

**Daikoku Denki Co.**  
 6430 Tokyo Stock Exchange First  
 Section

3-Aug.-15

Important disclosures  
 and disclaimers appear  
 at the end of this document.

FISCO Ltd. Analyst  
 Ikuo Shibata

\* Industry self regulation to limit machines highly conducive to gambling is going to be applied to pachinko machines from November 2015 and to pachinko slot machines from December 2015.

## ■ Establishing overwhelming superiority that its competitors cannot match

Daikoku Denki <6430> (hereafter, “the Company”) has two main segments, the Information System Segment, which develops, manufactures, and sells computer systems for pachinko (Japanese pinball) parlors or halls, and the Control System Segment, which develops, manufactures, and sells display and control units and pachinko slot machines. The Company holds the top share, or approximately 35%, of the Japanese market for hall computers, reflecting an information management method that is the de facto standard for the industry. Meanwhile, the Company’s membership information service called the Daikoku Denki Strategic Information System (DK-SIS) gathers, processes and analyzes the daily operational information of pachinko halls with customer associations and gives feed-back to the managers of these halls to improve their operations. It is the only such system in Japan and the customer network built up upon this service supports the Company’s business base. The system was used by 3,719 pachinko and pachinko slot halls at FYE3/15. It has also made a fully fledged entry into the manufacture and sale of in-house developed pachinko slot machines.

As Japan’s pachinko market has been shrinking for several years, the Company is pursuing three main reforms to achieve growth over the medium to long term: 1) development of a next-generation hall computer, 2) shifting to a stock-type revenue model, and 3) expansion of in-house developed pachinko slot machines. Over the next few years, the Company will continue to advance its plan to invest about ¥10bn to develop a hall computer (including peripheral equipment) that will operate on a cloud server and be capable of advanced analysis of Big Data. It will be far superior to any competing computer and should allow the Company to increase its share of the Japanese market for these machines.

In FY3/15, both sales and profits declined; sales were down 5.1% y-o-y to ¥54,043mn, and operating profit declined 73.3% to ¥1,425mn. Sales were largely in-line with the forecast, but while it had been anticipated that profits would be kept down by R&D expenses and other factors, temporary cost factors, such as the loss following the bankruptcy of a pachinko machine manufacturer client, put further downward pressure on profits. So if we put to one side these temporary factors and look at the growth of peripheral equipment, which the Company is focusing on, and on the steady launch of its in-house developed pachinko slot machines, its results seem to be basically progressing in-line with targets.

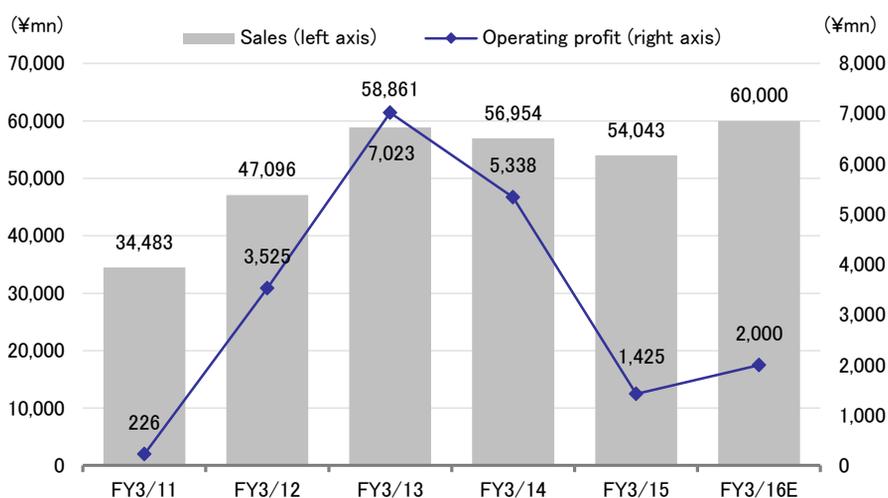
For FY3/16, the Company is forecasting an 11.0% y-o-y rise in sales to ¥60,000mn and a 40.3% increase in operating profit to ¥2,000mn. Although there are concerns about the effects of self regulation in the industry,\* which is forecast for the H2 of the fiscal year, the Company intends for the fully fledged deployment of its own brand of pachinko slot machines to be the driving force behind its results.

At FISCO, we consider that the Company’s results will be dictated by the effects of industry self regulation and trends in the sales of pachinko slot units. But taking into consideration its results up to the present time and the assumptions for its targets, we judge that it will be possible for it to achieve its results forecasts.

## ■ Check Point

- No.1 market share in pachinko hall computers
- The Information System Segment achieved record high sales for the third consecutive fiscal year
- The Company expects contribution from the fully fledged deployment of its own brand pachinko slot machines

Trends in Full-year Results



## ■ Business Description

### No.1 market share for Pachinko hall computers

Daikoku Denki develops, manufactures, and sells computer systems for pachinko halls as its core business. It also manufactures and sells display and control units for pachinko machines and pachinko slot machines, and pachinko slot machines developed in-house.

As the pioneer in the development of hall computers, which assist the management of pachinko halls, the Company won hall's trust and pachinko fan's satisfactions by providing the management system which put emphasis on data management, introduction of innovative peripheral equipment for its hall computers, and utilization of the only membership information service in the pachinko industry; and it holds the top share of the Japanese market for hall computers.

Its hall computers are installed in about 4,100 pachinko halls in Japan, primarily high-end halls, giving it an approximately 35% share of the market.

The Company's two main businesses are the Information System Segment and the Control System Segment, but the Information System Segment provided 68.6% of its total sales in FY3/15 and is the main source of stable profit.

#### (1) Information System Segment

The Information System Segment offers a complete line of information equipment and services to support sales and operational management at pachinko halls. Hall computers are the core of the system used within halls, and these are supported by peripheral equipment, such as prize customer management systems and information display systems. For consolidating and analyzing the data recorded by this equipment, the Segment offers services such as a hall operational support service and a membership information service unique in the industry and serves as a strategic tool.

