

24-Apr-13

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

FISCO Ltd. Analyst
Shinobu Kasaya

■ Likely to exceed forecasts for FY6/13, reflecting strong sales of security equipment

Ai Holdings corp. was established in April 2007 through the merger of Dodwell BMS Ltd., which primarily sold security equipment systems and systems for issuing IC cards, and Graphtec Corp., which engaged mainly in the manufacture and sale of measuring equipment and peripheral computer equipment. Subsequently, Ai Holdings bought Shiomi Sekkei (Design) Co., Ltd. and made it a subsidiary, which is now called Ai Sekkei (Design) Co., Ltd. Through this subsidiary, Ai Holdings is advancing into the business of structural design with special expertise in earthquake-resistance measurement and design.

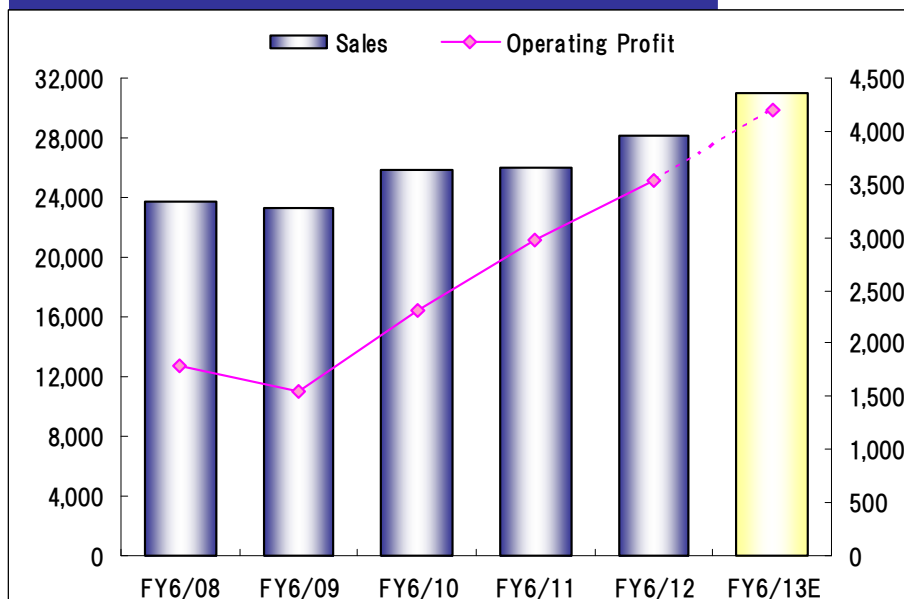
In the first half of the fiscal year through June 2013, i.e., in H1 FY6/13, Ai Holdings recorded notable growth, with consolidated sales of ¥16,079mn, up 15.1% year-on-year (y-o-y), and consolidated operating profit of ¥2,326mn, up 36.7% y-o-y. These figures substantially exceeded the company's forecasts, of ¥15,000mn and ¥1,900mn, respectively. Sales of security equipment were brisk, due to an increase in the number of units sold to condominiums and to greater sales to companies through sales agent Fuji Xerox Co., Ltd. Ai Holdings' US subsidiary, Silhouette America Inc., greatly increased its sales of information equipment for craft and hobby use in North America. Finally, Ai Sekkei Co. received more work for measuring the earthquake-resistance of buildings.

For FY6/13, the management of Ai Holdings maintained its original forecasts, even though the company achieved 52% of projected sales and 55% of projected operating profit in H1 FY6/13, and the company normally achieves more of its sales and profit in H2 than in H1. Thus, it seems that sales and profits should surpass management's forecasts for the full fiscal year.

■ Check Points

- Expanding growth businesses through aggressive M&A
- Sales of compact cutting machines for craft and hobby use are growing rapidly in the US and Europe
- With greater profits, the company is likely to increase its dividend

