

Aeria Inc.

3758

TSE JASDAQ

4-Nov.-2020

FISCO Ltd. Analyst

Kimiteru Miyata



FISCO Ltd.

<http://www.fisco.co.jp>

■ Index

■ Summary	01
1. Operates IT services, contents, and asset management businesses	01
2. Formulated management policy for 2H FY12/20 and FY12/21 onward premised on “with COVID-19” conditions	01
3. Operating profit declined in 1H FY12/20 due to impact of COVID-19	01
4. Anticipating an earnings bottom in FY12/20 and recovery in profitability and growth potential over the medium term	02
■ Company profile	03
1. Company profile	03
2. History	03
■ Business overview	05
1. Business description	05
2. IT services business	05
3. Contents business	06
4. Asset management business	10
■ Management policy for “with COVID-19” conditions	11
1. Management philosophy	11
2. Management policy in 2H FY12/20	12
3. Future management policy	12
■ Results trends	13
1. 1H FY12/20 results trends	13
2. FY12/20 outlook	15
3. Medium-term growth scenario	16
■ Shareholder return policy	16
1. Dividend	16
2. Shareholder benefit program	17
■ Information security	18

*This is an English translation of a report issued on October 5, 2020.

■ Summary

Aiming to improve profitability and growth potential with a portfolio of three businesses

1. Operates IT services, contents, and asset management businesses

Aeria <3758> (hereinafter referred to as “the Company”) has three main business areas - IT services, contents, and asset management. The IT services business handles data services and an affiliate* platform, the contents business develops smartphone games and handles related businesses, and the asset management business consists of real estate sales and planning, minpaku operation, and other areas. The Company steadily expanded contents business and asset management business by leveraging M&A supported by stable income from IT services business in past years. This strategy contributed to a major hit with the A3! smartphone game, acquisition of the popular Ikemen game series, and expansion of IP business in the contents business and establishment of a business format in the asset management business. Within this context, despite the impact of COVID-19 on results, the Company aims to rebound by leveraging its effective portfolio consisting of three businesses.

* Affiliate: This is an advertising method of receiving compensation from parties selling products when an introduction of the product on SNS or other services results in a purchase.

2. Formulated management policy for 2H FY12/20 and FY12/21 onward premised on “with COVID-19” conditions

The Company formulated a management policy premised on “with COVID-19” conditions that will rigorously promote selectivity and focus and improvement in profitability to address the impact of COVID-19. While contents business is likely to be the main target, particularly during 2H FY12/20, the initiative advocates early suspension and exit from titles that lack sufficient cost-effect performance and priority on new development that supports opportunity in IP business. Furthermore, the Company intends to curtail high-cost outsourcing and promote profitability improvement by advancing in-house production within the group. Over the medium term, it prepared policies that factor “with COVID-19” conditions into existing goals, including realization of business portfolio composition that generates stable earnings, creation of synergies within businesses and among businesses, subsidiary profitability enhancement and reorganization, and active development in growth markets that utilize the group’s business assets. The Company also plans to actively harness other company IP and external business resources through establishment of joint ventures and provision of know-how to accelerate IP business developments.

3. Operating profit declined in 1H FY12/20 due to impact of COVID-19

In 1H FY12/20, the Company reported ¥14,077mn in net sales (-2.3% YoY) and ¥154mn in operating profit (-91.6%). Profit fell mainly because of the global COVID-19 outbreak which spread rapidly from February 2020 onward. IT services business was relatively stable, despite weaker affiliate advertising income, because of steady income in data services business. Asset management business, however, posted higher sales because of the property transfer period; despite this, the business experienced a profit setback from upfront costs amid lack of progress in acquiring new properties and a shortage of attractive properties as financial institutions adopted stricter financing policies. Contents business incurred the weakest results among the three businesses on account of suspensions and delays of events and promotions along with new contents development costs and promotional costs. The Company also booked impairment losses after considering asset recovery prospects and other factors. This put net profit attributable to owners of the parent at a ¥4,311mn loss (compared to a ¥1,044mn profit in the previous year).

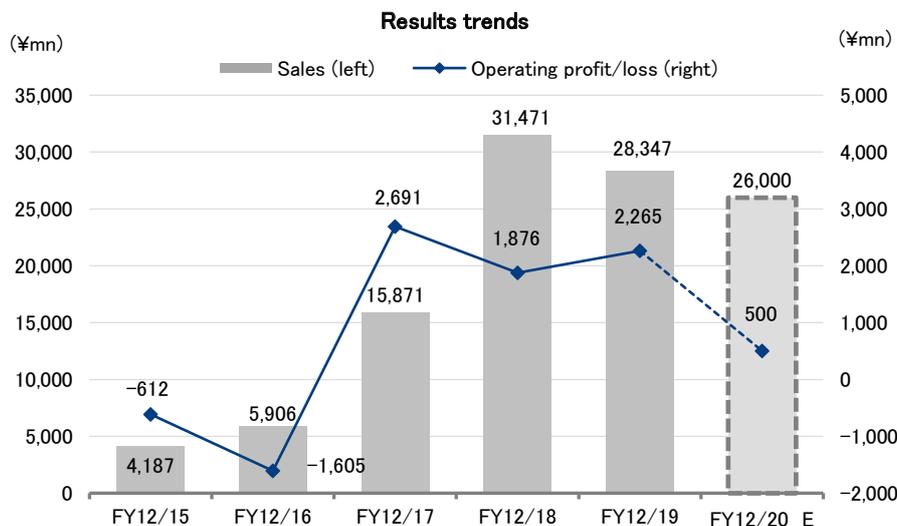
Summary

4. Anticipating an earnings bottom in FY12/20 and recovery in profitability and growth potential over the medium term

In FY12/20 guidance, the Company projects ¥26,000mn in net sales (-8.3% YoY) and ¥500mn in operating profit (-77.9%). It plans to revive earnings through selectivity and focus and improvement in profitability. IT services business will hold strategy seminars for affiliates and take other steps to strengthen the platform. Given the possible impact from promotion shortages due to event suspensions and delays on 2H, contents business will offset this effect with infection measures and initiatives to control capacity (volume) along with online-based promotions. Asset management business, which is currently experiencing gradual recovery including new properties and credit provision conditions, will provide highly convenient services and other support to buttress the recovery trend. The Company hopes to revive profitability and growth potential over the medium term from a bottom in FY12/20 with these measures.

