets of ¥382mn, such as from a decrease in investment securities.

Liabilities increased ¥2,097mn to ¥10,766mn. This was mainly because current liabilities rose ¥2,066mn compared to the end of the previous fiscal year to ¥9,049mn, including due to increases in short-term loans payable of ¥765mn and accounts payable of ¥1,472mn. Net assets increased ¥510mn to ¥11,164mn, as the negative factors, like the acquisition of treasury stock of ¥263mn, were exceeded by positive factors, including the increases in retained earnings of ¥395mn and non-controlling shareholders' equity of ¥392mn.

Looking at the cash flow situation, the balance of cash, deposits, and equivalents at the end of March 2016 had increased ¥927mn compared to the end of the previous fiscal year to ¥7,911mn. Cash flow provided by operating activities was ¥1,751mn. This was because although trade receivables increased ¥1,307mn, net income before adjustment for income tax increased to ¥1,446mn, and outstanding accounts rose to ¥1,507mn. In contrast, cash flow used in investing activities was ¥508mn, as despite revenue from a business transfer of ¥256mn, expenditures to acquire tangible non-current assets was ¥303mn, to acquire intangible non-current assets was ¥323mn, and to acquire investment securities was ¥156mn. In addition, cash flow used in financing activities was ¥306mn, due to expenditures (net) to repay long-term loans payable of ¥296mn and to acquire treasury stock of ¥297mn.

Looking at the management indicators, while net assets are steadily accumulating, the equity ratio, which expresses financial soundness, declined slightly compared to the end of the previous fiscal year to 45.5%, due to the effects of the acquisition of treasury stock. Conversely, although ROE, which expresses profitability, fell to 5.6% because of a reduction in extraordinary income, both the ROA and the operating margin improved following the higher results.

Balance sheet, cash flow statement, and management indicators

Balance sheet (¥mn)

	FY4/15	FY4/16	Change	Main change factors
Current assets	12,596	15,989	3,392	Cash and deposits +927, Accounts receivable +1,307, Merchandise and finished goods +615
Non-current assets	6,726	5,942	-784	Intangible non-current assets -322, Investments and other assets -382
Total assets	19,323	21,931	2,607	
Current liabilities	6,983	9,049	2,066	Short-term loans payable +765, Accounts payable +1,472, Long-term loans payable scheduled for repayment with 1 year -287
Non-current liabilities	1,686	1,717	30	Lease obligations +59, Long-term loans payable -8
Total liabilities	8,669	10,766	2,097	
(interest-bearing debt)	3,197	3,666	469	Short-term loans payable +765, Long-term loans payable (including scheduled for repayment within 1 year) -296
Net assets	10,654	11,164	510	Retained earnings +395, Non-controlling shareholders' equity +392, Treasury stock -263
Total liabilities and net assets	19,323	21,931	2,607	

Cash flow statement

Operating CF	2,207	1,751	
Investing CF	-524	-508	
Financing CF	585	-306	
Cash and equivalents	6,983	7,911	927

Management indicators

<Soundness>		
Current ratio	180.4%	176.7%
Equity ratio	50.9%	45.5%
D/E ratio	32.5%	36.8%
<Profitability>		
ROE	12.9%	5.6%
ROA	5.4%	6.4%
Operating margin	5.8%	6.7%

Source: prepared by FISCO based on the Company's financial results summary and briefing materials

Based on the growth in the existing businesses, is aiming to expand by launching new businesses in the three fields of "Health Tech," "IoT", and "Real Estate Tech"

(3) The SiLK VISION 2020 medium-term business policy

Following the end of SiLK VISION 2016, which was the medium-term management plan announced in March 2013 that ran up to FY4/16, the Company has announced SiLK VISION 2020 as its medium-term business policy up to FY4/20. The policy describes its consolidated results targets for FY4/20 of net sales of ¥50bn and operating income of ¥5bn from the FreeBit Group's commitment to its external markets.

This basic policy outlines the goal of achieving business expansion in the medium to long term by aiming to realize growth by strengthening its existing businesses in the areas of "mobile" and "ad technology," and launching new businesses in the three fields the Company cited in SiLK VISION 2016, of "Health Tech," "IoT," and "Real Estate Tech" within the "Life Revolution" area.