Hall computers display the operating condition of each machine and sales data, and are the core systems for supporting pachinko hall operations. As mentioned above, these computers are supported by peripheral equipment, such as prize customer management systems and information display systems; and also serve as the foundation of the DK-SIS system, the membership information service. The major strengths of this business are that peripheral equipment and support services are often sold with hall computers as a package deal. Other than the sales of its information system equipment, the Company is shifting to a stock-type revenue model by reinforcing regular fee income business from after-sales management support service and information supply service.



Daikoku Denki Co.  
6430 Tokyo Stock Exchange First Section

3-Aug.-15

Hall computers and the main peripheral equipment



= Top market share of around 35%



(2) Control System Segment

The Control System Segment produces LCD display units, control units, switches and motors to makers of pachinko and pachinko slot machines. Applying the expertise obtained in hall computers during many years of analyzing data from pachinko machines through its DK-SIS, the Segment is serving as a developing partner to machine manufacturers by proposing specifications based on trend analysis of popular machines, and involved in contents business by obtaining the rights to use popular characters, beyond the Segment's position as a unit manufacturer.

Daikoku Denki began manufacturing and selling in-house developed machines on a full scale from FY3/14 through the brand of DAXEL Inc., its consolidated subsidiary (subsequently, "own brand"). The Company has had a series of hit products with original value creation that has more emphasis on entertainment, like the pachinko slot game machines Magical Suite Prism Nana and Sasami-san@ Ganbaranai Slot, and has established a high quality brand image specialized in anime.

Results of in-house developed pachinko slot machines



まじかるすいーと  
**マジカルスイート**  
MAGICAL SUITE PRISM NANA™  
Magical Suite Prism Nana  
Launched January 2013  
4,000 units sold

©2012 prismnana  
©DAXEL



ササミさん@  
かみは@ないすって  
Sasami-san@ Ganbaranai Slot  
Launched September 2014  
6,000 units sold

©Akira, Shogakukan / Production Committee@Ganbaranai

## ■ Company Strengths

### **Introduce information equipment that is the first of its kind in the industry and open up new markets through original characters**

#### **(1) By offering valuable innovations, the Company established market development type growth model**

Since its establishment, Daikoku Denki has consistently planned and developed new categories of goods and services, thereby developed the pachinko market and achieved growth. It has not just developed machines with superior functions but emphasized the importance of data management and the need for information disclosure. Thus, it has been able to present ideas with added value to the various aspects of management of pachinko halls.

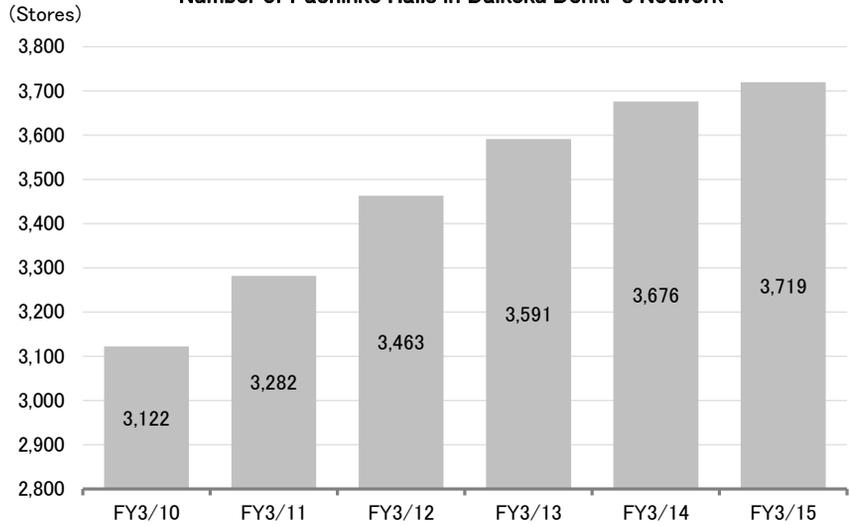
Launched in 1974, the Company's first hall computer enabled the managers of pachinko halls to introduce a hall management method based on data management. Previously, pachinko halls accumulated only basic information, but with the introduction of hall computers, data-based hall management became the de facto standard. In subsequent years, the Company introduced other kinds of information equipment with revolutionary functions. One such piece of equipment was the Data Robo terminal, which provides information about different models of pachinko machine to the pachinko hall visitors. This equipment has enhanced the profitability of pachinko halls by increasing the efficiency of pachinko hall management and the satisfaction of pachinko machine fans.

One new business being pursued by Daikoku Denki is the in-house developed pachinko slot machines that differ from previous pachinko slot machines and pachinko machines, which tend to be chosen based on the appealing of gambling. As mentioned above, the Company commercialized a pachinko slot game machine that displays original animation characters created by popular illustrators, and it pursued the commitment to quality in animations and voice actors. This high-quality machine has won accolades from pachinko slot machine fans who also love animation videos, and the Company has again established a new market for amusement equipment.

#### **(2) The Company has established a strong network of pachinko halls**

Another advantage Daikoku Denki has is the DK-SIS, hall computer based membership information service. This service connects the Company and member pachinko halls through networks, and gathers, processes and analyzes the daily operational information of pachinko halls recorded by hall computers, and feed-back useful information to the managers of these halls to improve their operations. The managers of halls in which Daikoku Denki's hall computers are installed can make proper store management by using useful information such as operational data on nationwide pachinko machines and sales data broken down by the model of pachinko machine. As for Daikoku Denki, this firm network with member halls is supporting its operating base. The Company also serves as a think tank on the pachinko industry and, as a leading company of the industry, this elevates the Company's brand name. The service is currently used by 3,719 pachinko and pachinko slot halls that operate approximately 1.37mn machines, or 30.0% of all the machines installed in Japan, and gathers the data of ¥10.2 trillion annual sales.