Key Points

- Achieved growth in contents business with the A3! hit, CYBIRD acquisition, and expansion of IP business
- IT services business is stable, and the Company is bolstering asset management business with reinforced online activities
- Seeks rebound from COVID-19 impact with selectivity and focus and improvement in profitability and targets profitability and growth potential recovery from FY12/21



Source: Prepared by FISCO from the Company's financial results

■ Company profile

Steady business evolution accompanying advances in the network society

1. Company profile

The Company has three main business areas - IT services, contents, and asset management. The IT services business handles data services, system development business, and provision of an affiliate platform. Contents business mainly develops, distributes, and operates smartphone and tablet games and also implements IP business*¹ that includes selling music CDs and character goods and holding 2.5D stage events*² and other events and live shows. Asset management business sells and handles leasing and management of properties and provides consulting and online services. Since its founding, the Company has aimed to “become an essential presence, similar to air, in the network society” by actively harnessing Internet and mobile technologies and keeping pace with the development of network society. With this spirit, it has taken on challenges in many businesses since being founded.

*1 IP business: Business model that seeks to increase income by broadening application of IP (intellectual property rights) to peripheral business and leasing and selling IP to others

*2 2.5D stage events: Musicals and other 3D theater contents based on 2D animation, games, and other contents and ideas

Stage of targeting synergies within businesses and among businesses

2. History

Takayuki Nagashima, Chairman and Representative Director, and Yusuke Kobayashi, President and Representative Director, founded predecessor Communications Online to deliver Internet-related information provision services in Chiba Prefecture in 1998. The Company entered the game industry (online games) with the acquisition of Game Pot (later absorbed by GMO Group) in 2001, established Aeria in 2002, and listed shares on the Osaka Stock Exchange’s Hercules market (now Tokyo Stock Exchange JASDAQ market) in 2004. Leveraging income from IT services business Air Internet Service Co., Ltd. acquired in 2005, it expanded to smartphone games, affiliate platform business, and other areas. It entered the real estate business and launched the asset management business in 2017. The Company is currently seeking manifestation of synergies within individual businesses and among businesses following exhaustion of M&A-driven expansion of business scope. Furthermore, since it has successfully cultivated game characters and other IP into a major income source, the Company is also moving forward in strengthening peripheral businesses that utilize its IP. While the global COVID-19 outbreak in 2020 affected the Company as well, management is promoting further synergies within businesses and among businesses and broader IP business through selectivity and focus and improvement in profitability and thereby seeking recovery in profitability and growth potential.

Aeria Inc. | 4-Nov.-2020
 3758 TSE JASDAQ | <https://www.aeria.jp/ir/>

Company profile

History

Date	Event
May 1998	Established Communication Online Ltd.
September 1999	Established internetcom K.K. (merged with US-based Jupitermedia, capitalized at ¥20mn)
May 2001	Established Gamepot Inc. (merged with Gagamel.com (Korea); capitalized at ¥20mn)
October 2002	Established Aeria Inc. (through spin-off)
December 2004	Listed on Osaka Stock Exchange's Hercules Market (stock code: 3758)
November 2005	Acquired 100% of shares in AIR Internet Service Co., Ltd., making it a wholly owned subsidiary
December 2005	Listed Gamepot Inc. on Sapporo Stock Exchange's Ambitious Market
December 2005	Established Aeria Finance Inc. as wholly owned subsidiary to run investment business
April 2006	Acquired 20% stake in Yutaka Shoji Co., Ltd., making it an equity-method affiliate
August 2006	Acquired 50.1% stake in ACQUIRE Corp., making it a subsidiary
August 2006	Established Aeria Games & Entertainment, Inc.
October 2006	Established Aeria IPM, Inc. as wholly owned subsidiary to oversee copyrights
June 2007	Acquired 100% of shares in Kurezo Co., Ltd., making it a wholly owned subsidiary
June 2007	Acquired 41.3% stake in Taiko Holding Co., Ltd. (owner Akatsuki Securities), making it a subsidiary
January 2008	Began offering email delivery ASP services through AIR Internet Service
March 2008	Added vulnerability detection tool (<i>Retina</i>) as part of standard service through AIR Internet Service
April 2008	Transferred all shares in consolidated subsidiary Gamepot Inc. to So-net Entertainment Corp.
July 2008	Acquired Daito Me Co., Ltd. through share exchange, making it a wholly owned subsidiary
July 2008	Began offering carbon offset support program through AIR Internet Service
August 2008	Established European subsidiary as subsidiary of US-based Aeria Games & Entertainment, Inc.
September 2008	Began business partnership with aprecio Corporation
March 2009	Began offering groupware ASP for Cybozu Office 8 through AIR Internet Service
July 2010	Began offering cloud-based service to help prevent misdirected email through AIR Internet Service
December 2012	Removed Aeria Games & Entertainment, Inc. from subsidiaries by establishing AGGP Holdings, Inc. as an intermediary holding company
December 2014	Acquired Gamania Digital Entertainment Inc. through share exchange, making it a wholly owned subsidiary
April 2015	Acquired Infotop Capital Corp. through share exchange, making it a wholly owned subsidiary and making Infotop Corp. (now First Penguin) a second-tier subsidiary
June 2015	Acquired Liber Entertainment Inc. through share exchange, making it a wholly owned subsidiary
October 2015	Acquired ASGARD Co., Ltd. through share exchange, making it a wholly owned subsidiary
December 2015	Acquired GESI Co., Ltd. through share exchange, making it a wholly owned subsidiary
June 2017	Completed transition of Arithmetic Inc. as a wholly owned subsidiary through simple share exchange
July 2017	Acquired GOODVISION CORPORATION through simple share exchange, making it a wholly owned subsidiary
July 2017	Acquired Twist Inc.*, making it a subsidiary
August 2017	Acquired Impression inc. through simple share exchange, making it a wholly owned subsidiary
August 2017	Acquired Sakuragate Inc. as wholly owned subsidiary through simple share exchange
August 2017	Acquired eitarosoft, inc. through simple share exchange, making it a wholly owned subsidiary
September 2017	Acquired Xenoverse Inc. through simple share exchange, making it a wholly owned subsidiary
October 2017	Acquired GG7 Inc. through simple share exchange, making it a wholly owned subsidiary
November 2017	Acquired Total Management Corporation, making it a subsidiary
January 2018	Entered into agreement to establish joint venture company with Wanin International Co., Ltd.
February 2018	Acquired shares of Seisyou Co., Ltd., making it a subsidiary
June 2018	Acquired CYBIRD Co., Ltd., making it a wholly owned subsidiary
January 2019	Sold eitarosoft, Inc. and Seisyou
January 2019	Established Aeria Contents Holdings Inc. as an intermediate holding company in the contents business
January 2019	Established Aeria One Inc. as an external alliance contact point for group company assets
April 2019	Established Celebrate Message Inc. that lets users submit an offer to famous CASTs that requests a personal message
November 2019	Acquired shares of Invest Online, Inc. to acquire it as a subsidiary

