

FreeBit Co., Ltd.

3843

Tokyo Stock Exchange First Section

31-Jan.-2018

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FISCO Ltd.

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

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■ Summary

Profits down on higher sales in FY4/18 1H (as planned) Close to realizing investment results in life revolution fields

FreeBit Co., Ltd. <3843> (hereafter, also the Company") provides a variety of Internet-related services mainly to corporations, including infrastructure for Internet service providers (ISPs), support for entering the MVNO*¹ business as a Mobile Virtual Network Enabler (MVNE), cloud infrastructure, particularly virtual data centers (VDCs)*², and consulting and solutions for Internet services. It also works through Group companies to supply ISP services, MVNO services, web marketing services, Internet services to collective housing (condominiums), and other services to individuals.

*¹ MVNO is the abbreviation of Mobile Virtual Network Operator. It is a virtual mobile communications business that involves conducting an independent communication business by piggybacking on the wireless communications infrastructure of other communication businesses, such as NTT DOCOMO, INC. <9437>, KDDI CORPORATION <9433>, and SoftBank Corp. <9984>.

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

In September 2016, the Company launched the HealthTech Business, the core of which is the business of EPARK Health Care, Inc. (currently, FreeBit EPARK Health Care, Inc.), which was made a consolidated subsidiary. In March 2017, it made a consolidated subsidiary of For Members, which conducts a real estate brokerage business, to acquire a foothold in the real estate tech field.

1. FY4/18 1H result trends

Profits declined on higher sales in FY4/18 1H consolidated results with net sales of ¥19,407mn (+3.8% year on year (YoY)), operating profit of ¥422mn (-62.2%), ordinary loss of ¥300mn, and net loss attributable to owners of parent of ¥806mn. Sales grew in 1H thanks to gains in the Broadband Business with a rise in condominium Internet deployments and expansion of business scale in ad technology service and affiliate service within the Ad Technology Business. Operating income fell sharply because of increases in SG&A expenses (personnel costs and other expenses) amid investments in the HealthTech and Real Estate Tech Businesses.

2. FY4/18 outlook

FreeBit should maintain initial forecasts for FY4/18, targeting sales and profit gains of ¥40,000mn in net sales (+13.6% YoY), ¥2,000mn in operating income (+51.4%), ¥1,900mn in ordinary income (+135.3%), and ¥100mn in profit attributable to owners of parent. The projected 13.6% sales increase factors in advances in the Ad Technology and Broadband Businesses as overall drivers. Operating income should expand to ¥2,000mn, despite investment outlays in the HealthTech and Real Estate Tech Businesses, due to larger profit increases in the Broadband and Ad Technology Businesses. While the HealthTech Business posted a ¥460mn loss in 1H, we expect a substantial improvement in 2H income because subsidiary FreeBit EPARK Health Care realized single-month profitability in November.

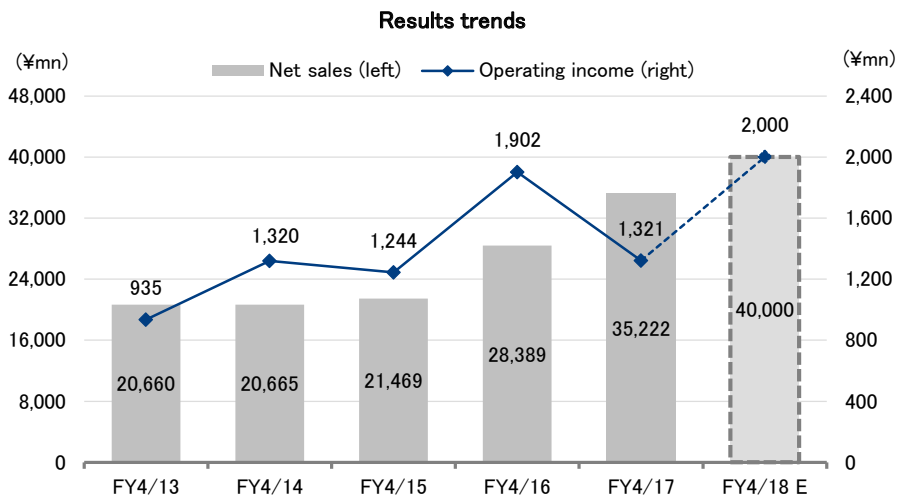
Summary

3. Medium- to long-term growth strategy

FreeBit announced SiLK VISION 2020, a four-year medium-term business policy, in June 2016 with FY4/20 goals of ¥50,000mn in sales and ¥5,000mn in operating income. In Lifestyle Revolution area, FreeBit has been investing in the HealthTech and Real Estate Tech Businesses. The HealthTech Business attained single-month profitability in November 2017 and is likely to post breakeven income in FY4/18 3Q as a result. In the Real Estate Tech Business, FreeBit acquired For Members, which handles real estate brokering services under the Aeon Housing brand, as a consolidated subsidiary and is currently striving to improve income and establish advantages with the rollout of new services utilizing IT. It aims to reach single-month profitability during FY4/19. These investments have arrived at transitions from investment to recovery phases, albeit with some discrepancy in phase timing, and are close to realizing results.