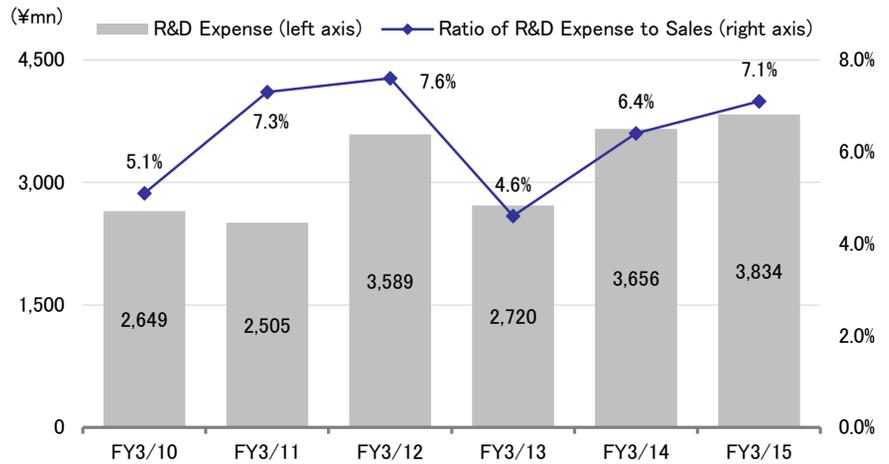
Number of Pachinko Halls in Daikoku Denki's Network



**(3) Stable revenue base supports the Company's investment in the future growth**

Daikoku Denki's main source of competitiveness is its investment in future growth, including its R&D expense. Over the past few years, the Company has maintained aggressive investment in future growth driver fields such as pachinko slot machines and a next-generation hall computer, and other products. The stable revenue stream or Cash Cow provided by the high-margin Information System Segment make this investment possible. The Company's ability to balance large profits from its existing businesses with heavy investment in businesses of the future allows it to maintain sustainable value creation.

Research and Development Expense and Ratio of Expense to Sales



## ■ Industry Environment

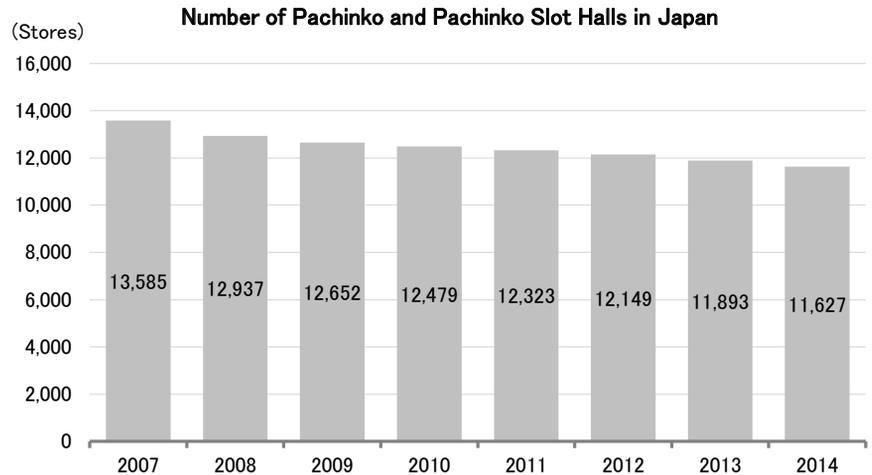
### The increase in the size of halls is proving a tailwind and the market scale is recovering to ¥4 trillion

Japan's pachinko industry has been shrinking for years, reflecting a decline in the pachinko fan's population, a trend toward playing games with low rental costs for balls, increases in Japan's consumption tax, and other factors. According to surveys by the National Police Agency, the number of pachinko and pachinko slot halls in Japan declined at an average annual rate of 1.7% for five years from 2010. In 2014, the number of halls was 11,627 (down 266 halls y-o-y) and Daikoku Denki served about 4,100 of these halls, or about 35%. Most of Daikoku Denki's customers are high-end pachinko halls, so those halls are relatively insensitive to economic cycles and have money enough to invest in new businesses.

Daikoku Denki Co.

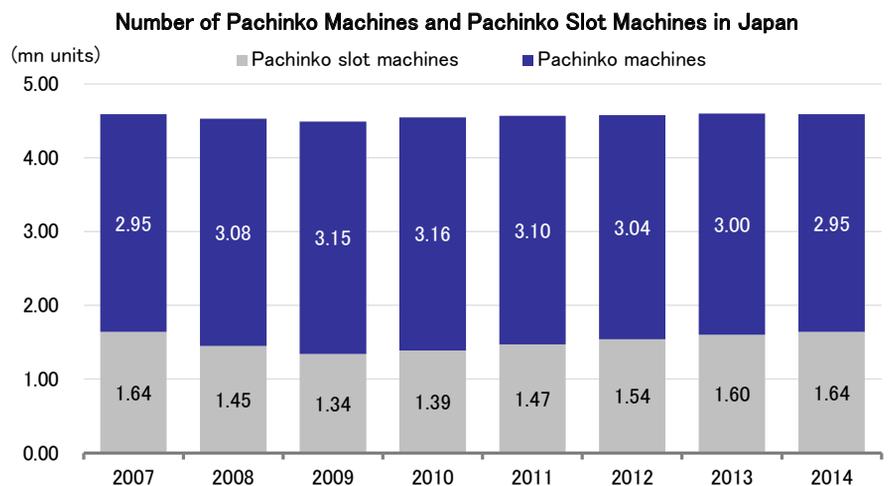
6430 Tokyo Stock Exchange First Section

3-Aug.-15



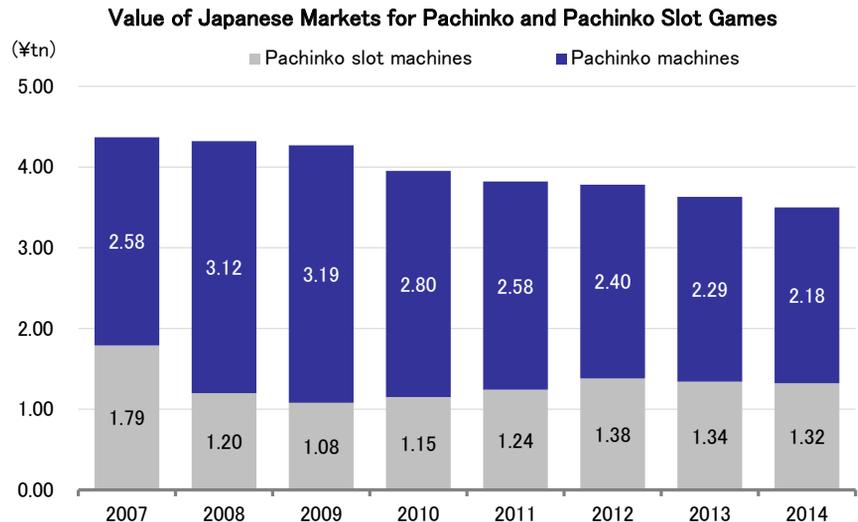
Source: The Present State of Businesses Affecting Public Morals in 2014, Consumer and Environmental Protection Division, Community Safety Bureau, National Police Agency

However, according to Company estimates, while the number of pachinko machines in Japan has declined, the number of pachinko slot machines has increased, meaning the combined number of pachinko and pachinko slot machines has trended practically unchanged. Since the number of pachinko and pachinko slot halls decreased over the same period, this indicates the trend for large scale hall operations. Upsizing of pachinko and pachinko slot halls with advantage of scale, benefits Daikoku Denki, as the Company can seek high investment effect from advanced functionality and added values.