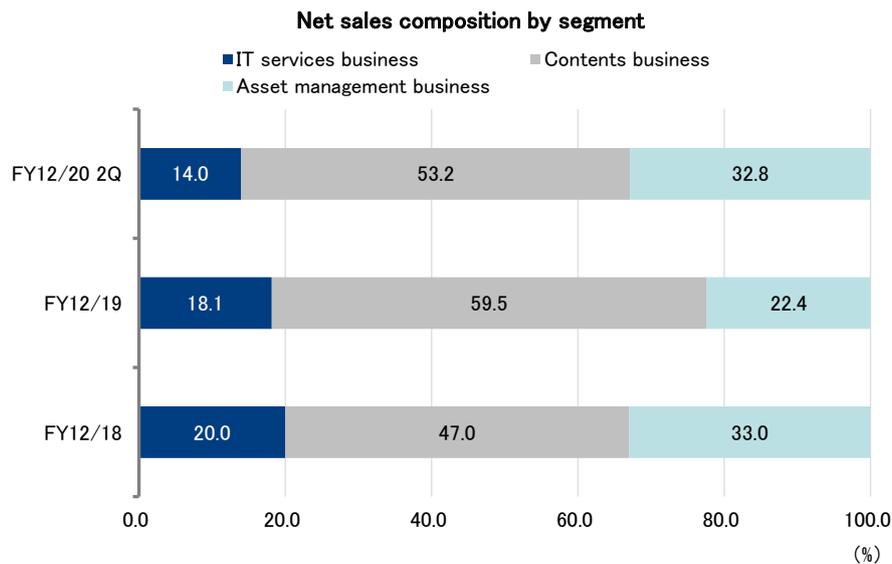
Source: Prepared by FISCO Inc. from the Company's website

Business overview

Business portfolio with three businesses that complement each other

1. Business description

In IT services business, mainstay AIR Internet Service Co., Ltd. and First Penguin Inc. are sustaining stable income. The contents business is cultivating and expanding IP business against a backdrop of popular smartphone games, including CYBIRD's Ikemen series and Liber Entertainment's A3! and I★Chu. The asset management business has readied teams for planning, procurement, sales, and operation while controlling risks associated with real estate business. In FY12/19, the net sales composition by segment was 18.1% for IT services, 59.5% for contents and 22.4% for asset management; in 1H FY12/20, these figures were 14.0%, 53.2%, and 32.8%, respectively. While segment sales ratios are adjusted in response to the external environment, we think these results indicate that the Company has assembled a portfolio of businesses that effectively addresses business risk.



Source: Prepared by FISCO from the Company's results briefing materials

Data service and ASP businesses offer stable income sources

2. IT services business

Main businesses in the IT services segment are AIR Internet Service, which operates a data service business; First Penguin, which operates an ASP* business; and companies that provide system solutions and consulting, social app development, and social media assistance.

* ASP (Affiliate service provider) refers to management of sales and compensation payments between sellers and introducers and handling of payments and product transfer service between sellers and buyers as a broker connecting sellers, buyers, and introducers.

Business overview

AIR Internet Service provides various internet services for businesses, including its cloud-based email solutions service (All in One Mail), a cloud-based reservations management system (Reserve Keeper) for restaurants, proprietary WEBooth hosting services (which comes with its own online storage service), and ISP* services for domain registration and other website-related services. With the bulk of its business stemming from its data center operations, AIR Internet Service generates an exceptionally steady stream of revenues and earnings. While use of smartphones and other portable devices has risen with advances in telework recently, the Company is reinforcing security measure functions and options for this usage. Main new services aimed at telework include the mobile device management (MDM) app for security measures, including remote lock when handsets are lost, “Active! zone” hosting service that debilitates targeted mail attacks, and optional display of country path information for identification of suspicious mail using path information. Management hopes to utilize these services to acquire new customers and promote upselling to existing customers.

* ISP (Internet Service Provider): This refers to a business operator that provides connection to the Internet over public communication lines, etc.

First Penguin operates “infotop,” an Internet commerce portal site (platform) that handles a wide range of information goods (*), in mainstay ASP business. Registered “infotop” sellers, buyers, and introducers have totaled more than 3.3mn people up to now, and the platform handles over 85,000 information products. This business generates strong, stable income. While this business model has similarities to Rakuten Ichiba, it differs substantially in terms of only handling a single category (information goods), managing commercial flow, and using introducers (affiliate partners). Other businesses besides ASP include advertising business that capitalizes on ASP business knowhow, contents production business that converts knowledge and knowhow to contents, payment business that utilizes AQUAGATES payment service, and human resource business that supports job hunts in Japan and other countries. AQUAGATES deployed Paidy (next-month payment), an online payment service that accommodates a wide range of payments without requiring advance registration, in October 2019.

* Information goods: Information on asset management, personal enhancement, and other topics provided as a good with strict review standards

Full utilization of IP business facilitated by CYBIRD

3. Contents business

In contents business, the Company has supplied games to the platforms of each era, including PCs, mobile phones, and smartphones. While smartphone games are currently the most popular offerings, the Company has earned praise for developing smartphone games and has increased hits in recent years. The Company acquired CYBIRD, which owns blockbuster Ikemen series content, and is broadening the line-up of hit games as well as expanding IP business by utilizing characters cultivated in hit titles for other opportunities besides games.