Key Points

- Mainly relies on the cash-generating Broadband Business and the all-time high earnings of the Ad Technology Business
- Reported lower profits on increased sales in FY4/18 1H, investing in the HealthTech Business as planned
- Close to realizing investment results in the Lifestyle Revolution area



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

■ Company profile

Broadly supplies Internet and mobile infrastructure Diversifying into utilization of information technology in health care, real estate, and other life businesses

1. Company profile

The Company provides a variety of Internet-related services mainly to corporations, including infrastructure for ISPs, support for entering the MVNO business as an MVNE, cloud infrastructure, particularly VDCs, and consulting and solutions for Internet services. It also works through Group companies to supply ISP services, MVNO services, web marketing services to individuals, as well as Internet services to collective housing (condominiums), and other services.

Tone mobile inc., a joint venture with Culture Convenience Club Co., Ltd. and equity-method affiliate of the Company, is currently focusing on expansion of smartphone business, including through provision of the TONE proprietary smartphone service.

2. Company history

The Company was founded in Shibuya Ward, Tokyo, in 2000 (its predecessor was FreeBit.com Co. Ltd.). Its business grew mainly for services for ISPs and it was listed on the Mothers market of the Tokyo Stock Exchange in 2007. Using the opportunity of its listing, it accelerated the expansion of its business areas through M&A. It made a consolidated subsidiary of DREAM TRAIN INTERNET INC. in that same year and of GIGAPRIZE Co., Ltd. <3830> in 2009. In 2010, alongside making a consolidated subsidiary of Full Speed Inc. <2159>, which is an Internet advertising agency, the Company also made consolidated subsidiaries of For it Inc., which conducts an affiliate advertising business, and BEKKOAME INTERNET. INC., which conducts an IT platform business. In this way, it is expanding its business areas based on its corporate philosophy of "Being the NET frontier! Expand the Internet and contribute to society." In 2011, it entered the MVNE/MVNO business and also accelerated growth in the mobile business field. In 2016, it entered the health tech business, using an M&A as the first step. In March 2017, to acquire a foothold in the real estate tech field, it made a consolidated subsidiary of For Members, which conducts a real estate brokerage business. In 2016, its listing was reassigned to the First Section of the Tokyo Stock Exchange.

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 3843 Tokyo Stock Exchange First Section | <http://freebit.com/en/ir/highlights.html>

Company profile

Company history

Date	Main events
May 2000	Founded as FreeBit.com Co., Ltd. in Shibuya Ward, Tokyo, to provide Internet business support
December 2002	Changed its corporate name from FreeBit.com Co., Ltd. to FreeBit Co., Ltd.
March 2007	Listed on the Mothers market of the Tokyo Stock Exchange
August 2007	Made a consolidated subsidiary of DREAM TRAIN INTERNET INC., which operates an ISP business for individuals
March 2009	After making a consolidated subsidiary of Media Exchange Co., Ltd., which had been listed on the Mothers market of the Tokyo Stock Exchange (delisted after becoming the Company's wholly owned subsidiary and merged with DREAM TRAIN INTERNET through an absorption merger), its subsidiary GIGAPRIZE Co., Ltd. <3830>, which conducts a condominium ISP business, was also made a consolidated subsidiary
August 2010	Made consolidated subsidiaries of Full Speed Inc. <2159>, which operates an Internet advertising agency, For it Inc., which operates an affiliate advertising business and provides its proprietary program Affiliate B, and BEKKOAME INTERNET. INC., which operates an IT platform business
March 2011	Entered into the MVNO business (as a MVNE)
June 2012	Full Speed launched the advertising management integration program AdMatrix series
July 2013	Started providing the freebit MVNO Pack, an MVNE (MVNO supporter) service for MVNOs through an L2 connection from NTT DOCOMO, INC. <9437>
November 2013	DREAM TRAIN INTERNET started providing freebit mobile, an MVNO service that offers all aspects, from terminal development through to user support, in an integrated manner
January 2015	Established FreeBit Mobile, Inc., which conducts an MVNO business (currently, Tone mobile inc., a joint-venture company with Culture Convenience Club Co., Ltd.)
April 2015	Founded freebit investment inc. with the objective of conducting investments for business expansion
September 2015	DREAM TRAIN INTERNET started providing DTI SIM, a mobile, high-speed data communications service
December 2015	Full Speed established GoJapan Inc. as a joint-venture company with Asia Smart Travel (Beijing) Information Technology Co., Ltd. and started a travel app business for tourists visiting Japan
March 2016	Started to provide mobabiji, a cloud PBX service for corporations
July 2016	Listing changed to the First Section of the Tokyo Stock Exchange
September 2016	Made a consolidated subsidiary of EPARK Health Care, Inc., which provides health care solutions services
February 2017	Changed the corporate name of EPARK Health Care to FreeBit EPARK Health Care, Inc.
March 2017	GIGAPRIZE made a consolidated subsidiary of For Members
April 2017	GIGAPRIZE merged with its wholly owned subsidiary ESP Co., Ltd. through an absorption merger
May 2017	Full Speed conducted a company split for the video ad network business for smartphones and established Calmbold Inc.
August 2017	Acquired Medip inc., a digital signage provider for medical facilities, as a consolidated subsidiary

