COMPANY RESEARCH AND ANALYSIS REPORT

AOI TYO Holdings Inc.

3975

Tokyo Stock Exchange First Section

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Index

Summary

In FY12/20, results ultimately outperformed revised forecasts amid rapid recovery in 4Q, and despite substantial setbacks due to the coronavirus. Meanwhile, the Company engaged in business and organizational restructuring to address changes in the business environment

1. Company overview and history since establishment

AOI TYO Holdings Inc. <3975> is a joint holding company established in January 2017 through the management integration of AOI Pro. Inc. and TYO Inc. The AOI TYO Group mainly plans and creates TV commercials and also focuses on its Solutions Business that includes direct business with advertisers and video content marketing. It holds a top share in TV commercial production through the management integration of the two industry-leading companies.

The decision to proceed with management integration took into account the lack of prospects for major growth in conventional TV commercial production as well as likely expansion of business scope related to advertising, including methodology and structural changes. It comes against a backdrop of diversification of media (primarily through the internet) and devices (smartphones, tablets, and others) and major shifts in the industry landscape with advances in technology, such as communications speed, data analysis, VR*1, and AR*2. This integration aims to realize economies of scale, create synergies and accelerate the pace of new value creation and business expansion through consolidation and effective utilization of business resources.

*1 VR (virtual reality) refers to the technologies and methods to realize various types of experiences, including in virtual worlds, portraying something like the real world but one that goes beyond time and space.
*2 AR (augmented reality) refers to the technologies and methods to realize an augmented reality by adding some other content to the information that people can perceive in the real world.

2. FY12/20 results overview

In FY12/20 results, net sales decreased 21.7% YoY to ¥51,087mn and operating loss was ¥727mn (compared to operating income of ¥2,118mn in the previous fiscal year). The Company's earnings results turned negative amid a substantial decrease in revenue attributable to the impact of the coronavirus. This is particularly a result of sales revenues having declined significantly in the Video Advertising Business largely due to a downturn in advertising demand amid cancellations and postponements of filming services associated with Japan's first state of emergency declaration. Meanwhile, the Advertisement-Related Business also encountered a substantial drop in sales revenues largely due to cancellations and postponements of various events. However, the Company ultimately managed to achieve results at levels outperforming its revised forecasts given that 4Q sales of its Video Advertising Business and Solutions Business recovered to levels nearly on par with those of the same period of the previous fiscal year. In profits, the Company shifted to an operating loss with the decline in sales having weighed on profits. Looking only at 2H FY 12/20, however, it achieved positive operating income results due to recovering net sales and cost reductions.

3. Direction going forward

In March 2019, the Company formulated its medium-term management policies and it has progressed changing to management that emphasizes "quality over quantity." However, due to the impact of the coronavirus, major changes to lifestyles have caused the speed of environmental changes to further accelerate and responding to advertisers' new needs has become an urgent task. Therefore, the Company has announced a new five-year medium-term management plan to accelerate its medium-term management policies (announced on August 24, 2020). Nevertheless, there has been no major change in direction going forward. Under the theme of "Group-wide update of production functions," the aim is to implement a major reorganization of the Group to respond to an era of reforms. The targets for the plan's final fiscal year (FY12/25) are consolidated net sales of ¥68bn, consolidated operating income of ¥4.4bn, EBITDA of ¥5.7bn, and ROE of at least 10%. In particular, the results targets are premised on emphasizing an improvement in profitability, including through cost reductions. Meanwhile, the reorganization has involved transitioning to a two-business structure consisting of the Content Production Business and the Communication Design Business since FY12/21.

4. FY12/21 forecasts

For the FY12/21 results forecasts, net sales are expected to increase 3.7% YoY to ¥53,000mn and operating income to ¥900mn (compared to an operating loss of ¥727mn in the previous fiscal year) as the Company anticipates a return to positive earnings amid an increase in sales and substantially higher profits. Under the assumption that Japan's advertising market is bound to mount a gradual recovery, the prospect of growth in net sales seems likely amid a scenario that has the Communication Design Business achieving recovery in the wake of effects of the coronavirus in FY12/20 while serving new advertiser needs, and despite the prospect of net sales remaining nearly unchanged in the Content Production Business. In profits as well, the Company is poised to generate substantially higher earnings due to higher sales and ongoing cost reductions.

Key Points

- In FY12/20, the Company posted a substantial downturn in sales and an operating loss due to the coronavirus. However, results ultimately outperformed revised forecasts amid rapid recovery in 4Q
- The newly announced five-year medium-term management plan has set the theme of "Group-wide update of production functions" and implemented a major reorganization of the Group to respond to an era of reforms
- The targets for the plan's final fiscal year (FY12/25) are consolidated net sales of ¥68bn and consolidated operating income of ¥4.4bn, and the Company will work to improve profitability through cost reductions
- In FY12/21, a return to positive earnings amid a substantial increase in profits seems likely due to factors that include recovery in the wake of FY12/20 results, the Company serving new advertiser needs, and ongoing cost reductions

Company profile

Joint holding company established for the integration of AOI Pro. and TYO. Holds a top industry share for TV commercial production