Source: The Present State of Businesses Affecting Public Morals in 2014, Consumer and Environmental Protection Division, Community Safety Bureau, National Police Agency

According to Daikoku Denki's estimate, the value of Japan's combined market for pachinko and pachinko slot games, as measured by the gross profit earned by all halls nationwide, has fallen each year, and this value has also declined on a per-machine basis. Thus, even though pachinko halls and pachinko slot halls are increasing in average size, they continue to operate in a challenging business. Daikoku Denki believes that the combined market for pachinko and pachinko slot games could recover to about ¥4trn per year in mid-term once the pachinko industry has recovered from a temporary downturn in business following the latest consumption tax hike, and if Japan's economy is able to overcome deflation as the country prepares to host the Olympic Games in Tokyo.



In FY3/16, industry self regulation to limit machines that are highly conducive to gambling are expected to be applied (to pachinko machines from November 2015 and to pachinko slot machines from December 2015). In the past also, the Company has experienced a slump in results in hall computers due to limits placed on models considered too conducive to gambling and there are concerns of a similar slump this time. But if viewed from a difference perspective, this development can be considered as promoting the conversion to the management of hall computers that are not dependent upon gambling.

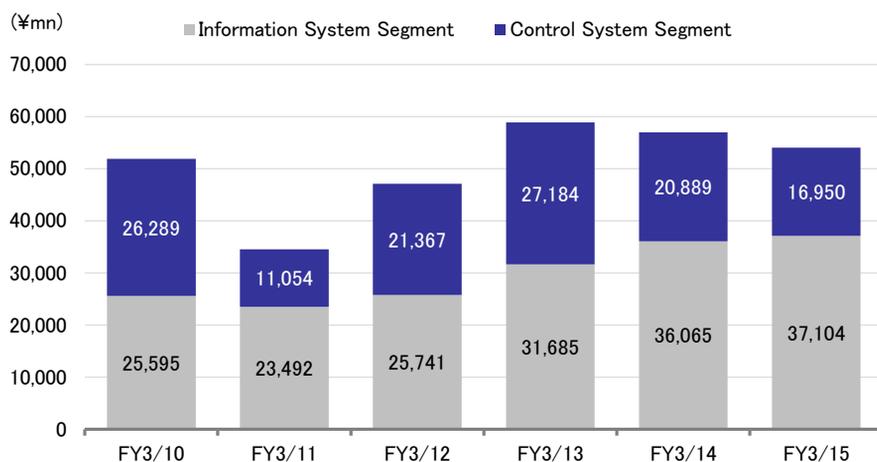
## ■ Financial results trends

### The Information System Segment achieved record high sales for the third consecutive fiscal year

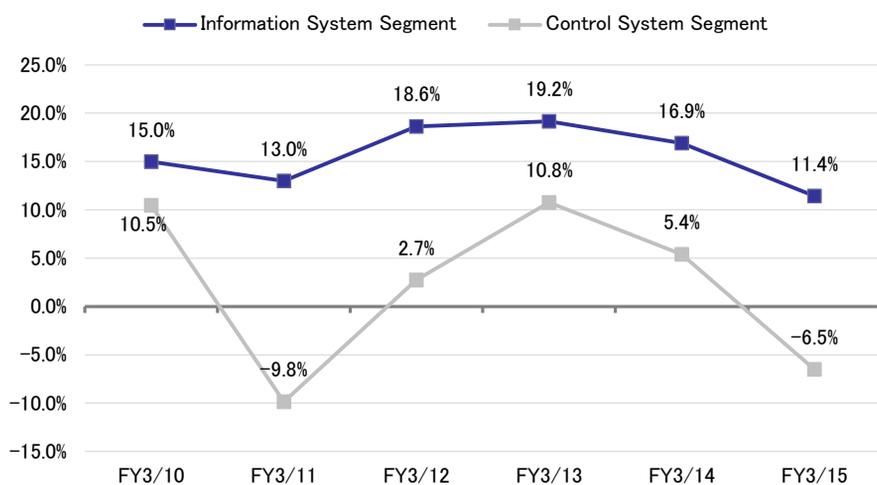
#### (1) Performance over the past six fiscal years

Looking back at the results over the past 6 fiscal years, in FY3/11, the Company's sales shrank y-o-y because of restrained consumer spending and the impact of the Great East Japan Earthquake. But since then, the Company's sales have rebounded even though the pachinko industry has continued to consolidate. This recovery was led by the Information System Segment, which holds high market shares for its products and achieved record high sales for three consecutive fiscal years up to FY3/15.