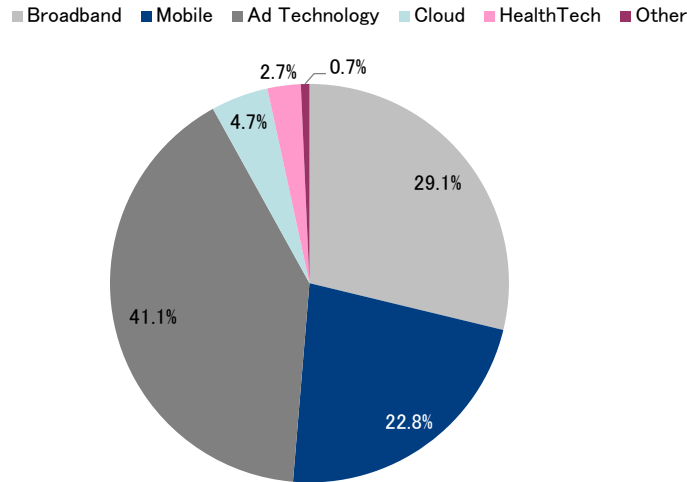
Source: Prepared by FISCO from the Company's website

Company profile

3. Business descriptions

Segment sales breakdown consists of Broadband Business at 29.1%, Mobile Business at 22.8%, Ad Technology Business at 41.1%, Cloud Business at 4.7%, HealthTech Business at 2.7%, and Other Businesses at 0.7%.

Percentage of net sales by segment (FY4/18 1H)



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

■ Business overview

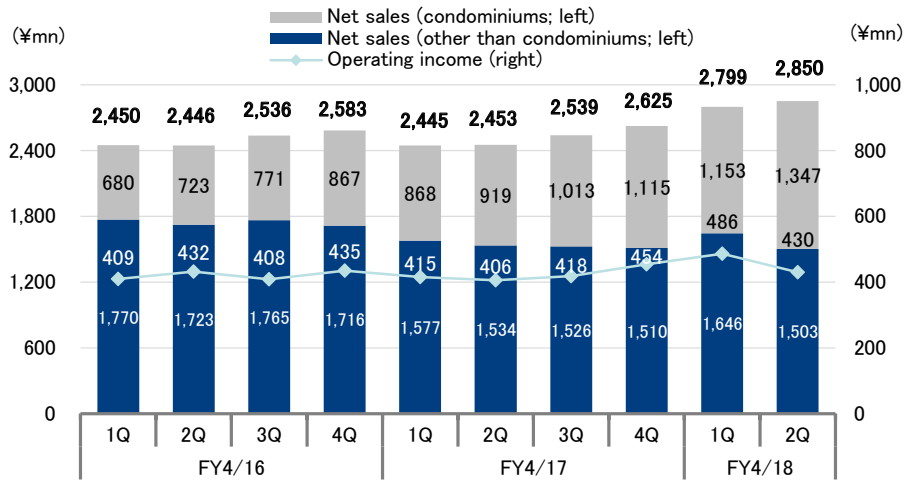
Mainly relies on the cash-generating Broadband Business and the all-time high earnings of the Ad Technology Business

1. Broadband Business

Sales climbed 15.3% YoY to ¥5,649mn and segment profit rose 11.7% to ¥916mn in FY4/18 1H, posting double-digit gains in sales and profit. Condominium Internet sales increased at GIGAPRIZE. This improvement lifted profit, even with higher personnel costs and costs related to starting the Aeon Housing business. Condominium Internet deployments are picking up thanks to the launch of collaborations with multiple large home manufacturers. Installations reached a total of 220,000 homes (up by 29,000 homes versus the end of the previous fiscal year). The operating margin is strong at 16.2% (FY4/18 1H). This business functions as a cash cow for FreeBit.