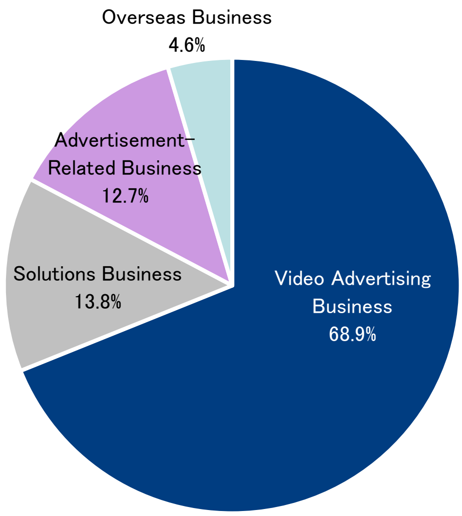
1. Business overview

AOI TYO Holdings is a joint holding company that owns AOI Pro. and TYO. The AOI TYO Group plans and creates TV commercials and is engaged in its Solutions Business that includes direct business with advertisers and video content marketing. It was founded in January 2017 through management integration of two industry-leading companies and holds a top share in TV commercial production.

The AOI TYO Group consists of a single Advertising Business segment and four sub-segments (Video Advertising, Solutions, Advertisement-Related, Overseas). While the mainstay Video Advertising Business generates about 70% of overall sales, the Company is focusing on the Solutions Business to meet new advertising needs as a growth driver. In FY12/21, the Company began transitioning to a two-business structure consisting of the Content Production Business and the Communication Design Business, in alignment with its reorganization (more details later in this report).

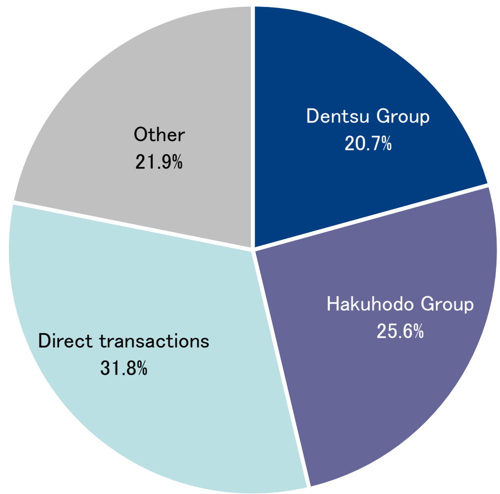
Sales mix by customer was well balanced with 20.7% to the Dentsu Group <4324>, 25.6% to the Hakuhodo Group (Hakuhodo DY Holdings Inc.) <2433>, 31.8% in direct transactions, and 21.9% to others. Additionally, sales composition by media type is TV commercial production at 56.8%, entertainment content at 4.5%, digital content at 23.0%, overseas at 4.1%, and other at 11.6%. “Digital content” is growing rapidly along with expansion in online video advertising demand as a trend.

Sales composition by business (FY12/20 result)



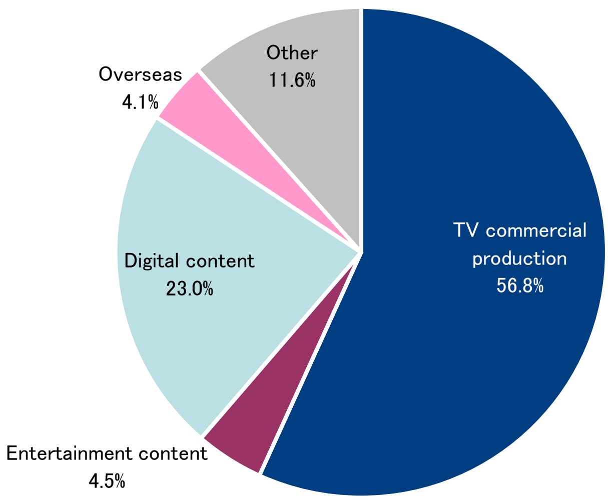
Source: Prepared by FISCO from the Company’s results briefing materials

Sales composition ratios by customer (FY12/20 result)



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

Sales composition ratios by medium (FY12/20 result)



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

Below, we review each of these business areas.

(1) Video Advertising Business

The Company plans and produces TV commercials, online video and other advertising video. TV commercials were the main business for AOI Pro. and TYO, and integration of these two industry-leading companies established a top market share. Both companies produce numerous excellent works amid continuation of a healthy orders environment. While the Company faces concerns about profitability decline because of changes in advertising media related to the growing internet presence and the printless shift as well as the need for income structure reforms and better work efficiency, it aims to establish a dominant position in high-quality video advertising, its strength, including in the expanding online video market.

(2) Solutions Business

This business provides measures for problem-solving for customers. Its results currently roughly equate to the combined results of the TYO Offering Management Business Unit*1 and AOI Pro.'s subsidiary Quark tokyo Inc.*2 (including its subsidiary Mediator Inc.*3).

*1 Supplies one-stop solutions mainly through multifaceted media activities via direct business with advertisers.
*2 Provides services that range from marketing strategy formulation mainly for videos to all PDCA solutions required by communications in the digital era.
*3 A joint venture between Quark tokyo and Cyber Communications Inc. of the Dentsu Group (established August 20, 2019)..