### Breakdown of Sales by Segment



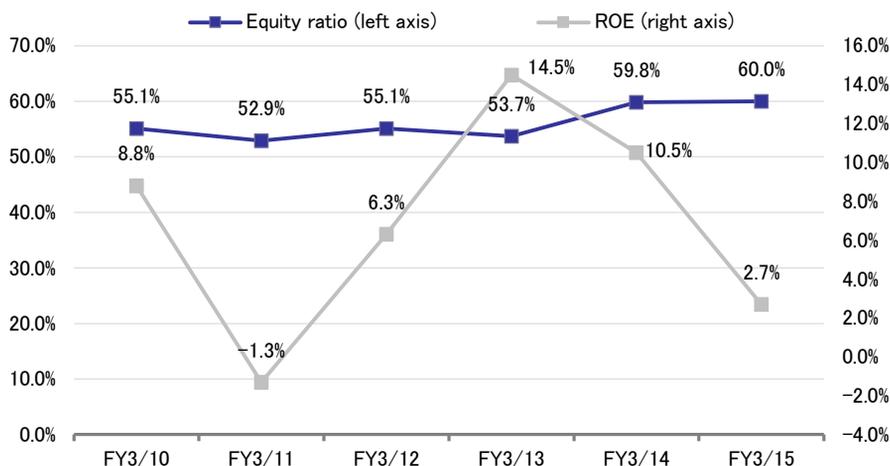
### Operating Profit Margins by Segment



Supported by the high profitability of the Information System Segment, the Company has maintained a high profit margin since its recovery from 2011 disasters. The profit margin has declined since FY3/14 due to factors including the increase in development expenses for next-generation hall computers. But when taking into account this expense, it can be said that it is still being maintained at a high level.

The Company's equity ratio, a measure of financial stability, has remained high, reflecting large retained earnings, and rose to 60.0% in FY3/15. The current ratio, which indicates the ability to make payments in the short term, was 175.5% in FY3/15, mainly due to large holdings of cash and deposits. ROE, which is a measure of capital efficiency, fell to a level of 2.7% in FY3/15 (from 10.5% in FY3/14), so the temporary cost factors had a major impact.

Equity Ratio and ROE



**(2) FY3/15 Results**

In Daikoku Denki's FY3/15 consolidated results, both sales and profits fell. Sales declined 5.1% y-o-y to ¥54,043mn, operating profit fell by 73.3% to ¥1,425mn, recurring profit dropped by 71.4% to ¥1,566mn, and net profit weakened by 73.3% to ¥874mn. Sales were 98.3% of the Company's initial forecasts, so were basically as expected. But operating profit was greatly below the target, at 47.5%. However, the majority of the shortfall in operating profit compared to the target (approximately ¥1,575mn) were temporary cost factors; specifically, a loss following the bankruptcy of a pachinko machine manufacturer customer (around ¥950mn) and a loss associated with changes to estimated costs in outsourced software development (approximately ¥350mn).

Looking at sales by segment, in the Information System Segment, sales of peripheral equipment for hall computers, such as information disclosure systems and card reader (CR) units, grew considerably, more than the Company had forecast, which supported the growth of the Segment's sales. But in the Control System Segment, sales were much lower than planned due to the declines in the number of sales models and the increase in the rate of reused parts among customers. Consequentially, the total sales result for both segments was roughly in-line with expectations.

While it was anticipated that the profit level would be kept down due to the change to the profit model and the increase in R&D expenses (up 4.9%), the temporary cost factors, including the loss following the bankruptcy of a pachinko machine manufacturer customer, put further downward pressure on profits. As a result, the operating profit margin fell greatly to 2.6% (from 9.4% in the previous fiscal year).

On the one hand the equity ratio, which is an indicator of the Company's financial strength, was 60.0% and maintained its high level (up from 59.8% at FYE3/14). But on the other hand ROE, which is an indicator of capital efficiency, fell to 2.7% (down from 10.5%) because of the temporary cost factors.



Daikoku Denki Co.

6430 Tokyo Stock Exchange First Section

3-Aug.-15

Results by Segment

(¥mn)

	FY3/14 Result		FY3/15 Result		% of sales		FY3/15 Initial Company forecast		vs. Plan	
		Change		Change		%		Change		%
Sales	56,954	-	54,043	-	-2,911	-5.1%	55,000	-	-957	98.3%
Information Systems	36,065	63.3%	37,104	68.7%	1,039	2.9%	33,000	60.0%	4,104	112.4%
Control Systems	20,889	36.7%	16,950	31.4%	-3,939	-18.9%	22,000	40.0%	-5,050	77.0%
Adjustment	0	0.0	-11	-0.0	-11	-	0	-	-11	-
Cost of goods and services sold	38,288	67.2%	38,407	71.1%	119	0.3%	37,000	67.3%	1,407	103.8%
SG&A expenses	13,353	23.4%	14,233	26.3%	880	6.6%	15,000	27.3%	-767	94.9%
Operating profit	5,338	9.4%	1,425	2.6%	-3,913	-73.3%	3,000	5.5%	-1,575	47.5%
Information Systems	6,093	10.7%	4,244	7.9%	-1,849	-30.3%	4,300	7.8%	-56	98.7%
Control Systems	1,127	2.0%	-1,105	-	-2,232	-	500	0.9%	-1,605	-
Adjustment	-1,883	-	-1,713	-	-	-	-1,800	-	-	-
Recurring profit	5,474	9.6%	1,566	2.9%	-3,908	-71.4%	3,000	5.5%	-1,434	52.2%
Net profit	3,278	5.8%	874	1.6%	-2,404	-73.3%	2,000	3.6%	-1,126	43.7%

R&D expense	3,656		3,834		178	4.9%
Information Systems	1,628		2,710		1,082	66.5%
Control Systems	2,028		1,124		-904	-44.6%

Sales of leading products by segment					
Information Systems					
Information disclosure systems	9,562		8,971		-591
Prize mgt. systems	3,838		2,968		-870
MG service	2,862		3,380		518
Control Systems					
Display units	10,083		7,775		-2,308
Component sales	7,243		5,518		-1,725

Results by segment are as follows.

In FY3/15, the Information System Segment increased its sales by 2.9% y-o-y to ¥37,104mn, but segmental operating profit dropped 30.3% to ¥4,244mn, meaning sales rose but profits fell. The Segment sold 131 hall computers in FY3/15, which was down from 203 in FY3/14. But it sold more peripheral equipment for hall computers, such as VEGASIA (CR units) and BiGMO PREMIUM (data display terminal), than it had forecast, leading to overall sales growth. Sales of the Management Support Service or MG service, which was promoted by the Segment, grew 18.0% y-o-y to ¥3,380mn in FY3/15, due in part to an increase in the number of halls that use the DK-SIS.

Operating profit in the Information System Segment decreased y-o-y in FY3/15 for two main reasons: 1) R&D expenses increased 33.6% y-o-y as the Segment continued to develop a next-generation hall computer, and 2) the Company changed its profit model for CR units, which has achieved significant growth, by lowering the profit margin on sales of the units in exchange for the increase of monthly management fee of information collected by these units. This change of profit model reduces the profitability of the products sold, but instead the Company can earn continuous after-sales fee income, so this change does not reduce the Company's overall profitability.