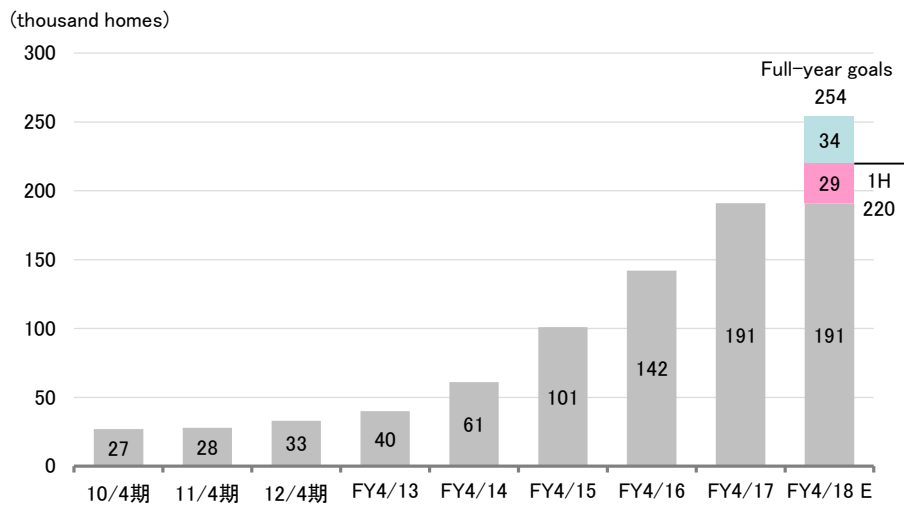
Business overview

Net sales and segment profit in the Broadband Business



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

Trends in the introduction of condominium Internet services

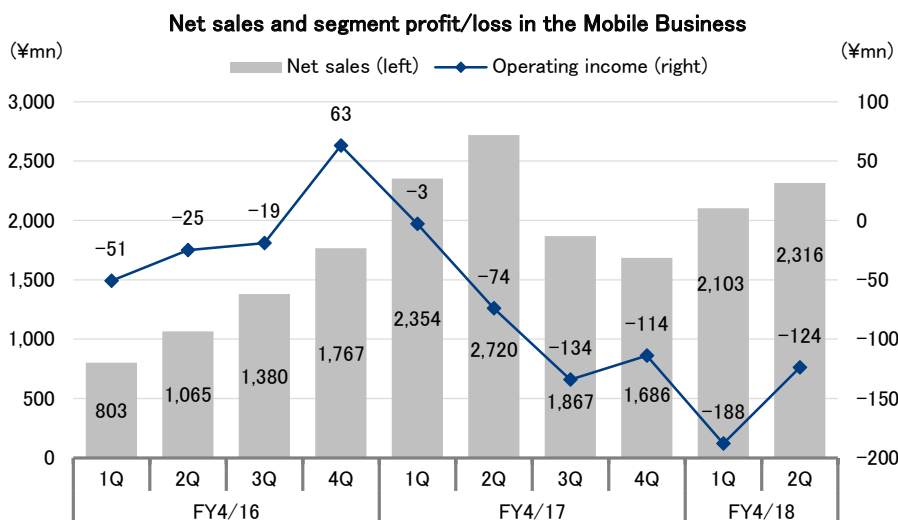


Source: Prepared by FISCO from the Company's results briefing materials

Business overview

2. Mobile Business

Sales dropped 15.3% YoY to ¥4,420mn in FY4/18 1H mainly due to a decline in initial issuance of SIM cards and the absence of a large one-time sale of smartphones to Tone mobile recorded in the previous year. The Mobile Business faces uncertainty in its business environment because of the impact of management strategies at MVNOs, its customers. FreeBit intends to pursue growth in B2C services (DTI SIM and Tone mobile) and solutions services (mobabiji, freebit cloud security SIM, and others) with a robust gross margin and thereby improve its earnings structure. In September 2017, provision of DTI SIM's prefix-type voice call option Otoku Call began.



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

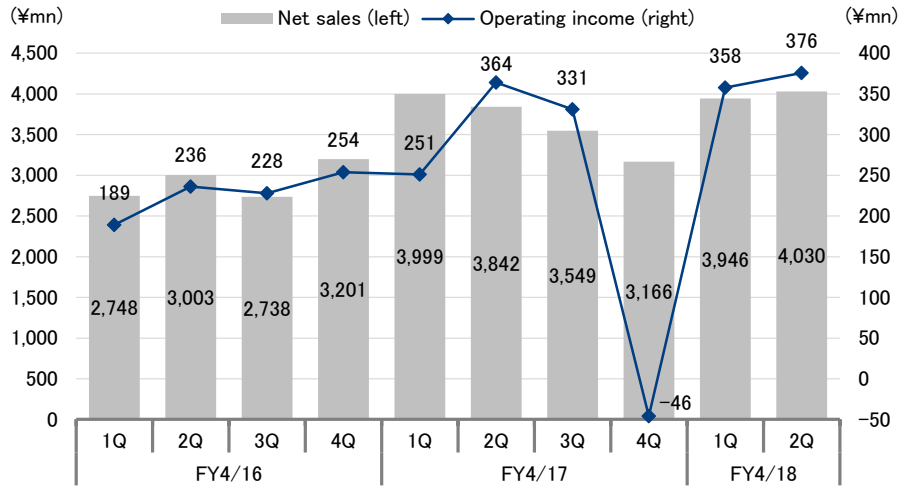
3. Ad Technology Business

Both sales and profits booked all-time highs in FY4/18 1H at ¥7,976mn in sales (+3.5% YoY) and ¥735mn in segment profit (+26.1%). Main profit drivers were higher gross profit accompanying increased sales at the Full Speed Group and an earnings boost from decline in provisions to the allowance for doubtful accounts. AdMatrix, a proprietary total platform for ad operations, has been making further advances with a new video function and acquisition of its own data. This platform is solidifying its position as the No.1 domestic Demand Side Platform (DSP). The afb affiliate platform*2, an affiliate service provider (ASP)*3, offers highly rated unique features and has been sustaining No.1 status in media usage satisfaction. Business has been steadily expanding thanks to these aspects. FreeBit intends to establish a branch company to handle entry into the Taiwanese market that has strong affinity with affiliates in January 2018.