Initiatives in the medium-term business policy by the Group's main companies

Company name	Descriptions of the initiatives
FreeBit	Generate revenue from launching and promoting a "health care" related new business, and the launch of a new mobile communications service that is bundled with surveillance cameras and various sensors
GIGAPRIZE	Launch of a living environment-related business aiming to increase scale
Full Speed	Product development compliant with the latest advertising technologies, such as video- and AI-related, and the launch of an app business for foreign visitors to Japan
DTI	Strategic expansion of "DTI SIM," a mobile service for consumers
freebit investment	Actively investing in businesses according to themes, including Health Tech, Fin Tech, Real Estate Tech, IoT, and inbound demand from foreign visitors to Japan

Source: the Company's financial results briefing materials

With regards to the three fields in the Life Revolution area, for "IoT" the Company plans to launch in the summer a new mobile communication service bundling surveillance cameras and various sensors. For "Health Tech," it will launch new businesses (the specific details are currently being considered), and it plans to develop them to cooperate with Full Speed, which has related clients in the same field, and thereby pursue synergy effects. For "Real Estate Tech," GIGAPRIZE, which specializes in businesses related to real estate, is planning initiatives using its existing business as a foothold.

Prior investment to launch new businesses, centered in "Health Tech," will keep down growth in operating income to single digit

(4) The FY4/17 Company targets

The Company's targets for the FY4/17 results are for a double-digit increase in net sales, a single-digit increase in operating income, but a decline in net income, with net sales forecast to rise 23.3% to ¥35,000mn, operating income to grow 5.1% to ¥2,000mn, but net income attributable to the owners of parent to fall 54.8% to ¥250mn.

Overview of the FY4/17 Company targets

(¥mn)

	FY4/16		FY4/17		
	Result	Relative to sales	Target	Relative to sales	% change y-o-y
Net sales	28,389	-	35,000	-	23.3%
Operating income	1,902	6.7%	2,000	5.7%	5.1%
Ordinary income	1,322	4.7%	1,500	4.3%	13.4%
Net income attributable to the owners of parent	553	1.9%	250	0.7%	-54.8%

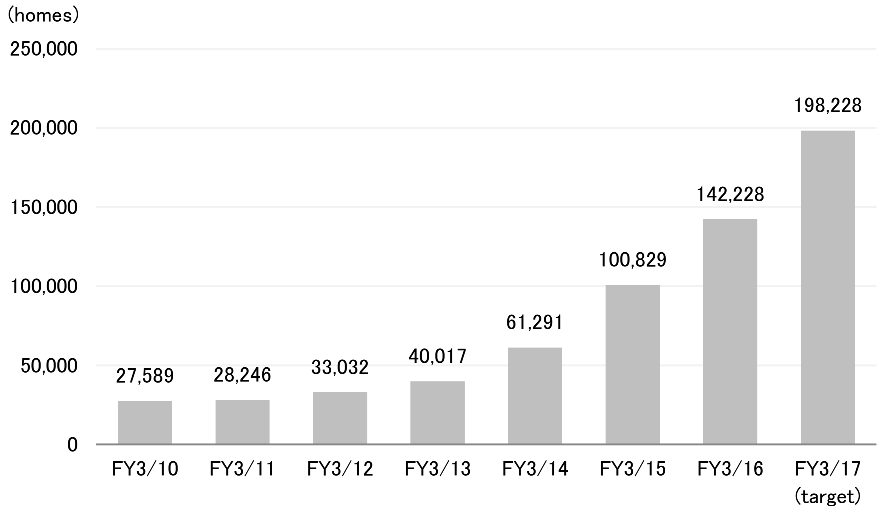
Source: prepared by FISCO based on the Company's financial results summary and briefing materials

The same as in the previous fiscal year, it is thought that the main reason for the double-digit increase in net sales will be the expansion of the Mobile Business and the Ad Technology Business. The reason why despite the higher sales, operating income will only increase by a single digit is because the forecast incorporates the prior investment of ¥500mn to ¥600mn in order to launch the new businesses, centered on “Health Tech.” In addition, the expected major decline in net income is from the fact that the temporary factors that occurred in the previous fiscal year, including a gain on the sale of a business, are not expected in this fiscal year, and also due to factors like an increase in income tax from the strong results recorded by the subsidiaries (approximately ¥240mn), and that net income attributable to the non-controlling shareholders of GIGAPRIZE and Full Speed (approximately ¥500mn) will be recorded.