In the Control System Segment, sales declined by 18.9% y-o-y to ¥16,950mn in FY3/15, and the Segment recorded an operating loss of ¥1,105mn (compared to an operating profit of ¥1,127mn in FY3/14). The number of display units sold declined 17.7%, due mainly to the decrease in the number of models. In addition, makers of pachinko and pachinko slot machines increased their rates of reused parts to lower costs, from 24.4% in FY3/14 to 66.8% in FY3/15. Thus, overall sales and profits fell below the targets.

In addition to the impact of the decline in sales, the temporary cost factors of a loss following the bankruptcy of a pachinko machine manufacturer customer and a loss associated with changes to estimated costs in outsourced software development resulted in the Segment slumping to an operating loss.

The Company sold approximately 7,000 units of 2 models for its in-house developed pachinko slot machines, which it is currently focusing on. In addition to selling around 6,000 units of Sasami-san@ Ganbaranai Slot, which became a particularly big hit, the performance of hall computers as highly operational models greatly contributed to the Segment's results. It is estimated that the profit-and-loss breakeven point is sales of around 7,000 to 8,000 units, so as yet it has not become profitable. But it can at least be said to have made solid progress toward the fully fledged deployment from the current fiscal year (FY3/16).



Daikoku Denki Co.

6430 Tokyo Stock Exchange First Section

3-Aug.-15

### Sales Volumes of Information Systems and Control Systems

	Sales Volumes (Information Systems)		
	FY3/14	FY3/15	Y-o-Y
Hall computers	203 Units	131 Units	-72 Units
Call lamps			
BiGMO series	45,924 Units	17,125 Units	-28,799 Units
BiGMO PREMIUM	48,046 Units	58,587 Units	10,541 Units
IL-X	104,873 Units	82,747 Units	-22,126 Units
VEGASIA CR units	77,223 Units	109,561 Units	32,338 Units
Face recognition systems	23 Stores	11 Stores	-12 Stores

	Sales Volumes (Control Systems)		
	FY3/14	FY3/15	Y-o-Y
Display unit models	18 Products	14 Products	-4 Products
Units sold	300,807 Units	247,649 Units	-53,158 Units

\*Does not include the Pachinko slot machines of consolidated subsidiary DAXEL

## The Company expects contribution from the fully fledged deployment of pachinko slot machines

### (3) Company Forecasts for FY3/16

For its FY3/16 consolidated results, Daikoku Denki is forecasting an 11.0% y-o-y increase in sales to ¥60,000mn, a 40.4% rise in operating profit to ¥2,000mn, a 27.7% increase in recurring profit to ¥2,000mn, and a 60.2% growth in net profit to ¥1,400mn.

As an assumption at the time of the initial forecasts, there were concerns about the impact of industry self regulation, but on the whole it seems like the pachinko and pachinko slot industry will be basically unaffected.

In sales by segment, sales in the Information System Segment are forecast to decline as the new product effects that acted up to the previous fiscal year have run their course. But in the Control System Segment, the fully fledged deployment of in-house developed pachinko slot machines is expected to contribute greatly to an increase in sales.

Profits will be affected by increases in investment expenses for next generation hall computers, in outsourcing expenses from the rise in the number of pachinko slot machine units sold, and in SG&A expenses because of higher sales promotion expenses and sales commissions (¥18,000mn, up 26.5% y-o-y). However, the operating profit margin is forecast to improve to 3.3% (from 2.6% in the previous fiscal year) following the elimination of the temporary cost factors in the previous fiscal year.

### Company Forecasts for FY3/16 versus FY3/15 Results

	FY3/15 Results		FY3/16 Forecasts		% of sales	
		Changes		Changes		%
Sales	54,043		60,000		5,957	11.0%
Information Systems	37,104	68.6%	35,000	58.3%	-2,104	-5.7%
Control Systems	16,950	31.4%	25,000	41.7%	8,050	47.5%
Adjustment	-11	-	0	-	-	-
Cost of goods and services sold	38,407	71.1%	-	-	-	-
SG&A expenses	14,233	26.3%	18,000	30.0%	3,767	26.5%
Operating profit	1,425	2.6%	2,000	3.3%	575	40.4%
Information Systems	4,244	11.4%	2,900	8.3%	-1,344	-31.7%
Control Systems	-1,105	-	1,000	4%	2,105	-
Adjustment	-1,713	-	-1,900	-	-	-
Recurring profit	1,566	2.9%	2,000	3.3%	434	27.7%
Net profit	874	1.6%	1,400	2.3%	526	60.2%
R&D expense	3,834		5,600		1,766	46.1%
Information Systems	2,710		3,700		990	36.5%
Control Systems	1,124		1,900		776	69.0%
Sales of leading products by segment						
Information Systems						
Information disclosure systems	8,971		8,900		-71	-0.8%
Prize mgt. systems	2,968		2,800		-168	-5.7%
MG service	3,380		3,700		320	9.5%
Control Systems						
Display units	7,775		7,400		-375	-4.8%
Component sales	5,518		4,400		-1,118	-20.3%

We encourage readers to review our complete legal statement on “Disclaimer” page.



Daikoku Denki Co.

6430 Tokyo Stock Exchange First Section

3-Aug.-15

Results forecasts by segment are as follows.

Sales in the Information System Segment are forecast to decline 5.7% y-o-y to ¥35,000mn, and segment operating profit to fall 31.7% to ¥2,900mn. The Company anticipates it will sell 150 hall computers (up 14.5%). However, the reason it is forecasting a decline in sales are that the new product effects that caused sales of peripheral equipment (CR units and information disclosure equipment) to grow a pace greater than anticipated up to the previous fiscal year have run their course. On the other hand, sales of the Management Support Service (MG Service) that the Company is promoting are forecast to grow steadily to ¥3,720mn (up 10.0% y-o-y), and are expected to underpin the performance of its highly profitable services.