*2 Network of over 550,000 partner sites. Utilizing PC knowhow to deploy services to tablets, smartphones, and mobile devices. Formerly called "Affiliate B."
 *3 Service provider that distributes ads with performance-based fees

Business overview

Net sales and segment profit/loss in the Ad Technology Business



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

Overview of B-to-B marketing

No.1 domestic DSP in B-to-B marketing

Realization of ADMATRIX DSP, a proprietary targeting ad distribution platform

Establishing an overwhelming industry position with domestic top-class corporate IP data obtained using proprietary technology plus a new video function and further expansion of proprietary data



B-to-B marketing assistance DSP capable of targeting domestic companies and industries that possesses domestic top-level distribution inventory volume and utilizes the largest domestic IP data volume and proprietary analysis technology

Patent-applied technology **DOI** (Dynamic Office IP Identification)

Variable IP address / Fixed IP address

Alliance partners (DMP)

Recent release plan coming soon

Movie function
New video function

✕

New Data
Acquisition of unique data

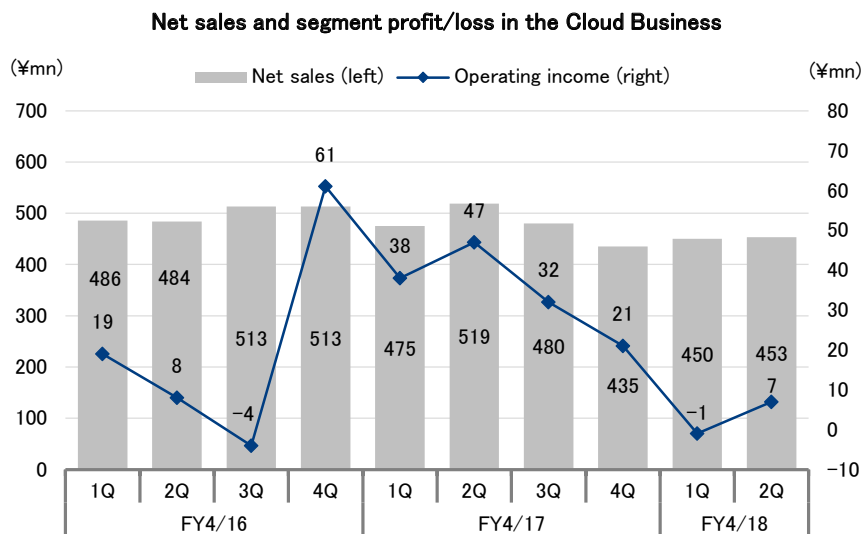
Source: Prepared by FISCO from the Company's results briefing materials

Business overview

4. Cloud Business*

Sales declined 11.1% YoY to ¥904mn and segment profit dropped sharply to ¥600mn (-94.8%) in FY4/18 1H. Profit weakened on increase in prorated costs because of takeovers of group subsidiaries in the context of ongoing revisions to legacy service.

* Cloud refers to the format of supplying software and other contents through a network to users and data centers and servers that store and manage related data. A public cloud is a service or system that anyone can use from the Internet. A private cloud is a service or system used by a large company or others on a self-operated network. A hybrid cloud has both aspects and combines advantages of the two formats to enhance security and cost management.



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

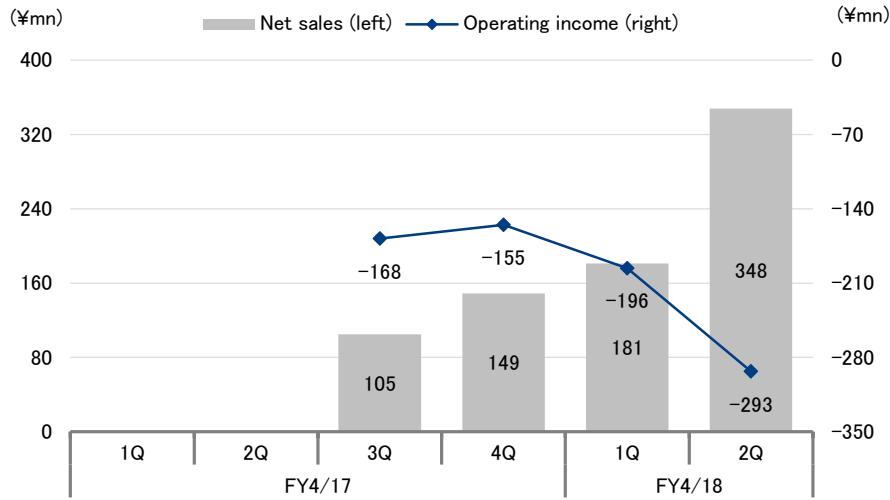
5. HealthTech Business

In FY4/18 1H, net sales were ¥529mn and the segment loss was ¥490mn. In September 2016, the Company acquired the shares (acquired 47.5% of the voting rights) and made a consolidated subsidiary of EPARK Health Care, which specializes in the pharmacy industry and provides various services, including EPARK Kusuri-no-Madoguchi, a comprehensive pharmacy portal site. In February 2017, its corporate name was changed to FreeBit EPARK Health Care and it began conducting business in the health tech field.

The business concept is for the Company to evolve its technological capabilities for the media platform that connects to the end users (the patients) and the dispensing pharmacies, and to provide information and highly convenient reservation, delivery, and other services to these end users. The revenue models are diverse and include advertising revenue as media, commission from receiving patients, and reservation system usage fees. "EPARK OKusuri Techo" is a free app handled as a service for end users (patients), and it has been attracting attention for its highly convenient functions, including pharmacy-reception reservations, an alarm to indicate when it is time to take medicine, and drug-information registration. It has been reported on by the media and cumulatively it has been download more than 180,000 times (as of October 2017), which makes it the No.1 app of its kind. The number of reservations at pharmacies is rising exponentially and further growth is expected in the future as per store reservations are also increasing. This segment achieved profitability in November 2017 on a single-month basis despite being in the middle of an investment phase. It is also likely to achieve profitability on a half yearly basis during FY4/18 2H.