Business overview

(1) CYBIRD

CYBIRD, which the Company acquired as a subsidiary in June 2018, is a longstanding smartphone game firm with a respected presence in puzzle games and astrology, and provides new technologies, such as voice service solutions based on Amazon Echo, Google Home, and other Voice UI*. CYBIRD's primary income source is the Ikemen series, a romance game with strong storylines geared toward women. The cumulative number of members for the series exceeds 30mn people worldwide, including Japan, North America, and Asia. It is a blockbuster product with 13 distributed titles and receives overwhelming support in the game market for women. The Company's acquisition of CYBIRD as a subsidiary not only strengthened the line-up but also enabled the knowhow accumulated by CYBIRD over a period of 20 years in overseas initiatives and IP business development to be applied to the group's other games and characters.

* Voice UI: This is an AI-equipped user interface that utilizes voice input. This service is actively provided by Amazon and Google.

As a new title, CYBIRD released "Ikemen Prince – Beauty and the Beast Final Love" in July 2020 that lets users experience painfully sweet romance with eight princes who have a "beast" interior based on the French folktale "Beauty and the Beast." This is a major release that commemorates the eighth year of the Ikemen series and was very popular ahead of the actual release with pre-registration at more than 100,000 people. CYBIRD has organized a multi-faceted campaign that includes the launch of the "Ikemen Fan Club (IFC)," the first official fan club, a special site on dating, and special benefits for IFC Diamond members. The Ikemen series is a long-lived business as seen in Fukuchiyama's (Kyoto) selection of Mitsuhide Akechi, a popular character in "Ikemen Sengoku –Romances Across Time" released five years ago, as its PR Warlord in spring 2020.

"Ikemen Prince – Beauty and the Beast Final Love" (left) and Mitsuhide Akechi from "Ikemen Sengoku –Romances Across Time" (right)



Source: The Company's results briefing materials

CYBIRD naturally applies IP business to the Ikemen series. It broadens income scope by using characters that capture fan support from game hits (taking on a presence of their own) and other IP in animation, CDs, events, theater, publishing, and other non-game areas and also offering peripheral goods and services by increasing venue and time contact with fans, including digital and real environments. Reinforced promotion of IP business creates a positive spiral of simultaneously diversifying income opportunities and distributing risk via enhanced IP brand clout and a rebound effect of stronger IP clout on game earnings capacity. As explained below, while CYBIRD previously had a policy of cultivating its own IP, management updated the policy to increasing income opportunities by applying IP business knowhow to other company IP too because it takes time to cultivate native IP and CYBIRD has reached a level at which it can fully leverage IP business knowhow. For example, the Company launched an examination program for "Incredible Zorori," a longstanding popular children's book, in July 2020.

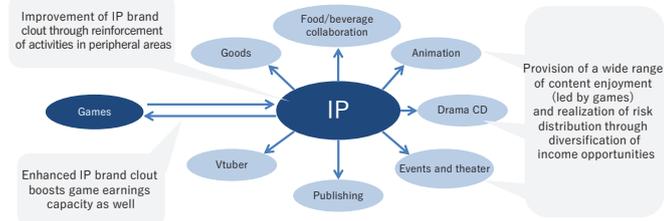
Aeria Inc. | 4-Nov.-2020
 3758 TSE JASDAQ | <https://www.aeria.jp/ir/>

Business overview

“Ikemen series” eighth year campaign (left) and IP business emanating from games (right)



Source: The Company's results briefing materials



(2) Liber Entertainment

Liber Entertainment is a core company in the contents business that develops and operates smartphone games, develops consumer games, and operates consulting business for games as its main businesses. It has achieved success by steadily developing games with focus on Ikemen training games for women and delivered a hit with the I★Chu smartphone game in 2015 as well as a major hit with A3! in 2017. It is also expanding business scope to peripheral businesses that utilize its IP. Hit products have an effect for three years, and broadening to peripheral businesses can extend the period even more. This is a well-performing subsidiary that is currently truly ready for growth.

A3! is an Ikemen training game in which the player assumes the role of director at a run-down theater on the verge of closing and trains new Ikemen actors through rehearsals and makes the production a success. The entire series is dubbed with voices, and minigames have been recorded to generate additional income. Liber Entertainment started service in January 2017. A3! has been a major hit, reaching 7mn downloads in June 2020. IP business activities include music CDs, comic anthologies, and other goods and well-received MANKAISTAGE A3! and other 2.5D events and SEASON SPRING & SUMMER animation. Furthermore, ahead of the third-version A3! release, Liber Entertainment opened Velvet BOOK STORE pop-up stores at Animate stores nationwide and Ikebukuro PARCO and is distributing the Spotlight theater magazine. It aims to make this a long-running business through synergies with IP business.

Concept image for A3! (left) and Velvet BOOK STORE (right)



Source: The Company's results briefing materials



Business overview

Liber Entertainment also has multiple other hits besides A3!, Soen No Kantai, which became its first hit for men, is a full-fledged naval battle game in which the player becomes the general commander of the Soen fleet and battles with a mysterious enemy, the shadow fleet. In September 2020, it implemented a limited event with Tsuburaya Production’s Ultra Monsters IP. Liber Entertainment provides CUE!, a training game for a beautiful girl voice actor that targets men. This game places strong emphasis on the entertainment aspect that transcends the boundary between real and virtual through training a voice actor using the actual voice of a new female voice actor. Management aims to promptly expand IP business. These products have all been hits with over 1mn downloads each. Recently, Liber Entertainment started distribution of I★Chu Etoile Stage, the second release in the I★Chu series, a hit romance rhythm adventure game to train an idol, in April 2020. The new version changed visuals and conducted a full-voice revision and full rewriting of the main story that facilitate even more enjoyment of the I★Chu world. Liber Entertainment is proceeding with animation and theater versions as well.