In addition to the impact of lower sales in keeping down profits, development expenses of ¥3,700mn (up 36.5% y-o-y) for the next-generation hall computers are planned and consequentially, the segmental profit margin is expected to fall to 8.3% (from 11.4% in previous fiscal year).

In the Control System Segment, a major recovery in results is expected, with sales to rise 47.5% y-o-y to ¥25,000mn and segmental profit to reach ¥1,000mn (compared to a loss of ¥1,105mn in the previous fiscal year). Continuing on from the previous fiscal year, the number of display units sold will be impacted by the decline in the number of models and also because the rate of reused parts among customers will be at the same level as the previous fiscal year. But the growth in results from the fully fledged deployment of the Company's own brand pachinko slot machines is expected to be a major driving force behind the recovery in results. Specifically, based on a sales target of a total of 30,000 units from 4 models, the Company is forecasting to return to profitability with sales of ¥10,000mn.

In terms of profits, while R&D expenses are set to increase ¥1,900mn (up 69.0% y-o-y), this will be absorbed by the higher sales and in addition, the temporary cost factors of the previous fiscal year will be eliminated. Therefore, the Company is forecasting a major improvement in the segmental profit margin of 4.0% (compared to a loss of ¥1,105mn in the last fiscal period).

**Sales Targets in FY3/16**

	Sales Volumes (Information Systems)		
	FY3/14	FY3/15	Y-o-Y
Hall computers	131 Units	150 Units	19 Units
Call lamps			
BiGMO series	17,125 Units	20,000 Units	2,875 Units
BiGMO PREMIUM	58,587 Units	60,000 Units	1,413 Units
IL-X	82,747 Units	85,000 Units	2,253 Units
VEGASIA CR units	109,561 Units	90,000 Units	-19,561 Units
Face recognition systems	11 Stores	30 Stores	19 Stores

	Sales Volumes (Control Systems)		
	FY3/14	FY3/15	Y-o-Y
Display unit models	14 Products	14 Products	±0 Products
Units sold	247,649 Units	238,000 Units	-9,649 Units

At FISCO, we consider that the Company's results will be dictated by the effects of industry self regulation and the trends in the sales of pachinko slot machines. The former may have a negative impact in the H2 of the year, but as the Company has already fully analyzed its potential impact and incorporated this into its forecasts, it is considered that it will not be a factor behind results falling below targets. With regards to the latter also, as indicated by the results of Sasami-san@Ganbaranai Slot that was a hit product in the previous fiscal year, the Company has acquired name recognition as a high quality brand specializing in anime, so it is thought that achieving its sales target of an average of 7,500 units per model will not be that high of a hurdle.

## ■ Company History

### **An industry leader and the first in its industry to become a member of Keidanren (Japan Economic Federation)**

The predecessor of Daikoku Denki was established in Osaka City in 1964 by Shinji Kayamori, the father of Daikoku Denki's current president, Hideyuki Kayamori. Initially, the Company was a sales agency for electronic calculators. It then branched out into the sale of magnetic counters and developed devices to count the coins inserted into baseball pitching machines at batting centers. In 1968, it developed a device to count the balls in a pachinko machine, its first venture into the pachinko industry. In 1974, the Company entered the hall computer business, and since the 1990s, as pachinko and pachinko slot machines have become more electronic, the Company has supported the growth of the pachinko industry by supplying superior hall computers, which have become the most important tool for operating halls efficiently.

In 1990, the Company developed the DK-SIS service, the membership information service for pachinko halls, and the pachinko industry's first call lamps, which display information about Jackpot machines. In 1991, the Company began selling Data Robo terminals, which provide information about varieties of pachinko machine models to fans of these machines. By developing such revolutionary equipment for managing data and disclosing information, the Company contributed to the efficient operation of pachinko halls, increased the pleasure of pachinko fans, and supported the sales and profits of the pachinko industry.

By the mid-1990s, the Company had established a position of the leading company in the pachinko equipment market, but in 1996, the pachinko industry changed the regulations pertaining to pachinko machines, and scrapped about 700,000 pachinko machines that judged to be too conducive to gambling and considered socially inappropriate. This caused a sharp drop in sales in the pachinko industry and at the Company, which lost about 100 employees that year. During such a trying period, the current president, Hideyuki Kayamori entered the Company. He had studied information technology at Kyoto University's graduate school and he is not only planning to expand current business base but also envisions next generation business by utilizing the vast amount of data the Company had accumulated.

With the aim of converting pachinko and pachinko slot games into socially acceptable forms of amusement, in 2006, Daikoku Denki established as a subsidiary pachinko slot machine maker, Daxel Inc. and began developing its own pachinko slot machines.

Daikoku Denki listed its shares on the Second Sections of the Tokyo Stock Exchange and the Nagoya Stock Exchange in November 2002. In April 2004, it elevated its listings to the First Sections of both exchanges. In 2014, the Company celebrated its 50th year and became a member of Keidanren, the Japan Economic Federation, as the first member with business centering on the pachinko equipment industry.

## ■ Growth Strategy

### **Its strength that enables it to undertake large-scale developments is a major advantage**

The Company is pursuing its three-year medium term management plan with FY3/15 as its first year. It has positioned the period until its next generation hall computers are completed as an important investment period and is implementing business reforms in order to develop the industry as a whole and achieve further growth. The Company has not disclosed any specific numerical targets, but it is taking the following three steps to achieve growth over the medium to long term.

### 1) Developing the next-generation hall computer

In FY3/14, the Company started developing the next-generation hall computer, which will operate on a cloud server and be capable of advanced analysis of Big Data. Unlike previous hall computers, the next-generation computer will be able to gather and analyze data on customer behavior and to recommend actions to improve sales and profits, thereby contributing to the growth of the pachinko hall industry. This capability could also be applied to other business areas. For three years from FY3/15, the Company plans to invest about ¥10bn in R&D primarily to develop the next-generation hall computer (including for peripheral equipment), although it has not announced a date for the initial sales of this computer. By launching sales of this computer, which will be far superior to any other such machine, over the medium term the Company plans to raise its share of the Japanese market for hall computers to 50%, as Tokyo prepares to host the Olympic Games in 2020. In September 2014, the Company expanded its Kasugai Plant in Aichi Prefecture to help it increase its market shares in information systems.