Business overview

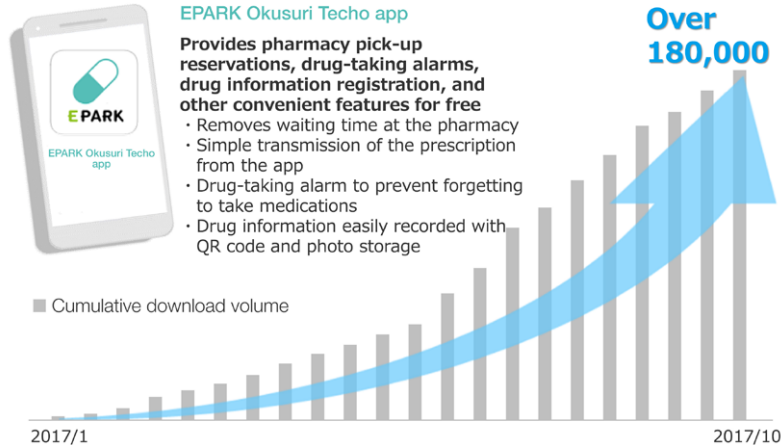
Net sales and segment loss in the HealthTech Business



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

Progress in the HealthTech Business

Cumulative downloads of the EPARK OKusuri Techo app at over 180,000



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

Results trends

Reported lower profits on increased sales in FY4/18 1H Investing in HealthTech Business and others as planned

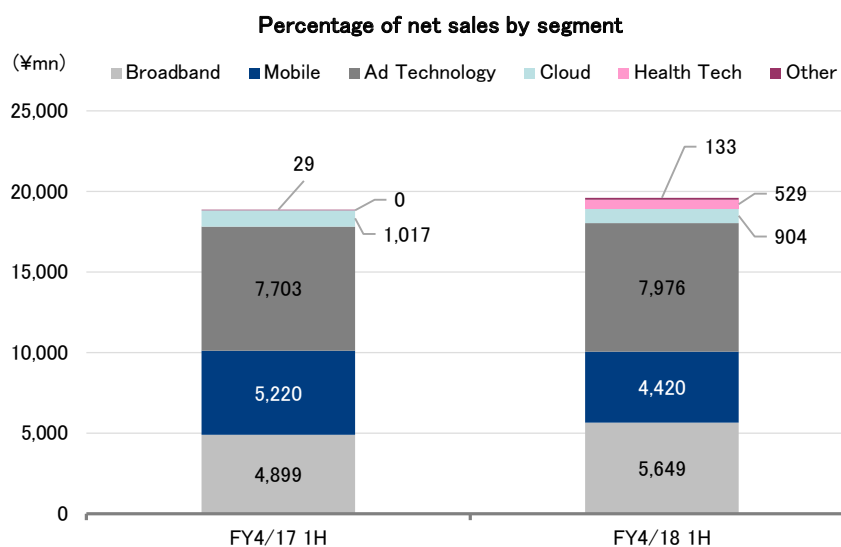
1. FY4/18 1H results

In the FY4/18 1H consolidated results, net sales increased 3.8% (YoY) to ¥19,407mn, operating income decreased 62.2% to ¥422mn, ordinary loss was ¥3mn, and the net loss attributable to owners of parent was ¥806mn. The Company posted increased sales and decreased profits.

FY4/18 1H results

	FY4/17 1H		FY4/18 1H		YoY
	Result	Ratio to sales	Result	Ratio to sales	
Net sales	18,689	-	19,407	-	3.8%
Cost of sales	14,349	76.8%	14,569	75.1%	1.5%
Gross profit	4,339	23.2%	4,838	24.9%	11.5%
SG&A expenses	3,221	17.2%	4,415	22.8%	37.1%
Operating income	1,118	6.0%	422	2.2%	-62.2%
Ordinary income	839	4.5%	-3	-0.0%	-
Profit attributable to owners of parent	192	1.0%	-806	-4.2%	-

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



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

Results trends

Sales strengthened 3.8% YoY primarily due to growth in the Broadband Business from increase in deployments of condominium Internet facilities and expansion of ad technology services and affiliate services in the Ad Technology Business. Gross profit increased 11.5% on manifestation of businesses where FreeBit has been investing. SG&A expenses climbed sharply by 37.1% due to higher personnel costs and other expenses related to growing business scale. Operating profit hence fell 62.2%. By segment, FreeBit's structure roughly consists of profits obtained in the Broadband and Ad Technology Businesses and investments in the HealthTech and Real Estate Tech Businesses.

Ordinary income came under pressure from a heavy impact by the decline in operating income and a share of loss of entities accounted for using equity method related to expansion of the Tone mobile business. Net profit attributable to owners of parent slipped mainly on the setback in ordinary income.