The forecasts for each segment are as follows.

a) Broadband Business
Net sales are forecast to increase 10.2% y-o-y to ¥11,041mn, but segment income to decrease 11.4% to ¥1,493mn. The main reason for the higher net sales is from the steady expansion of the condominium Internet service, including from the effects of the partnership with Mitsuuroko. But despite this, profits are forecast to decline because of the rise in network costs, such as from the increase in the use of rich content.

Trends in the results for the introduction of the condominium Internet service



b) Mobile Business
Net sales are forecast to increase 68.5% to ¥8,451mn and segment income to achieve profitability at ¥92mn (compared to a loss of ¥33mn in the previous fiscal year). The reasons for this are the continued expansion in sales of the “freebit MVNO Pack” from its improved name recognition in the MVNE and MVNO markets; the fully fledged launch of sales of “Mobabiz,” a new Cloud-based PBX service; and also the growth in sales of the smartphone business for the sales of handsets for Tone mobile, which is occurring alongside the store openings within TSUTATA stores.

Within these efforts, Mobabiz, which was announced in March, is a service in which calls can be made and received not in the usual way of installing a PBX in the user’s office, but through a smartphone that is installed with a specialist app and that uses an extension call function and a fixed telephone number. The Company has concluded a sales agency agreement with IE Group, Inc. in the HIKARI TSUSHIN, INC. <9435> Group, and in addition, it is cooperating with 300 dealers and aiming to expand its share of the business phone market that is said to be worth ¥150bn a year.

The Mobabiz business model includes the following points; 1) it ensures the quality of the business-use calls through utilizing patented technologies, including the Company’s proprietary Emotion Link (Emotion Link Active Node)* technology, 2) the call charge is reduced by up to 78%, 3) it reduces sound equipment and maintenance costs through utilizing NTT optical calls and putting PBX on the Cloud, 4) it promotes BYOD (Bring Your Own Device), in which employees can utilize for work their own smartphone, and 5) calls can be made and received by smartphone using a fixed telephone number (0AB-J).

* Ubiquitous network solutions to realize safe and secure communications by connecting every type of information device to the Internet using the OverLay Internet.

c) Ad Technology Business

Net sales are forecast to rise 20.6% y-o-y to ¥14,099mn and segment income to grow 22.2% to ¥1,110mn, for double-digit increases in both sales and profits. This is because the results of the existing businesses of Full Speed and FORiT are expected to trend strongly.

d) Cloud business

Sales and profits are expected to once again fall, with net sales declining 4.9% y-o-y to ¥1,899mn and segment income decreasing 8.4% to ¥78mn. But the decline is forecast to slow down. This will be because while the rate of decrease for legacy services of housing and hosting will be reduced, the Cloud infrastructure service will expand, centered on the virtual data center (VDC).

Returning Profits to Shareholders

Basic policy is to continuously return profits to shareholder from a medium- to long-term perspective

The Company's basic policy is to develop and expand its business for the future by retaining the internal reserves necessary to strengthen its management foundations and financial position while prioritizing continuous returns of profits to shareholders at the same time as obtaining their understanding on its policy for the business expansion that it is aiming for from a medium- to long-term perspective. With regards to the payment of dividends from retained earnings, the Company appropriately returns profits to shareholders in consideration of the progress made in its Medium-Term Management Plan and business performance in each respective consolidated fiscal year.

In accordance with this policy, the Company plans to pay a dividend of ¥7 in FY4/16 (dividend payout ratio of 28.3%). It also intends to continue to pay a dividend per share of ¥7 in FY4/17 (dividend payout ratio of 78.2%).

The Company conducted a share buyback with the objectives of raising value per share and implementing a flexible capital policy in response to changes in its management environment (number of shares acquired, 350,000 shares; acquisition period, September 14 to October 1, 2015; total cost of acquisition, ¥263.9mn).

Other than this share buyback, the Company has acquired its own shares on two other occasions in the past. The same as with the most recent buyback, the objectives were to raise value per share and to implement a flexible capital policy in response to changes in its management environment. But it is considered that this was because the share price was judged to have remained undervalued due to the previous slump in results. At FISCO, when considering that presently the results have clearly changed direction toward a full-fledged growth trend, going forward we consider that the Company will continue with its policy of returning profits to shareholders through stably paying dividends and conducting share buybacks.

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