(3) Advertisement-Related Business

This business includes planning and production of movies, TV dramas and events, as well as production of digital content, promotional content and music videos. The Company's strategy is to enclose the market by building up its track record by entering areas that have a strong affinity with the mainstay business and bolstering peripheral solutions (promotions and content).

(4) Overseas Business

The Overseas Business operates sites mainly in Southeast Asia (Thailand, Vietnam, Singapore, Indonesia, Malaysia, and India), engaging in business with both Japanese-affiliates and local companies. This business includes video production orders received from overseas. These are the main areas that both AOI Pro. and TYO have been actively engaged in.

2. History

(1) AOI Pro.

AOI Pro. goes back to Aoi Advertising Promotion Inc., which was established in 1963 to produce TV commercials in Tokyo's Minato Ward. It solidified a business base as a video production company focused on TV commercials. In 1990, it listed shares on JASDAQ, taking the lead in this industry, with the aim of making further advances and strengthening social credibility.

It subsequently created numerous videos that attracted substantial interest, fueling healthy growth and listed on the Second Section of the Tokyo Stock Exchange in 1998 and on the First Section in 2000. It established a firm position as one of the major TV commercial production companies.

In September 2011, meanwhile, it launched an overseas site to handle TV commercial production in Indonesia. In October 2014, it added nakamino Co., Ltd.*, which specializes in measurement and operation of online video platform effects, to the group (equity-method affiliate) through a capital alliance with the aim of a full-fledged ramp-up of video content marketing, a new growth area. These initiatives gave it an edge versus peers in building operations to address diversifying media, growing demand for online videos and other digital content, and entry by Japanese companies into the fast-growing Asian region.

* It turned this entity into a consolidated subsidiary at the end of December 2015 through an injection of additional capital and changed the company name to Quark tokyo Inc. in April 2016.

(2) TYO

TYO was established as a TV commercial production company in April 1982 in Roppongi, Minato Ward, Tokyo. It was established after other major commercial production companies had been formed. Five commercial creators, including Hiroaki Yoshida the honorary chairman of AOI TYO Holdings, established the company with the dream of "Creating an Ideal Company of Creators, by Creators, for Creators."

The company listed on JASDAQ in 2002. It expanded business by leveraging its creative capabilities in the production of numerous TV commercials that left an impression with consumers, notably one promoting travel to Kyoto for Central Japan Railway Company (JR Central) <9022>. Upon the market being changed to the Second Section of the Tokyo Stock Exchange in October 2013, the Company's listing was reassigned to the First Section in January 2014.

TYO has been involved in various types of content production, including TV commercials, online videos, digital content and events. Its strength is providing optimal, one-stop solutions for advertisers' advertising promotions and promotional activities. It led the industry with a sales structure and accumulation of knowledge in dealing directly with advertisers* and has focused on building long-term relationships with advertisers, expanding project sizes and capturing sales promotion expenses. Furthermore, it has been actively engaged in overseas expansion.

* Since starting direct business with advertisers in July 2003, the TYO Offering Management Business Unit has currently taken charge of the entire group's direct business with advertisers.

(3) Background to the management integration (January 2017)

In the background to the management integration is the diversification of media and devices (such as smartphones and tablets) focused on the internet, in addition to dramatic changes to the advertising industry environment, including communications speed and data analysis, and the progress being made in technological innovations, such as VR and AR. In this environment, major growth in conventional TV commercial production, which had been the Company's mainstay, is unlikely, but advertising-related business areas is expected to expand, with accompanying changes to their methods and structures.

Based on this sort of awareness of the business environment, the companies judged that integration was necessary to grow in the medium to long term to expand market share, strengthen negotiation power, and maintain robust capital strength. They also wanted to build a competitive and advanced business model by newly forming a group to lead the industry and concentrating and effectively utilizing management resources.

Financial highlights

In FY12/20, the Company recorded an operating loss amid a significant decrease in sales and profits. However, results ultimately outperformed revised forecasts amid rapid recovery in 4Q

1. FY12/20 results

In FY12/20 results, net sales decreased 21.7% YoY to ¥51,087mn, operating loss was ¥727mn (operating income of ¥2,118mn in the same period in the previous fiscal year), ordinary loss was ¥1,149mn (ordinary income of ¥1,763mn), and loss attributable to owners of parent was ¥2,552mn (loss attributable to owners of parent of ¥1,280mn). The Company incurred an operating loss amid a substantial decrease in sales due to the coronavirus. However, net sales and operating loss results ultimately outperformed the revised forecasts announced on August 24, 2020, amid rapid recovery in 4Q.

Net sales decreased in each business segment due to the coronavirus. This is particularly a result of sales revenues having declined significantly in the Video Advertising Business largely due to a downturn in advertising demand amid cancellations and postponements of filming services associated with Japan's first state of emergency declaration. Meanwhile, the Advertisement-Related Business also encountered a substantial drop in sales revenues largely due to cancellations and postponements of various events. However, the Company ultimately managed to achieve results at levels outperforming its revised forecasts given that 4Q sales of its Video Advertising Business and Solutions Business recovered to levels nearly on par with those of the same period of the previous fiscal year. Orders received also increased in 4Q, upon having shifted to an upward trajectory beginning in 3Q subsequent to the government's lifting of the state of emergency declaration. Accordingly, although not at levels achieved as of the end of FY12/19, backlog of orders is at the adequate level of ¥13,306mn (down 8.9% YoY) as of the end of FY12/20.