Reinforced investments, though financial soundness is not an issue

2. Financial position and management indicators

Total asset value increased ¥707mn from the end of the previous fiscal year to ¥26,304mn at end-FY4/18 1H. Current assets rose by ¥494mn mainly from an increase of ¥837mn in notes and accounts receivable - trade and a decline of ¥477mn in cash and deposits. Non-current assets were up by ¥212mn primarily due to rise in investments and other assets of ¥238mn.

Liabilities grew by ¥1,596mn from the end of the previous fiscal year to ¥15,942mn. Within this, current liabilities increased by ¥549mn (primarily higher short-term loans) and non-current liabilities increased by ¥1,046mn (mainly higher long-term borrowing).

In the management indicators of financial stability (at the end of FY4/18 1H), the current ratio was 176.8% and the equity ratio was 33.0%, so there are no concerns about the Company's financial stability despite aggressive investments.

Results trends

Consolidated balance sheet and management indicators

	End-FY4/17	End-FY4/18 1H	Change
(¥mn)			
Current assets	17,414	17,908	494
(Cash and deposits)	10,249	9,771	-477
(Notes and accounts receivable - trade)	4,226	5,064	837
(Merchandise and finished goods)	202	437	235
Non-current assets	8,182	8,395	212
(Intangible assets)	4,708	4,606	-102
(Investments and other assets)	1,587	1,826	238
Total assets	25,597	26,304	707
Current liabilities	9,579	10,129	549
Non-current liabilities	4,766	5,812	1,046
Total liabilities	14,346	15,942	1,596
Total net assets	11,251	10,362	-888
Total liabilities and net assets	25,597	26,304	707
<Soundness>			
Current ratio (current assets ÷ current liabilities)	181.8%	176.8%	-
Equity ratio (shareholders' equity ÷ total assets)	37.7%	33.0%	-

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

Forecasts

FreeBit should maintain initial forecasts for FY4/18 targeting of ¥40,000mn in sales and ¥2,000mn in operating income. It has confidence in a recovery in profitability from likely realization of single-month profitability in the HealthTech Business in 2H.

● FY4/18 outlook

The forecasts for the FY4/18 full year consolidated results are for higher sales and profits, affirming initial forecasts, with net sales to increase 13.6% YoY to ¥40,000mn, operating income to rise 51.4% to ¥2,000mn, ordinary income to grow 135.3% to ¥1,900mn, and profit attributable to owners of parent of ¥100mn.

Forecasts

The Ad Technology and Broadband Businesses will continue to drive growth in sales. Total sales are likely to expand 13.6% YoY, including the addition of sales from a subsidiary in the HealthTech Business (covered by consolidation since 2H of the previous year) for a full year. The upbeat Broadband Business and the recovery in the Ad Technology Business, which incurred a decline in profit in the previous year on non-collection of one-time credits, should lead growth in operating income. While FreeBit actually has the potential for about ¥2,800mn in FY4/18 operating income, the outlook was ¥2,000mn because of investments totaling about ¥800mn in the HealthTech and Real Estate Tech Businesses. Impacts on operating income in 1H amounted to -¥460mn in the HealthTech Business and -¥70mn in the Real Estate Tech Business. FreeBit EPARK Health Care, the subsidiary in the HealthTech Business, should head toward breakeven income in the HealthTech Business during 2H, judging from its attainment of single-month profitability in November, and thereby remove one of the factors that weighed on operating income. Additionally, the majority of goodwill from the DREAM TRAIN INTERNET acquisition already ended in 1H. FreeBit expects a contribution to higher profits on decline in goodwill amortization charges totaling about ¥170mn.

Outlook for FY4/18

(¥mn)

	FY4/17		FY4/18			
	Result	Ratio to sales	Forecast	Ratio to sales	YoY	Progress rate
Net sales	35,222	100.0%	40,000	100.0%	13.6%	48.5%
Operating income	1,321	3.8%	2,000	5.0%	51.4%	21.1%
Ordinary income	807	2.3%	1,900	4.8%	135.3%	-0.2%
Profit attributable to owners of parent	-150	-0.4%	100	0.3%	-	-

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

We think sales have been steadily proceeding at the plan pace with the 1H fulfillment rate at 48.5%. Operating income is likely to sharply recover thanks to the healthy Broadband Business, removal of one-time adverse impacts in the Ad Technology Business from the previous fiscal year, and anticipated gains in earnings of the Mobile and HealthTech Businesses. Ordinary income faced a ¥408mn investment loss at equity-method affiliate Tone mobile in 1H. This might linger as an impact on full-year earnings.

Medium- to long-term growth strategy

Realizing results from investments in Lifestyle Revolution area

The Company announced SiLK VISION 2020, its four-year medium-term business policy, in June 2016, which targets net sales of ¥50,000mn and operating income of ¥5,000mn in FY4/20. It has designated the core businesses and services for the two growth areas in the Group’s basic policy, of Mobile Revolution and Lifestyle Revolution.