Image from CUE! (left) and image from I★Chu Etoile Stage (right)



Source: The Company’s results briefing materials

(3) Changes achieved with IP business

Arithmetic Inc., which sells contents for women, has performed well since 2019 by broadening contents, including DYNAMIC CHORD, Starry☆Sky, and Forbidden Romance series, and expanded scope from character goods to music CDs, theater, and games. This uptick in business at Arithmetic, which has its own IP, is an outcome of the Company’s reinforcement of IP business. Additionally, celebrate message service started in April 2019 sends a personal message from a famous person for customer celebrations, such as a birthday or wedding. This service facilitates offers to celebrities, athletes, artists, talents, and others, including Yuto Nagatomo, a soccer player on Japan’s national team, and model and talent Yuki Poyo (Yuki Kimura), and is a business that uses other company IP, similar to Incredible Zorori.

In this way, the Company has increased momentum in IP business since acquiring CYBIRD as a subsidiary. CYBIRD’s knowhow in IP business accumulated over 20 years has been a major factor as explained above. Another important driver of further inroads by IP business in the contents business as a whole is Aeria Contents Holdings (ACH), established in 2019. ACH is an intermediate holding company in the group and was formed to realize synergies among the group’s contents business companies. The effect has been dramatic with IP business spreading rapidly to the entire contents business. Beyond contents business, the ACH effect has contributed to optimizing development and operational organizations at contents business companies and knowledge sharing through reinforcement of management structures utilizing CYBIRD’s corporate functions and optimal assignments of human resources. It is also positively affecting organizational operation and management structures for the entire group.

Aeria Inc. | 4-Nov.-2020
 3758 TSE JASDAQ | <https://www.aeria.jp/ir/>

Business overview

CYBIRD is making steady advances in its own IP business as well, such as development of businesses in new fields using Vtubers*, Voice UI, and other IP. FaneX, a fan loyalty support service, deserves attention as well. CYBIRD started the ultimate form of IP business with a fan club for the Ikemen series and is applying knowhow obtained from this effort to areas inside and outside of the group. It plans to support fan business ranging from goods and exams to portal site construction, Vtuber and Voice UI utilization, and events and live shows. It also appears to be considering use of FaneX to cultivate not only its own and other company IP but also electronic comics, electronic novels, and other indies IP. We think this initiative is premised on conversion to a 5G mobile communications system with high capacity and fast speed. Management realizes that 5G offers the opportunity to improve the sophistication and complexity of games and IP and promote further refinement and expansion of peripheral businesses. As this happens, ACH is likely to broadly and quickly spread new knowhow throughout the group to drive business. Since the Company is unlikely to have a large volume of new releases in game development due to taking more care to ensure investment recovery, IP business initiatives hence should be given more attention.

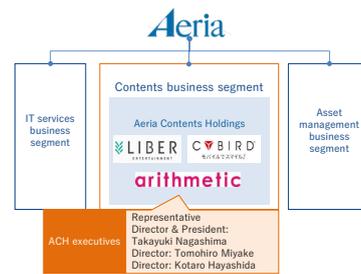
* Vtuber (Virtual YouTuber): IP for a YouTube channel as a YouTuber (virtual character)

Arithmetic's DYNAMIC CHORD (left) and starry☆sky (right)



Source: The Arithmetic website

ACH conceptual image



Source: Prepared by FISCO from the Company's results briefing materials

Generating synergies from strengths of the four companies

4. Asset management business

Asset management business mainly consists of Impression Inc., Total Management Corporation, Twist Inc., and Invest Online, Inc. Impression develops investment-purpose condominiums harnessing its strength in investment property sales, sells residence real estate, and handles renovation business, covering a wide range of areas, including services for other businesses. Total Management, which has connections to wealthy individuals, excels at developing standalone home sites and income-earning properties, renovates used apartments, handles real estate transactions, and provides consulting services. Twist offers minpaku operation agent service to individuals and others. Invest Online, acquired as a subsidiary in November 2019, is the newest addition with IT, online services, and industry information as strengths. It operates information provision sites for property investors, such as Shinchiku Itto Toshiho, Chintai Heiyo Jutaku No Susume, and INVEST ONLINE, and conducts matching of properties and investors and consulting.

Business overview

The addition of Invest Online to the Company's group is a good fit for the asset management business and the Group itself with its foundation in the Internet. While each of the companies in the asset management business already had relatively firm positions in their respective areas and generated profits, this line-up supports more synergies by broadening the scope of properties that can be developed and mutually utilizing property procurement routes and real estate investor networks. Since it also becomes easier to identify properties that can be converted to minpaku specifications, this lowers the hurdle to developing high value-added properties. Furthermore, there are expectations for synergies across the group as well, such as collaboration with contents business IP and real estate tech combined with IT service business. Despite temporary suspension due to the impact of COVID-19, domestic and overseas tourists are still likely to increase over the longer term due to Japan's national strategy of becoming a major tourist nation. We think the Company's asset management business offers robust potential, albeit while recognizing the need to control risk from fluctuation in real estate prices.

■ Management policy for “with COVID-19” conditions

Developing businesses from a longer-term perspective anticipating advances by the network society

1. Management philosophy

The Company advocates a management philosophy of “being an essential presence, similar to air, in the network society with a key word of communication while also creating valuable services enjoyed by all users and building businesses with high profitability that focus on fast-growing markets.” Given this stance, it promotes business, mainly developing smartphone games, from a medium- to long-term perspective that actively adopts new technologies and businesses, such as blockchain, AI, and AR/VR, while closely monitoring advances in the network society. The Company's business cycle hence evolves in a spiral manner with active investment in growth markets, reinforcement of the foundation in growth markets, and establishment of unique positions in new markets and technologies. Due to heavy impact by COVID-19, we believe the Company is currently at the stage of reinforcing its foundation in growth markets.

Rigorously promote selectivity and focus and improvement in profitability as 2H management policy

2. Management policy in 2H FY12/20

In 2H FY12/20, the impact from COVID-19 was stronger than what had been envisioned. As a result, the Company as well as companies throughout the world were heavily affected. Due to this environment, the Company prepared a new management policy premised on “with COVID-19” conditions and decided to rigorously promote selectivity and focus and improve profitability heading into 2H. Increased selectivity and focus, which is likely to mainly address contents business specifically means quick suspension of or exit from titles that lack prospect of cost-effect performance even in the case of well-known existing titles and priority on new title development on contents capable of supporting IP business (particularly in games). In profitability improvement, the Company is shifting away from outsourcing that often is costly and hinders thesis verification and shifting to internal work through collaboration with group companies. It intends to build a system that that will allow it to promptly and flexibly implement measures at low cost.