Net sales by customer declined for every channel, and the decreases were particularly large for major advertising agencies like the Dentsu Group and Hakuhodo Group.

In terms of profits, the Company shifted to an operating loss with a decline in sales having weighed on profits, despite efforts to cut costs including travel expenses and entertainment expenses with the aim of achieving the medium-term management plan target of reducing costs by as much as ¥2.0bn ahead of schedule. Based on its performance solely in the 2H FY12/20, however, the Company achieved positive operating income results along with recovering net sales. On the other hand, the Company's large extent of loss attributable to owners of parent is because of factors that include its posting of extraordinary losses such as ¥300mn impairment of goodwill due to the coronavirus and ¥86mn in loss on valuation of investment securities, in addition to ¥946mn in business restructuring expenses largely associated with office consolidations and reductions amid a substantial reduction in the number of consolidated subsidiaries and efforts to encourage employees to work from home, under the medium-term management plan.

Regarding financial condition, total assets decreased 8.8% compared to the end of the previous fiscal period to ¥48,682mn, mainly due to the decline in notes and accounts receivable - trade following the reduction in sales. Meanwhile, shareholders' equity decreased 13.1% to ¥19,925mn because of the recording of loss attributable to owners of parent, and therefore the equity ratio fell to 40.9% (43.0% at the end of previous fiscal period). Conversely, this is in part because cash and deposits increased 18.7% to ¥10,813mn, and also because the Company has achieved a current ratio at the high level of 223.9% and has established a commitment line (a borrowing framework) of ¥12bn with multiple financial institutions, so there are seemingly no concerns regarding liquidity or otherwise from a financial standpoint.

Financial highlights

FY12/20 results overview

(¥mn)

	FY12/19		FY12/20			
	Results	vs. net sales	Results	vs. net sales	Change	YoY
Net sales	65,229		51,087		-14,142	-21.7%
Video Advertising Business	43,860	67.2%	35,194	68.9%	-8,666	-19.8%
Solutions Business	8,145	12.5%	7,074	13.8%	-1,071	-13.1%
Advertisement-Related Business	9,846	15.1%	6,488	12.7%	-3,358	-34.1%
Overseas Business	3,378	5.2%	2,331	4.6%	-1,047	-31.0%
Cost of sales	53,514	82.0%	43,867	85.9%	-9,647	-18.0%
Selling, general and administrative expenses	9,596	14.7%	7,947	15.6%	-1,649	-17.2%
Operating income	2,118	3.2%	-727	-1.4%	-2,845	-
Ordinary income	1,763	2.7%	-1,149	-2.2%	-2,912	-
Loss attributable to owners of parent	-1,280	-2.0%	-2,552	-5.0%	-1,272	-
EBITDA	3,606		422		-3,184	-88.3%
Order backlog	14,606		13,306		-1,300	-8.9%
Sales ratio by customer						
Dentsu Group	12,941	19.8%	10,583	20.7%	-2,358	-18.2%
Hakuhodo Group	18,088	27.7%	13,074	25.6%	-5,014	-27.7%
Direct transactions	21,072	32.3%	16,259	31.8%	-4,813	-22.8%
Other	13,125	20.1%	11,169	21.9%	-1,956	-14.9%

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

Financial position as of the end of FY12/20

(¥mn)

	As of the end of FY12/19	As of the end of FY12/20	YoY	
			Change	Change rate
Current assets	36,003	33,014	-2,988	-8.3%
Cash and deposits	9,111	10,813	1,702	18.7%
Notes and accounts receivable - trade	16,873	13,222	-3,651	-21.6%
Work in process	4,510	4,331	-178	-4.0%
Non-current assets	17,348	15,667	-1,680	-9.7%
Property, plant and equipment	7,084	6,257	-827	-11.7%
Intangible assets	4,275	3,601	-673	-15.8%
Investments and other assets	5,988	5,808	-179	-3.0%
Total assets	53,352	48,682	-4,669	-8.8%
Current liabilities	18,343	14,743	-3,599	-19.6%
Accounts payable - trade	8,697	7,144	-1,552	-17.9%
Short-term loans payable	6,273	4,374	-1,899	-30.3%
Advances received	899	720	-179	-19.9%
Non-current liabilities	11,645	13,707	2,062	17.7%
Long-term loans payable	6,672	8,774	2,102	31.5%
Long-term deposits received	3,501	3,501	-	-
Total liabilities	29,988	28,451	-1,537	-5.1%
Net assets	23,363	20,231	-3,132	-13.4%
Shareholders' equity	22,935	19,925	-3,009	-13.1%
Equity ratio	43.0%	40.9%		
Current ratio	196.3%	223.9%		
D/E ratio	0.56x	0.66x		