Consolidated Sales and Operating Profit (¥mn),
FY6/08-FY6/13E



■ Company Outline

Business expansion achieved through aggressive M&A in growth areas

(1) Company History

In December 2006, Dodwell BMS and Graphtec agreed to establish a holding company, Ai Holdings, through a share swap. Graphtec was a global company in the niche market for such peripheral computer equipment as plotters and scanners and in the market for measuring equipment. However, its growth peaked in the early 1990' s, and thereafter, its business began to deteriorate. In contrast, by the mid-2000' s, Dodwell BMS served about 50,000 corporate customers through a network covering Japan. To improve its business, Graphtec, which had been curtailing its operations in Japan, entered a business agreement with Dodwell BMS in May 2005. In January 2006, Dodwell BMS underwrote a third-party allocation of new shares by Graphtec, becoming Graphtec' s top shareholder. In April 2007, Dodwell BMS and Graphtec established Ai Holdings and listed its shares on the First Section of the Tokyo Stock Exchange. In January 2009, Ai Holdings bought Shiomi Sekkei Co., Ltd., which is now Ai Sekkei Co., Ltd., and entered the business of building design. In September 2009, Ai Holdings established subsidiary Silhouette America Inc., through which, it entered the business of cutting machines for craft and hobby use in North America and Europe.

History of Ai Holdings

Apr-07	Established through the merger of Dodwell BMS and Graphtec. Listed on the First Section of the Tokyo Stock Exchange.
Jul-07	Purchased USTAGE, making it a subsidiary.
Jul-08	Purchased Neuron Co., making it a subsidiary.
Jan-09	Purchased Shiomi Sekkei Co., making it a subsidiary.
Feb-09	Shiomi Sekkei Co. began structural design, the appraisal of buildings for earthquake-resistance, and the strengthening of buildings against earthquake motion.
Jul-09	Established subsidiary Ai Engineering Co., Ltd.
Sep-09	Established Silhouette America Inc.
Jul-10	Shiomi Sekkei Co. changed its name to Ai Sekkei Co.

In the 1990' s, Dodwell BMS primarily sold and serviced special equipment for niche markets, such as Pitney Bowes franking machines and card issuing machines. The company decided that there was limited growth potential from a business model restricted to the sale and maintenance of such equipment. Thus, in 1999, Dodwell BMS bought Seiko Co., Ltd, which produced lenses for global makers of security cameras, and in 2000, Dodwell BMS started its own security equipment business. At about the same time, Pitney Bowes Co. held the majority share of the Japanese market for card issuing machines used by hospitals, while Pro-Mech Corp. held most of the Japanese market for card issuing machines used by medical clinics. In 2000, Pitney Bowes decided to abandon the card issuing machinery business, and Dodwell BMS bought the Japanese business. In the same year, it purchased Pro-Mech, giving it the dominant share of the Japanese market for card issuing machines used by hospitals and medical clinics. In 2001, Dodwell BMS took an equity stake in Takamisawa Cybernetics Co., Ltd. (6424) and thereafter jointly developed machines for cash cards issued by banks and other financial companies while expanding the market for such machines.

History of Dodwell BMS

1950	Established as Typewriter Service Co., Ltd.
1963	Reorganized as Dodwell Business Machines Service Co., Ltd.
1978	Renamed Dodwell BMS Ltd.
1999	Took a majority stake in Seiko Co., Ltd., making it a subsidiary
1999	Registered shares on the over-the-counter market
2000	Took a majority stake in Pro-Mech Corp., making it a subsidiary
2001	Took an equity stake in Takamisawa Cybernetics Co., Ltd.
2002	Listed shares on the Second Section of the Tokyo Stock Exchange
2003	Listed shares on the First Section of the Tokyo Stock Exchange
2003	Purchased the digital security network business of 3R Corp., Ltd., of South Korea
2005	Entered a business agreement with Graphtec Corp.



■ Company Outline

In 1949, a Mr. Watanabe, a former employee of Yokogawa Electric Corp. (6841), set up Watanabe Laboratories. In 1961, this company developed Japan's first X-Y plotter for the automatic production of graphs. Subsequently, the company entered the business of producing pen plotters for computer-aided design, a product that became a global success. In the early 1990's, however, Hewlett-Packard Inc., of the US, introduced ink-jet printers, and consequently, the demand for pen plotters dried up rapidly. Graphtec was forced to restructure, curtailing its operations throughout Japan, and finally, it sought assistance from Dodwell BMS through a formal agreement.