Intends to actively utilize external management resources over the medium term

3. Future management policy

The Company needs to apply the “with COVID-19” conditions premise to future management policy as well. Specific policies are (1) realization of business portfolio composition that generates stable earnings to boost growth potential even in social conditions with significant change, (2) creation of synergies within businesses and among businesses, (3) subsidiary profitability enhancement and reorganization in light of earnings and group contributions, (4) active pursuit of growth markets that utilize the group’s business assets, and (5) utilization of external business assets through capital participation and establishment of joint ventures.

Nevertheless, items (1) to (4) are essentially extensions of existing policy that add the “with COVID-19” conditions premise. We explained details in the business overview section, including risk distribution among the three business areas in the Company’s portfolio, synergy generation within businesses and among businesses through establishment of ACH and acquisition of Invest Online, and promotion of new businesses in the asset management business, such as the MDM application and other IT business and real estate tech. The clear change, meanwhile, is management’s decision to utilize external management resources, such as IP, contents, and human resources. The Company previously emphasized internalization with M&A deals, reinforcement of internal operations, and other measures and obviously still intends to bring inefficient outsourcing in-house in the near term. Over the medium term, however, it decided to actively utilize other company IP and other external management resources through capital participation, establishment of joint ventures, license rollout, and knowhow contribution. We think utilization of external resources in IP business is an effective way to achieve future growth considering time needed to cultivate proprietary IP and the Company’s knowhow in IP business.

Results trends

Event and other activity suspensions and postponements affected 2Q

1. 1H FY12/20 results trends

The Company reported 1H FY12/20 results with ¥14,077mn in net sales (-2.3% YoY), ¥154mn in operating profit (-91.6%), ¥97mn in recurring profit (-94.4%), and a ¥4,311mn net loss attributable to owners of parent. (vs. a ¥1,044mn profit in the previous fiscal year). The IT market continues to steadily grow with drivers from increase in Internet users accompanying further inroads by smartphones and other mobile devices and expansion of the e-commerce (EC) market. The market for games and other mobile contents, meanwhile, is simultaneously diversifying and expanding in scale. Given the need to develop attractive contents and deliver more complex and sophisticated services, participants face rising development expenses, personnel costs, and other costs and user acquisition competition has been intensifying among companies. The real estate market is confronting a shortage of suitable investment properties as prices climb and yields decline while financial institutions are taking a tough credit stance.

1H FY12/20 results

	1H FY12/19	Ratio to sales	1H FY12/20	Ratio to sales	Change
Net sales	14,404	100.0	14,077	100.0	-2.3
Gross profit	6,769	47.0	5,037	35.8	-25.6
SG&A expenses	4,923	34.2	4,882	34.7	-0.8
Operating profit	1,846	12.8	154	1.1	-91.6
Recurring profit	1,745	12.1	97	0.7	-94.4
Profit attributable to owners of parent	1,044	7.2	-4,311	-30.6	-

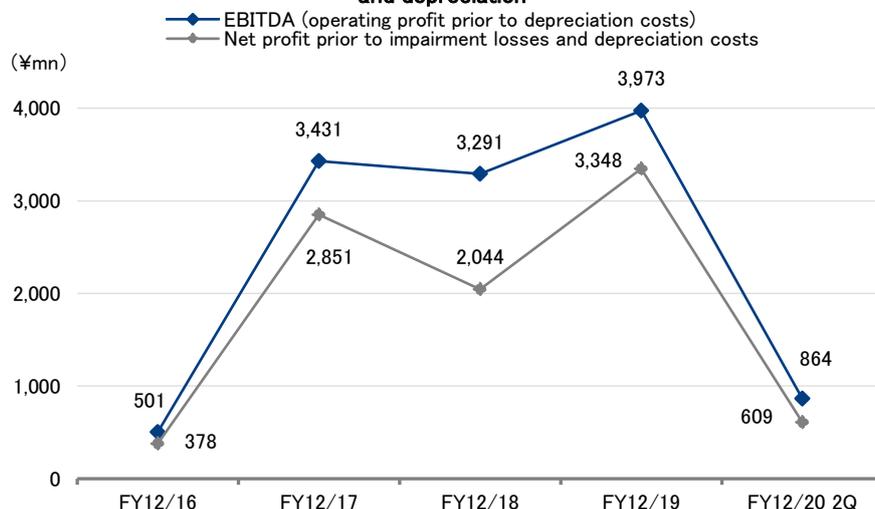
Source: Prepared by FISCO from the Company's financial results

Amid these conditions, the Company is strengthening its stable income foundation in IT services business and bolstering development, distribution, and operation of smartphone contents, building foundations in niche markets with narrowed targets, and deepening peripheral businesses in the contents business. In asset management business, it operates cautiously to control business risk by handling small-scale income-earning real estate with rapid turnover. Since February 2020, however, impact from the global COVID-19 pandemic has affected the Company as well. Consolidated sales and profits declined, despite telework and stay home demand in IT services and contents businesses, because of demand pullback from curtailed activity in contents and asset management businesses. The Company booked ¥4,211mn in extraordinary losses due to impairment losses on subsidiary goodwill and fixed assets with weakened income outlooks and investment recovery prospects accompanying these impacts.

Since the Company aims to strengthen and expand the business foundation by aggressively utilizing M&A, it uses EBITDA (operating profit + depreciation costs + goodwill amortization costs), which demonstrates cash soundness, as a profitability indicator. In 2H FY12/20, while the Company reported a ¥4,063mn net loss prior to goodwill amortization costs (net loss attributable to owners of parent + goodwill amortization costs; vs. a ¥1,401mn profit a year earlier), it retained investment wherewithal, even with COVID-19 impact, by posting ¥864mn in EBITDA (operating profit + depreciation costs + goodwill amortization costs; -63.8% YoY) and ¥148mn in net profit prior to impairment losses and goodwill amortization costs (net loss attributable to owners of parent + goodwill amortization costs + impairment charges).