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

2. Segment performance and activity results

(1) Video Advertising Business

Net sales fell significantly, declining 19.8% YoY to ¥35,194mn. Following the declaration of a state of emergency (April 7 to May 25) due to the coronavirus pandemic, sales were affected by various measures, mainly due to filming almost entirely stopping and requests to postpone TV commercial production. In 4Q, the Company achieved recovery on a quarterly basis back to nearly the same level as that of the same quarter in the previous fiscal year. This is attributable to factors that include resumption of economic activity along with the Company's flexible approach in terms of restarting business operations upon having created proprietary guidelines* and its introducing of video production methods with respect to remote work. Meanwhile, it is worth noting the view that structural change is evident in that the Video Advertising Business has come to account for a higher proportion of the segment's sales mix amid a scenario where sales of digital content including online videos decreased little relative to those of television commercials. As for profits as well, in 2H FY 12/20, the effective profit margin improved greatly to 34.5% (compared to 32.1% in the same period of the previous fiscal year) mainly due to a recovery in sales and a reduction in projects with a low profit margin, despite a scenario in 1H FY 12/20 where the effective profit margin decreased to 31.4% (33.5% in the same period of the previous fiscal year). The decrease is largely attributable to actual-costs claims stemming from cancellations and postponements of projects due to the coronavirus, in addition to external factors involving a decline in highly profitable print sales.

* Refers to concluding an advisory contract with a medical coordination company and creating proprietary guidelines for production operations. The aim is to thoroughly implement measures to prevent the infection from the spread of the coronavirus, such as taking a team when filming to manage hygiene measures, including medical practitioners, and conducting health checks and regularly implementing and confirming disinfection and ventilation.

(2) Solutions Business

Net sales decreased 13.1% YoY to ¥7,074mn, but greatly outperformed revised forecasts. The TYO Offering Management Business Unit achieved significant recovery in 4Q amid heightening demand from successful online companies and other such enterprises. Meanwhile, 4Q net sales of Quark tokyo (and Mediator) increased YoY as a result of the company having extensively cultivated business dealings with online-related companies and other such enterprises serving the youth demographic, and despite adverse effects from budget cuts among advertisers.

(3) Advertisement-Related Business

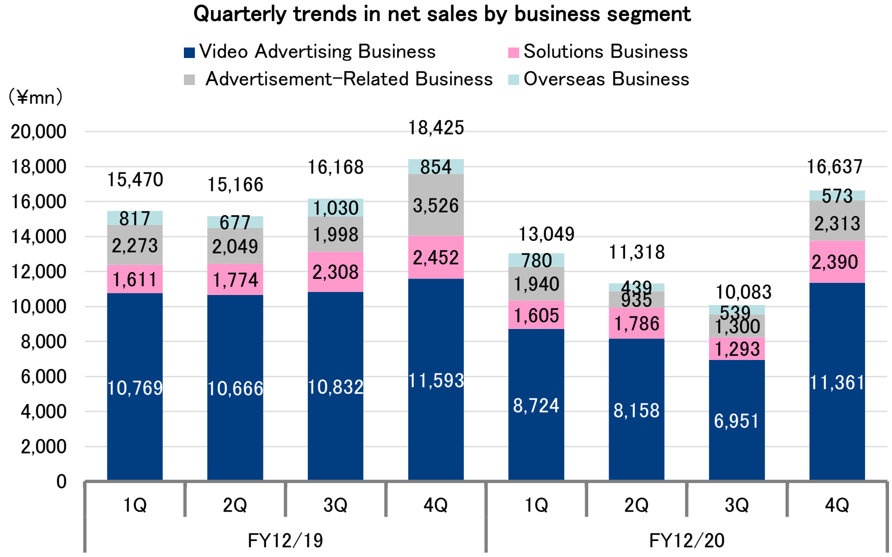
Net sales decreased 34.1% YoY to ¥6,488mn, but were largely on par with revised forecasts despite the significant downturn. Whereas the decline was caused by cancellations and postponements of various events due to the coronavirus, the Advertisement-Related Business mounted a recovery in 4Q due to expansion of the customer base amid emergence of a new mainstream format involving hybrid events combining online and live formats.

(4) Overseas Business

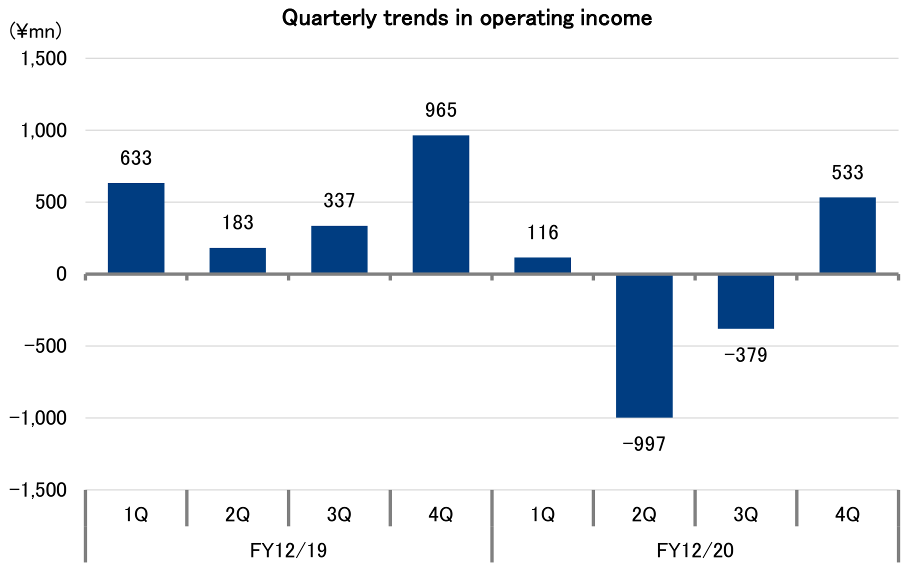
Net sales significantly decreased 31.0% YoY to ¥2,331mn, but were on par with revised forecasts. However, the coronavirus continues to affect results given that the pandemic continues in certain areas of Southeast Asia.