History of Graphtec

1949	Established as Watanabe Laboratories
1952	Name changed to Watanabe Measurement Equipment Mfg.
1961	Developed Japan's first X-Y plotter
1977	Name changed to Watanabe Measurement Equipment
1983	Name changed to Graphtec Corp.
1985	Shares listed on the Second Section of the Tokyo Stock Exchange
1987	Shares listed on the First Section of the Tokyo Stock Exchange
1995	Established subsidiary Graphtec North America Inc.
2005	Subsidiary Graphtec North America Inc. changed its name to Graphtec America Inc.

Strong sales of security equipment led to substantial profit growth in H1 FY6/13

(2)Description of Businesses

When Ai Holdings was established in April 2007, its two operating companies were Dodwell BMS and Graphtec. Dodwell BMS produced security cameras and other kinds of security equipment and machinery for issuing credit cards for banks and distribution companies and patient registration cards for hospitals and medical clinics. Graphtec produced information and measuring equipment, such as plotters, scanners and other kinds of peripheral computer equipment, as well as devices for environmental experimentation. Ai Sekkei Co., which undertakes structural design with special expertise in seismic evaluation, is now the third main operating company in the Ai Holdings group. Ai Holdings has 15 subsidiaries, of which, 14 are consolidated, and one is accounted for by the equity-in-earnings method. Through these subsidiaries, Ai Holdings engages in the following eight businesses.



Businesses Undertaken by Ai Holdings

Security equipment:

This business consists of the development, manufacture and sale of security system equipment, such as security cameras and recorders. It is conducted by Dodwell BMS and Ai Engineering.

Card equipment and other office equipment:

This business consists of the development, manufacture and sale of machines for issuing patient registration cards for medical institutions, machines for the automatic recording of return visits by patients to medical institutions, equipment for issuing and handling IC cards for financial institutions, and other office equipment. It is conducted by Dodwell BMS, Ai Engineering, and Pro-Mech Corp.

Maintenance service:

This business comprises the maintenance of security equipment and card equipment and is conducted by Dodwell BMS.

Peripheral computer equipment:

This business consists of the development, manufacture, sale and maintenance of peripheral computer equipment, such as plotters and scanners. It is conducted by Graphtec Corp., Silhouette America Inc., Graphtec North America Inc., and Graphtec Europe Inc.

Measuring equipment and environmental testing devices:

This business consists of the development, manufacture and sale of measuring equipment, mainly data loggers, which electronically record the results of measurements by environmental testing device sensors, and of environmental testing devices. It is conducted by Graphtec Corp., Graphtec North America Inc., and Graphtec Europe Inc.

Design:

This business consists of the design of buildings, mainly structural design, and the appraisal of earthquake resistance. It is conducted by Ai Sekkei Co., Chuo Sekkei Co., and Tanabe Sekkei Co.

Leasing, installment leasing, and installment sales:

This business is conducted by BM General Lease Co.

Other businesses:

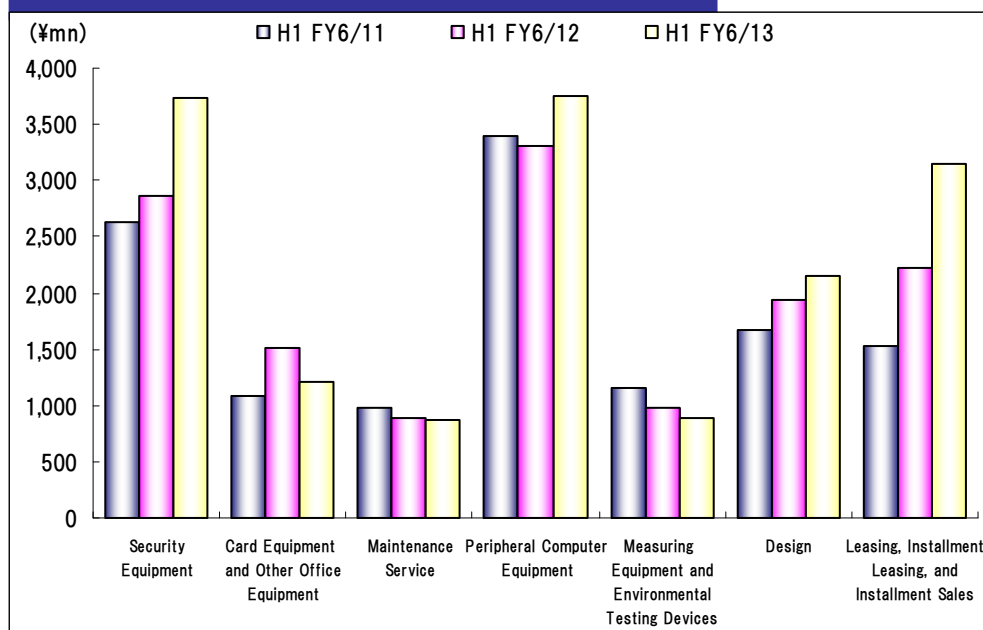
This segment includes the manufacture and sales of card readers and the development and sale of software. It is conducted by Nueron Co., Nueron Electronics Co., and USTAGE.