### 2) Converting business model to stock type revenue model

The Company is changing its Information System Segment's business model to stock type revenue system that collects service fees after the sale of such equipment. This change allows the Company to sell its hall computers and peripheral equipment at low prices, thereby increasing its price competitiveness and its market shares while after-sale service fees will be stable source of earnings.

### 3) Expanding the in-house developed pachinko slot machines

In-house developed pachinko slot game machines under its own brand are another growth driver planned by the Company. The first commercially successful model, Magical Suite Prism Nana, which was released in FY3/14, was the first such machine in the industry incorporating original characters and unique view of the world, and sold around 4,000 units. In addition to Sasami-san@ Ganbaranai Slot, which became a big hit product in the previous fiscal year, by incorporating a condensed version of all 12 episodes of a TV anime and the installation of large all LCD screens and large capacity 64GbitROM, the Company is realizing a form of pachinko slot entertainment that offers players new experiences with the emphasis placed on story, and has established a high quality brand image specialized in anime. Going forward also, its policy is to develop its businesses centered on the "Moe Suro (slot game with attractive characters)" model that is attracting attention in the "anime age," and rather than enjoyment only from the number of balls, players will enjoy the story content that is incorporated into playing its pachinko slot machines and the Company is planning to convert the pastime to a more socially acceptable form of amusement.

Profitability is forecast for this business in FY3/16 on a single fiscal year basis, and in the medium term, the Company aims for a market share of 5–10%. Toward this end, it plans to continue to invest heavily in development.

At FISCO, we considered that within the harsh business environment in the pachinko and pachinko slot industry, the fact that the Company is able to invest around ¥10 billion in the development of next generation hall computers is a major advantage. Even though the market is shrinking, we think it is fully possible that it will be able to achieve growth through increasing its market share. In addition, it is also highly likely that there will be a weeding-out of players in the hall computers industry based on capital strength, and this trend toward industry restructuring is also likely to work to the Company's advantage.

On the other hand, from this fiscal year the Company has begun the fully fledged deployment of its in-house developed pachinko slot machines and it will be necessary to keep an eye on how they perform in the future. Compared to existing manufacturers, it is able to spend a sufficient amount of time and money on developing each model, and it utilizes data analysis in order to develop machines that are highly appealing and enjoyable to play. So on these points also, it is considered fully possible that the Company will be able to demonstrate its superiority and these slot machines will greatly contribute to its results as a new growth driver. However, rather than stealing existing market share from its competitors, the key to successfully stimulating the market as a whole is likely to be creating original value that only the Company is able to provide in order to capture a new target market, such as anime fans. We will be paying close attention to whether it is able to achieve this.

## Shareholder Returns

### Provides a supplemental dividend based on results

The Company's policy up until recently was to pay an annual dividend of a minimum of ¥40 per share (a stable dividend) and to supplement this payment depending on its profits. But from FY3/16, it has raised the stable dividend to ¥50 per share

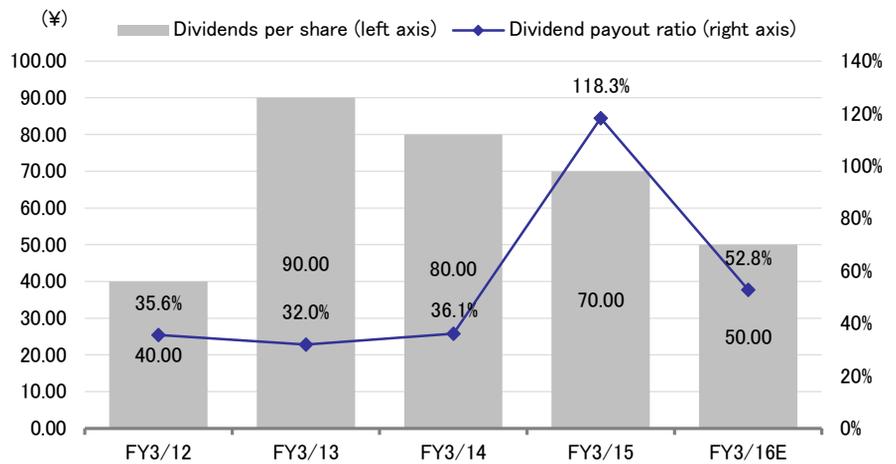
For FY3/15, initially an annual dividend of ¥40 was forecast, but in order to implement its policy of strengthening its management foundations, the Company has decided to pay an interim dividend of ¥10 per share and a year-end dividend of ¥60 per share for a total dividend of ¥70 per share. For FY3/16, an annual dividend of ¥50 is forecast (interim dividend of ¥10 and a year-end dividend of ¥40). However, as was stated above, the Company's policy is to supplement its dividend payment based on results, so the dividend may be increased.

Daikoku Denki Co.

6430 Tokyo Stock Exchange First Section

3-Aug.-15

Dividends per Share and Dividend Payout Ratio



## Disclaimer

FISCO Ltd. (the terms "FISCO", "we", mean FISCO Ltd.) has legal agreements with the Tokyo Stock Exchange, the Osaka Exchange, and Nikkei Inc. as to the usage of stock price and index information. The trademark and value of the "JASDAQ INDEX" are the intellectual properties of the Tokyo Stock Exchange, and therefore all rights to them belong to the Tokyo Stock Exchange.

This report is based on information that we believe to be reliable, but we do not confirm or guarantee its accuracy, timeliness, or completeness, or the value of the securities issued by companies cited in this report. Regardless of purpose, investors should decide how to use this report and take full responsibility for such use. We shall not be liable for any result of its use. We provide this report solely for the purpose of information, not to induce investment or any other action.

This report was prepared at the request of its subject company using information provided by the company in interviews, but the entire content of the report, including suppositions and conclusions, is the result of our analysis. The content of this report is based on information that was current at the time the report was produced, but this information and the content of this report are subject to change without prior notice.

All intellectual property rights to this report, including copyrights to its text and data, are held exclusively by FISCO. Any alteration or processing of the report or duplications of the report, without the express written consent of FISCO, is strictly prohibited. Any transmission, reproduction, distribution or transfer of the report or its duplications is also strictly prohibited.

The final selection of investments and determination of appropriate prices for investment transactions are decisions for the recipients of this report.

FISCO Ltd.