3. Quarterly performance trends

Looking at performance trends on a quarterly basis, net sales mounted a rapid recovery during 4Q despite having fallen significantly over 2Q FY12/20 and 3Q due to the coronavirus. The two segments of the Video Advertising Business and Solutions Business in particular returned to levels nearly on par with those of the same period of the previous fiscal year. In terms of profits as well, the Company recorded operating losses in 2Q and 3Q. However, it marked progress in shifting to a profit-generating earnings structure by achieving substantially better profitability in 4Q due to recovery in net sales and effectiveness of cost-cutting.



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



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

4. FY12/20 performance summary

Summarizing FY12/20, coronavirus has dealt a severe blow to the Company's operating results. But if looking at the situation from a different perspective there are positive signs looking ahead. For instance, the Company is capable of taking action in terms of rapidly implementing business and organizational reforms and transforming its earnings structure, particularly when it comes to addressing structural changes in the advertising market (changing advertiser needs, momentum toward new business channels, etc.). Moreover, the Company created proprietary guidelines amid unanticipated circumstances posed by the coronavirus and otherwise managed to resume operations while implementing thorough measures to prevent transmission of the virus. This has culminated in recovery of its financial results beginning in 4Q, which seemingly suggests that the Company deserves credit for its high capacity to address risk.

Main activity results

Increasing volume of direct business with successful online-related companies and other such entities

The Company has landed business directly serving flea market app operator Mercari <4385> involving its television commercials, out-of-home (OOH) media, web services and PR. Mercari selected the AOI TYO Group's services proposal over those of multiple competitors. Meanwhile, the AOI TYO Group directly takes charge of television commercials for Amazon Prime Video offered by Amazon.com, Inc <AMZN>. The company has furthermore gained orders involving campaigns entailing promotions beyond video. This has included promotions for LOTTE (including Painomi × Uber Eats tie-ins and various events) as well as achieving results in online video, events, graphics and social media for BMW. The Company deserves credit for instances where it has addressed changing advertiser needs amid a scenario of new business channels.

Direction going forward

Has announced a new five-year medium-term management plan based on the theme of "Group-wide update of production functions" and measures include business and organizational structural reforms

1. Medium-term management plan

To respond to rapid environmental changes, the Company formulated medium-term management policies in March 2019. Setting its basic policy to "be a powerful corporate group capable of responding to any era," it has changed to management that emphasizes "quality over quantity." In particular, in addition to further deepening its production of high-quality video and movies for branding, which is one of the Company's strengths, it has indicated a direction of strengthening peripheral solutions and widening the business scope. But since entering 2020, results have been declining significantly due to the impact of the coronavirus, while major changes to ways of living are causing the speed of environmental changes to further accelerate and responding to advertisers' new needs has become an urgent task. Based on this situation, to accelerate the medium-term management policies, the Company announced a new five-year medium-term management plan on August 24, 2020. However, there will be no major change of direction going forward. The key points are to further accelerate the realization of the medium-term management policies by setting "Group-wide update of production functions" as a theme and implementing a major reorganization of the Group to respond to an age of reforms.

2. Environmental awareness that forms the assumptions

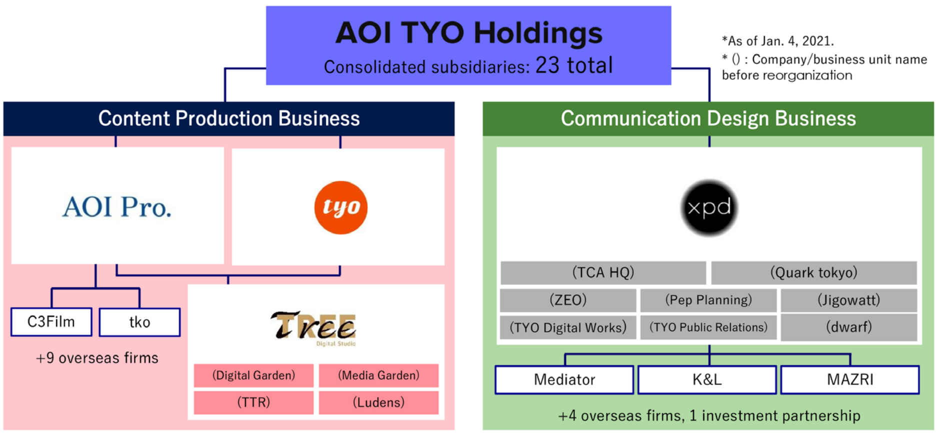
It is forecast that the TV commercial market will shrink at a maximum pace of around 2% a year, but that the online video advertising market will grow by around 20% a year due to the acceleration of the shift to digital. In this sort of environment, brand videos with high unit prices, which are one of the Company's strengths, will continue to grow, but this growth will be limited and it seems that low- to medium-priced videos will grow significantly. On the other hand, when it comes to trends among advertisers, the Company is encountering growing needs with respect to advertisers seeking to directly order only creative functions deemed necessary as they progressively shift to developing strategic advertising planning functions in-house. Meanwhile, an increasing number of SMEs and venture companies with annual advertising budgets ranging from ¥100mn to ¥1bn require a structure that makes it possible for them to provide one-stop services extending from marketing-orientated communication design through to planning, production, and management. Accordingly, it is apparent that there are growing needs in either case for business dealings directly with production companies like AOI TYO Holdings.