■ Company Outline

In H1 FY6/13, the security equipment business supplied 23% of Ai Holdings' consolidated sales, the peripheral computer equipment business supplied 23%, the leasing and installment leasing/sales business provided 20%, the design business accounted for 13%, and the card equipment and other office equipment business supplied 8%. These five businesses therefore accounted for 87% of total consolidated sales. The security equipment business supplied 46% of Ai Holdings' consolidated operating profit, the peripheral computer equipment business supplied 16%, the design business accounted for 14%, and the card equipment and other office equipment business supplied 11%. These four businesses therefore accounted for 87% of total consolidated operating profit.

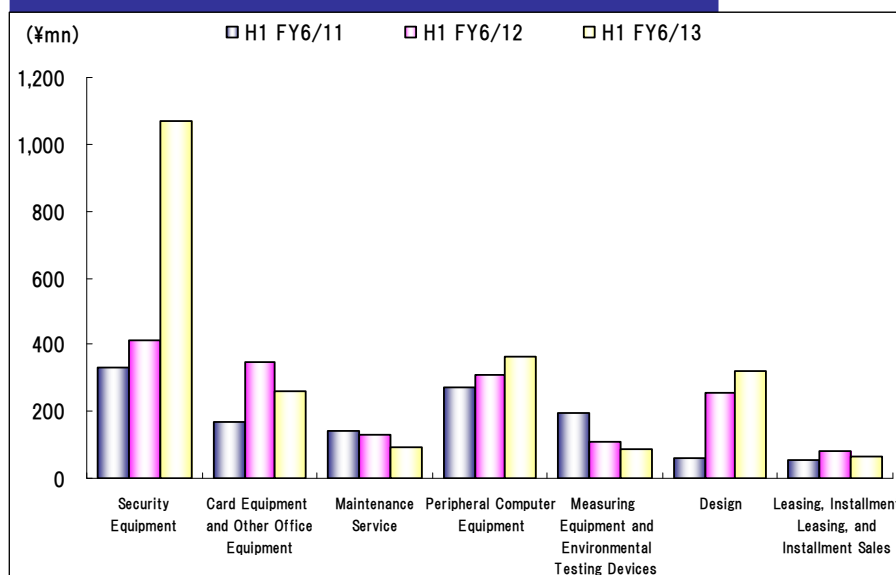
The operating profit margin in the security equipment business jumped to 28.6% in H1 FY6/13, from 15.4% in H1 FY6/12, reflecting a larger sales increase than the company had projected yet a minimal increase in SGA costs in the business. In the design business, the operating profit margin rose from 13.1% in H1 FY6/12 to 14.8% in H1 FY6/13, due to brisk orders for the evaluation of earthquake resistance. In the peripheral computer equipment business, the operating profit margin increased to 9.7% in H1 FY6/13, from 9.3% in H1 FY6/12, as Silhouette America Inc. doubled its operating profit y-o-y. On the other hand, accompanying sales declines in the card equipment and other office equipment business and in the measuring equipment and environmental testing devices business, the operating profit margins in these businesses declined from 22.1% to 21.7% and from 11.3% to 10.0%, respectively.