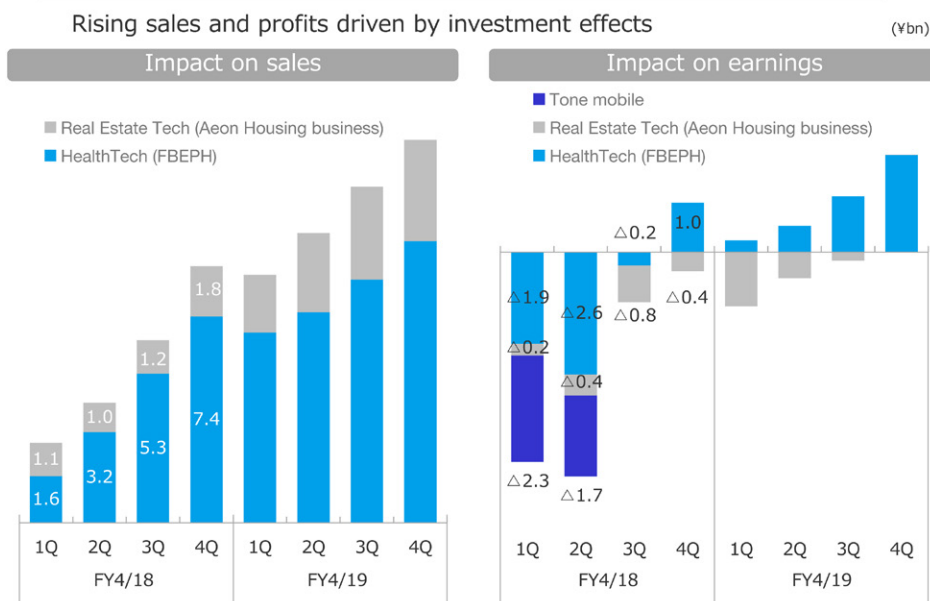
In the Lifestyle Revolution area, FreeBit has steadily invested in the HealthTech and Real Estate Tech Businesses, including about ¥460mn in health tech and around ¥70mn in real estate tech in FY4/18 1H (these investments lowered operating income). In the HealthTech Business, FreeBit attained single-month profitability in November 2017 and has a scenario of breakeven income in FY4/18 3Q. In the Real Estate Tech Business, FreeBit acquired For Members, which handles real estate brokering services under the Aeon Housing brand, as a consolidated subsidiary and is currently striving to improve income and establish advantages with the rollout of new services utilizing IT. It aims to reach single-month profitability during FY4/19.

In the Mobile Business, FreeBit contributed about ¥400mn in FY4/18 1H for the purpose of service expansion, advertising and promotions, and provision of a discounted plan in order to increase subscriber volume at equity-method affiliate Tone mobile. There are no plans for additional investment, and it appears that this business can survive on its own.

These investments have arrived at transitions from investment to recovery phases, albeit with some discrepancy in phase timing, and are close to realizing results. HealthTech Business, in particular, is attracting expectations.

Business outlook

Outlook for investments in focus businesses

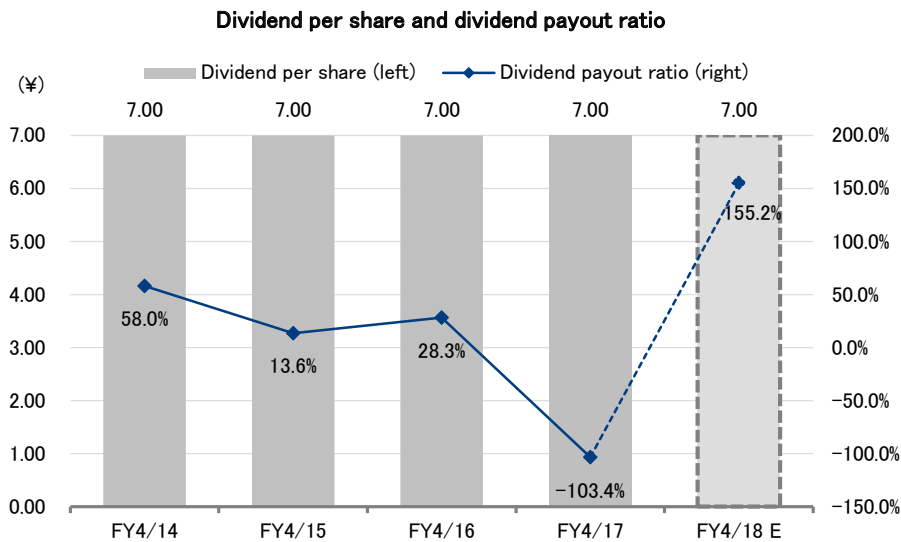


Source: Prepared by FISCO from the Company’s results briefing materials

Shareholder return policy

Planning to pay a ¥7 dividend at the end of FY4/18 too unrelated to the profit level

The Company returns profits to shareholders through paying dividends. Its basic dividend policy is to prioritize continuously returning profits to shareholders while also supplementing internal reserves and investing for business expansion. It recorded a net loss in FY4/17, but even so it maintained an annual dividend per share of ¥7. The forecast annual dividend per share for FY4/18 is the same, of ¥7, for a dividend payout ratio of 155.2%, regardless of the amount of profit.



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

Information security measures

FreeBit provides cloud services and a variety of other IT-related services and obviously possesses robust information security. The management division system's information security measures consist of various preventive measures for information infrastructure facilities, such as computer virus detection, construction of a virus-removal firewall, and use of anti-virus software.



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