Results trends

Trends in EBITDA and net profit prior to impairment losses and depreciation



Source: Prepared by FISCO from the Company's financial results and results briefing materials

Segment results in 1H FY12/20 were IT services business at ¥1,978mn in net sales (-26.4% YoY) and ¥220mn in operating profit (-15.2%), contents business at ¥7,532mn in net sales (-12.8%) and a ¥113mn operating loss (-¥1,603mn), and asset management business at ¥4,619mn in net sales (+46.4%) and ¥44mn in operating profit (-56.8%).

1H FY12/20 results by segment

(¥mn, %)

	1Q FY12/20			2Q FY12/20			1H FY12/20		
	Net sales	Ratio to sales	Change	Net sales	Ratio to sales	Change	Net sales	Ratio to sales	Change
IT services business	1,075	16.3	-25.6	907	12.0	-27.2	1,978	14.0	-26.4
Contents business	3,485	52.7	-20.9	4,047	53.8	-4.3	7,532	53.2	-12.8
Asset management business	2,047	31.0	50.3	2,572	34.2	43.4	4,619	32.7	46.4

	1Q FY12/20			2Q FY12/20			1H FY12/20		
	Operating profit	Margin	Change	Operating profit	Margin	Change	Operating profit	Margin	Change
IT services business	123	11.4	-8.0	97	10.7	-23.6	220	11.1	-15.2
Contents business	-442	-12.7	-	329	8.1	-61.1	-113	-1.5	-
Asset management business	37	1.8	12.7	7	0.3	-89.9	44	1.0	-56.8

Source: Prepared by FISCO from the Company's financial results

IT services business reported lower sales and profits, albeit within the anticipated range to some extent, even with stable income at AIR Internet Service that handles the data services business, because of decline in affiliate advertising income at First Penguin. Contents business posted weaker sales and a segment loss due to event and promotion suspensions and postponements and some pullback of user interest in games as impacts of the COVID-19 outbreak as well as increases in development costs and depreciation costs for new contents and the inability to reduce initial promotion costs for a new title release that are fixed costs. Asset management business recorded higher sales because of the property transfer period but had a profit setback from upfront costs amid lack of progress in acquiring new properties and a shortage of attractive properties as financial institutions adopted stricter financing policies.

Aims to secure operating profit in FY12/20 just as in 1H

2. FY12/20 outlook

For FY12/20, the Company forecasts ¥26,000mn in net sales (-8.3% YoY), ¥500mn in operating profit (-77.9%), ¥300mn in recurring profit (-86.4%), and a ¥4,200mn in net loss attributable to owners of parent (-¥5,714mn YoY). The Company's 2H management policy, as explained above, seeks early suspensions of and exits from low-margin titles and priority development of contents with IP business potential in "selectivity and focus" and reduction of outsourcing costs through utilization internal personnel and promotion of enhanced theory verification by subdividing investment units in "improving profitability." Management aims to secure operating profit in FY12/20 with these measures.

FY12/20 outlook

	(¥mn, %)				
	FY12/19	Ratio to sales	FY12/20 E	Ratio to sales	Change
Net sales	28,347	100.0	26,000	100.0	-8.3
Operating profit	2,265	8.0	500	1.9	-77.9
Recurring profit	2,209	7.8	300	1.2	-86.4
Net profit (loss) attributable to owners of parent	1,514	5.3	-4,200	-16.2	-

Source: Prepared by FISCO from the Company's financial results

Next, we review detailed measures for 2H in each of the businesses. In IT services business, the Company plans to bolster promotions for affiliate earners, such as holding strategy seminars online, to address decline in affiliate advertising income. It hopes that this effort will encourage rollout of videos that appeal to users and expand sales of low-priced products currently in a transition phase to some extent.

In contents business, while stay-home demand related to COVID-19 should work positively for games, event suspensions and postponements are preventing the Company from fully utilizing its robust IP business, including 2.5D stage events, and cancellations of big events, such as Comic Market, have undercut promotions for 2H. The latter situation is likely to modestly disrupt acquisition of new users. Since holding fall events is a key point for the following season, however, the Company seems likely to gradually resume and expand events while avoiding infection risk through guideline formulation and capacity control. Additionally, we expect ramp-up of promotions that incorporate online components that fit well with the contents. The start of similar activities for some events, such as the Game Show and Animate Girls' Festival (AGF, *), and anticipated lifting of restrictions on events, albeit gradually, are likely to provide tailwinds. These developments suggest that the Company's IP business and promotions should move toward full deployment amid the "new normal" in 2H.

* Animate Girls' Festival (AGF): Sales event for animation, games, and other goods targeting women in Ikebukuro. It is scheduled for November 2020.

In asset management business, while the Company was unable to acquire new properties, mainly in 2Q, because of the impact of COVID-19, conditions appear to be gradually recovering recently, including the credit situation. It intends to generate profits via cost controls and optimal assignment of human resources and also aims to improve user convenience through provision of services using real estate tech, such as visualization of property operation conditions.

Bottom in FY12/20, profitability and growth potential likely to recover from FY12/21

3. Medium-term growth scenario

The Company's management policy should pay off in profit acquisition over the medium term. Since the Company is sustaining positive values in EBITDA and net profit prior to impairment losses and goodwill amortization costs even with the COVID-19 outbreak, it should sustain a certain level of growth investments, despite highly volatile social conditions, and thereby continue business portfolio composition that generates stable earnings. Synergies within businesses and among businesses are showing up already, mainly at ACH, in IP business knowhow, suitable assignment of human resources, and business management. Procurement and sales route sharing has started moving forward, a positive trend in asset management business too. Furthermore, Aeria One, Inc., which was established at the same time as ACH, has improved progress in technology synergies for the entire group, such as IP, IT technology, and real estate tech. If the Company makes active use of external business resources through capital participation, formation of joint ventures, and other methods, it should significantly broaden the applicable scope and raise the growth speed of IP business. We also expect the Company to adeptly acquire growth areas in addressing telework, stay home, and other new environments, leveraging its DNA, while continuing to reorganize businesses that lack synergy prospects and low-margin businesses.