3. Priority measures

(1) Business and organizational structural reforms

The Company's business structure has focused on advertisement video production so far, but has changed to a two-business structure: The Content Production Business, responsible for the conventional advertising video production centered on consignment work from advertising agencies; and, the Communication Design Business, responsible for work from communication design through to execution centered on direct transactions with advertisers. Also, it reduced the number of consolidated subsidiaries from 33 companies to 23 companies.

Group structure



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

(2) Overview of respective business segments and direction going forward

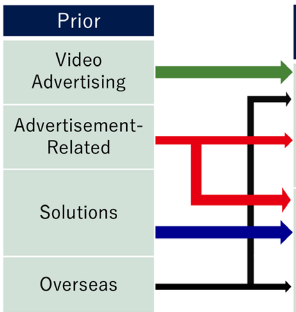
1) Content Production Business

The Content Production Business mainly encompasses entities such as AOI Pro. and TYO, and engages in an extensive range of content production including advertisement video production in Japan and abroad, post-production business, and xR content production. This business consolidates the work of the production subsidiaries in the former Video Advertising Business and the former Overseas Business and part of the work of the former Advertisement-Related Business. Going forward, the Content Production Business is set to pursue high quality and productivity by leveraging its strengths in the form of its industry-leading market share and expertise amassed thus far. It will also set its sights on expanding its coverage in the digital video market's low- to medium-priced segment, which is poised for growth. It is also focusing on content planning and production harnessing diversified post production (including sound editing and computer graphics work) as well as virtual reality, augmented reality, and other such immersive technologies.

2) Communication Design Business

In the advertising and marketing solutions domain, the Communication Design Business provides omnichannel execution particularly involving video, digital solutions, PR, events, and spatial design. The business will consolidate the operations of the former Solutions Business, Advertisement-Related Business, and Overseas Business, excluding production subsidiaries. With the business segment centering on new subsidiary xpd Inc., it will maintain a future policy aiming to strengthen the customer base while also providing higher value-added integrated marketing and communication services and expanding its range of services with respect to executing omnichannel promotions.

New business segment classifications



New	Overview	Major Group Companies
Content Production	Production of various video content for domestic and overseas advertising, post-production business and xR content production	AOI Pro. TYO TREE Digital Studio
Communication Design	Providing omnidirectional execution from video, to digital solutions, PR, events, spatial design, and more in the advertising / marketing solutions domain	xpd

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

(3) Deeping and strengthening Group management and reducing costs

Based on the newly formulated human resources management policy, the Company is strengthening recruitment of new graduates (including unifying selection management), reviewing the evaluation and remuneration systems and working on measures to bring together all the human resources in the Group, including by constructing a human resource development environment. It is also aiming for cost reductions of a maximum amount of ¥2bn, such as by consolidating offices, encouraging remote work, and improving productivity through digital transformation.

4. Key performance indicators (KPI) and results targets

The Company's targets for the medium-term management plan's final fiscal year (FY12/25) are consolidated net sales of ¥68bn, consolidated operating income of ¥4.4bn, EBITDA of ¥5.7bn, and ROE of at least 10%. However, results in FY12/20 are greatly declined temporarily due to the impact of the coronavirus, but it is still aiming for sustainable growth from FY12/21 onwards. In particular, the targets are premised on emphasizing an improvement to profitability through cost reductions. Also, breaking down the net sales target of ¥68bn, the plan is to increase sales from the Content Production Business to ¥47bn (up ¥7.7bn from the FY12/20) and from the Communication Design Business to ¥21bn (up ¥9.1bn). Moreover, its policy is to work to improve employee engagement and to contribute to the SDGs.

Business performance outlook

In FY12/21, the Company is poised for a return to profitability amid the prospect of substantially higher earnings. Meanwhile, it is addressing changes in advertiser needs while also strengthening its earnings structure through ongoing efforts to cut costs

1. FY12/21 forecasts

For the FY12/21 results forecasts, net sales are expected to increase 3.7% YoY to ¥53,000mn, operating income of ¥900mn (compared to an operating loss of ¥727mn in the previous fiscal year), ordinary income of ¥800mn (ordinary loss of ¥1,149mn), and profit attributable to owners of parent of ¥400mn (loss attributable to owners of parent of ¥2,552mn). Accordingly, the Company is likely to return to profitability due to the prospect of increased sales and substantially higher earnings.