Steady implementation of management policy hence is important from the standpoint of restoring medium-term profitability and growth potential. More importantly, if "with COVID-19" conditions take hold, it is expected that the environment of the contents business—an income driver—will improve greatly based on those conditions. In FY12/21, when knowledge related to COVID-19 has accumulated and "with COVID-19" conditions remain, we therefore expect strong profit additions to stable IT services business from asset management business and especially contents business that held back recent earnings. After this "recovery from the impact of COVID-19," the Company should enter a new phase of benefiting from IP business growth over the medium term with a portfolio that consists of three core businesses.

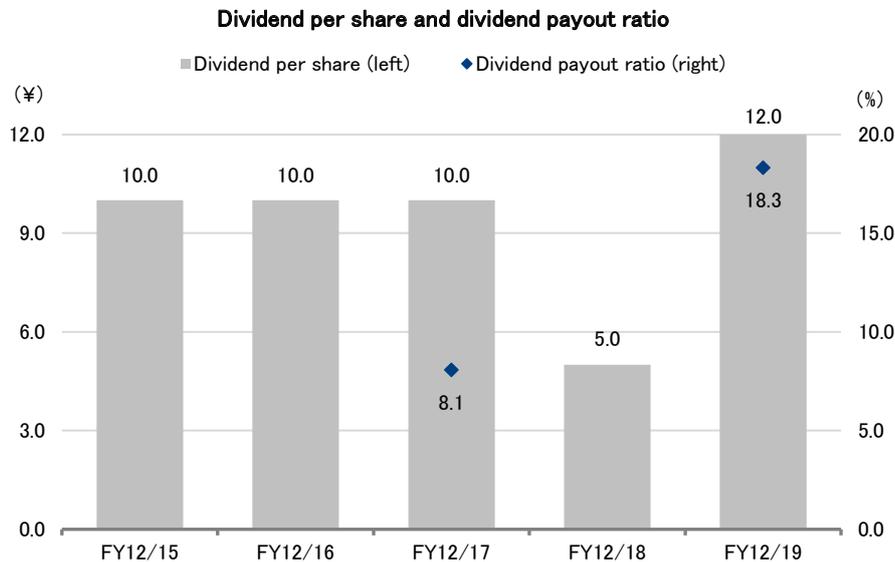
Shareholder return policy

Undecided FY12/20 dividend

1. Dividend

The Company acknowledges that returning profits to shareholders is an important management issue, but wants to expand profit retention in light of efforts to improve and strengthen operations and future business initiatives. It intends to use retained profit funds mainly for M&A and other capital alliances, R&D activities, and new business plans. For the surplus-fund dividend in FY12/19, the Company ended up raising the annual dividend outlay by ¥7 YoY to ¥12 (no interim dividend), in light of its basic policy of paying continuous stable dividend and healthy earnings. The Company has not decided the FY12/20 dividend as of end-1H, mainly because of COVID-19 impact.

Shareholder return policy



Note: The Company made a 2-for-1 share split on July 1, 2017.
 Source: Prepared by FISCO from the Company's financial results

Provided QUO cards for the popular title “Ikemen Sengoku – Romances Across Time” as a shareholder benefit FY12/19

2. Shareholder benefit program

The Company provides a shareholder benefit each year with the aim of deepening shareholder understanding of its businesses and encouraging share ownership over the longer term (it normally decides specific benefit content in December). It sends the benefit with a notification of resolutions for the general shareholder meeting which is typically mailed in late March to shareholders on the ledger as of the shareholder benefit standard date (at the end of December). The shareholder benefit in FY12/19 was QUO cards for the popular title “Ikemen Sengoku –Romances Across Time”, with expected distribution of ¥300 for 100 shares up to less than 1,000 shares, ¥500 for 1,000 shares up to less than 5,000 shares, ¥700 for 5,000 shares up to less than 10,000 shares, and ¥1,000 for 10,000 shares or more. Shareholder benefits for FY12/20 have not yet been decided.

■ Information security

Strict compliance with confidentiality in regards to personal information

In the course of business, some Aeria Group companies require that individual users registering for online services provide their personal information, including name, address, telephone number, and email address. Personal information may also be collected and held temporarily by client companies with the consent of the provider of that personnel information. Such personal data is treated as confidential by the Group, with internal access subject to restrictions and additional measures in place to prevent unauthorized external access. Aeria does not obtain any personal information through sales made at the App Store or Google Play.



Disclaimer

FISCO Ltd. ("FISCO") offer stock price and index information for use under the approval of the Tokyo Stock Exchange, the Osaka Stock Exchange and Nikkei Inc.

This report is provided solely for the purpose of offering information, and is not a solicitation of investment nor any other act or action.

FISCO prepared and published this report based on information which it considered reliable; however, FISCO does not warrant the accuracy, completeness, fitness nor reliability of the contents of this report or the said information.

The issuers' securities, currencies, commodities, securities and other financial instruments mentioned in this report may increase or decrease in value or lose their value due to influence from corporate activities, economic policies, world affairs and other factors. This report does not make any promises regarding any future outcomes. If you use this report or any information mentioned herein, regardless of the purpose therefor, such use shall be made based on your judgment and responsibility, and FISCO shall not be liable for any damage incurred by you as a result of such use, irrespective of the reason.

This report has been prepared at the request of the company subject hereto based on the provision of information by such company through telephone interviews and the like. However, the hypotheses, conclusions and all other contents contained herein are based on analysis by FISCO. The contents of this report are as of the time of the preparation hereof, and are subject to change without notice. FISCO is not obligated to update this report.

The intellectual property rights, including the copyrights to the main text hereof, the data and the like, belong to FISCO, and any revision, reprocessing, reproduction, transmission, distribution or the like of this report and any duplicate hereof without the permission of FISCO is strictly prohibited.

FISCO and its affiliated companies, as well as the directors, officers and employees thereof, may currently or in the future trade or hold the financial instruments or the securities of issuers that are mentioned in this report.

Please use the information in this report upon accepting the above points.

■ For inquiry, please contact: ■

FISCO Ltd.

5-11-9 Minami Aoyama, Minato-ku, Tokyo, Japan 107-0062

Phone: 03-5774-2443 (Financial information Dept.)

Email: support@fisco.co.jp