Under the assumption that Japan's advertising market is bound to mount a gradual recovery, the prospect of growth in net sales seems likely amid a scenario where sales remain nearly unchanged in the Content Production Business while the Communication Design Business serves advertiser needs in addition to recovering in the wake of the effects of the coronavirus in FY12/20.

In profits as well, the Company is poised to achieve substantially higher earnings resulting from higher sales and a continuation of cost-cutting efforts that began in FY12/20. In terms of costs, the Company has been lowering office-related expenses (land rent, consumables expense, utilities expense, etc.) by reducing the number of its consolidated subsidiaries and cutting back on offices by encouraging employees to work from home. It is furthermore poised to incur lower expenses, particularly in terms of decreasing personnel expenses, which are closely linked to financial results, ongoing efforts to curb entertainment expenses, travel expenses and other outlays that were reduced in FY12/20, and reducing outsourcing expenses and commission expenses.

FY12/21 forecasts

(¥mn)

	FY12/20		FY12/21			
	Results	vs. net sales	Forecasts	vs. net sales	Change	YoY
Net sales	51,087		53,000		1,913	3.7%
Content Production Business	11,828	23.2%	14,000	26.4%	2,172	18.4%
Communication Design Business	39,258	76.8%	39,000	73.6%	-258	-0.7%
Operating income	-727	-1.4%	900	1.7%	1,627	-
Ordinary income	-1,149	-2.2%	800	1.5%	1,949	-
Loss attributable to owners of parent	-2,552	-5.0%	400	0.8%	2,952	-

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

2. Business performance outlook of each business segment and action plans

(1) Content Production Business

Net sales are forecast to decrease 0.7% to ¥39,000mn. Although the Content Production Business is poised to mount a gradual recovery in the advertising market, its results are expected to remain largely unchanged, partially as a result of shifting some production employees to the Communication Design Business. The segment's action plan involves: 1) consistently securing orders from Dentsu and Hakuhodo, 2) expanding the customer base (this includes the ADK Group, foreign advertising companies, online advertising companies, and consulting companies; and involves gaining direct orders from platform providers), and 3) setting the stage for the full-scale launch of low- to medium-priced video production (from 2022 onward).

(2) Communication Design Business

Net sales are forecast to increase 18.4% to ¥14,000mn, which constitutes substantial growth as a result of the segment addressing changing advertiser needs. The action plan for the segment lists efforts that include: 1) engaging in initiatives to strengthen coordination among departments (in areas that include the managerial framework, employee evaluations, and compensation plans), and 2) enhancing functions that are insufficient (coordinating with PR companies and planning companies and accepting secondments of personnel, while also hiring new strategic planners).

3. Opinion of FISCO's analyst

At FISCO, we deem the Company to be sufficiently likely to achieve its results forecasts due to various factors such as the Company being off to a good start amid rapid recovery in 4Q FY12/20, completing measures to address the coronavirus, which consequently is not now affecting services such as filming and editing, and gradual recovery is anticipated in the overall advertising market. Although the Company endured a temporary setback in financial results in FY12/20 due to the coronavirus, we deem that structural changes offer substantial opportunities over the medium- to long-term. Going forward, the Company is bound to encounter challenges that entail swiftly addressing changes brought about by the coronavirus and positively making the best of the situation. In that sense, we expect the Company's return to a growth trajectory, given that the situation is perfect timing for the Company to take on its current business and organizational structural reforms.

In the medium-term management plan as well, targets are at levels that are fully achievable through thorough cost reductions. Rather, focus should be on how the Company can improve by adding value. In particular, starting from the axis of the new strategy, or in other words, the provision of a full line of services through direct transactions with SMEs and venture companies, we shall be closely following how the Company will increase its competitive advantage through the provision of new value, including the planning and production of content that utilizes the latest digital technologies and the provision of integrated marketing planning, and also what effects this will have on results (particularly on profitability).

Shareholder returns

Aiming for a consolidated dividend payout ratio of at least 30%

Going forward, the Company's basic dividend policy is to continue with a "consolidated dividend payout ratio of at least 30%." Based on this and the viewpoint of continuing to stably pay dividends, it has indicated that its policy is to return profits to shareholders appropriately according to results.

In FY12/20, the Company once again paid a period-end dividend of ¥12.0 per share, which is the same amount as FY12/19, despite having recorded a loss attributable to owners of parent. Whereas it did not pay out an interim dividend for FY12/19, it paid the period-end dividend from the viewpoint of maintaining stable dividend payments to the greatest possible extent. The Company plans to pay a period-end dividend of ¥12.0 per share again in FY12/21.

Also, with the aim of promoting medium- to long-term shareholding, the Company has introduced a shareholder benefits program. Specifically, it plans to provide shareholders listed or recorded in the shareholders' register on June 30 of each year that have held at least 5 units (500 shares) of the Company's shares continuously for at least 1 year with gifts depending on the number of shares held, including original QUO cards and perks from its original benefits program catalog.

Disclaimer

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