Consolidated Sales (¥mn) Generated by Seven Main Businesses, H1 FY6/11-H1 FY6/13



■ Company Outline

Consolidated Operating Profit (¥mn) Earned by Seven Main Businesses, H1 FY6/11-H1 FY6/13



Sales of security equipment to condominium buildings grew

(a) Security Equipment

As stated above, in 1999, Dodwell BMS took a majority stake in Seiko Co., which manufactured lenses for security cameras. Through Seiko Co., Dodwell BMS was able to start selling security cameras in 2000. Seiko supplied lenses to top makers of security cameras worldwide, and the most technically advanced makers were South Korean. To guard against possible threats from North Korea, South Korea had stressed security camera technology, and with the rapid spread of broadband digital services and the development of digital compression technology in Korea, the private sector in South Korea excelled in video compression on a global scale. In contrast, large Japanese electronics companies, such as Panasonic (6752), Mitsubishi Electric (6503), and Hitachi (6501), concentrated on the development of consumer electronic products, as there was less need for security cameras in Japan. Thus, Dodwell BMS was able to procure security cameras from makers in South Korea and Taiwan and to sell them at low prices in Japan, even after adding a sales agent commission.

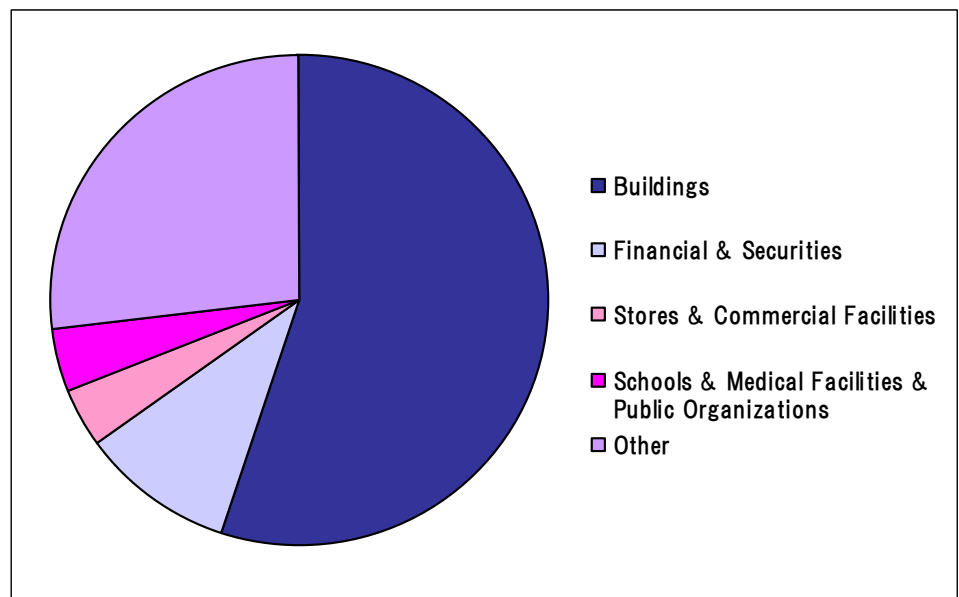
The two main customer categories for security equipment are condominium buildings and companies, including public organizations. In H1 FY6/13, condominium buildings accounted for 55% of the digital video recorders (DVRs) and iNEX network security software sold by the security equipment business, while financial companies, including securities companies, accounted for 10%, schools, medical facilities, and public organizations accounted for 4%, and stores and other commercial facilities accounted for 4%.

Security Cameras Sold by Dodwell BMS and Typical View Through Such Cameras



Source: Company

Breakdown of Security Equipment Sales in H1 FY6/13 by Customer Industry



Note: Based on sales of digital video recorders (DVRs) and iNEX network security software

Originally, most security equipment was sold to companies, primarily banks and other financial companies, and all sales were made by business partners (sales agents). Today, the three main business partners are Azbil Corp. (formerly Yamatake Corp.), Itoki, and Fuji Xerox. Fuji Xerox became a business partner two years ago, and with a nationwide network of sales offices, this company has been contributing notably to sales growth in the security equipment business. In H1 FY6/13, Fuji Xerox led sales growth in this business. It acquired large contracts not only for conventional security cameras to prevent crime, but also for cameras to monitor production lines for box lunches sold to convenience stores and for cameras to monitor the facilities for the care of the aged.

■ Company Outline

When Dodwell BMS first tried to sell security equipment to condominium buildings, it found direct cold sales ineffective. It therefore cultivated business ties with leading condominium building management companies, which had influence over the unions of condominium owners. Through these ties, Dodwell BMS was able to sell its equipment to condominium buildings. Dodwell BMS now employs about 150 people to sell security equipment to condominium buildings. Most of these sales people are young, and they have been very successful, as shown by the sales growth in H1 FY6/13.

Dodwell BMS sells security equipment only to existing condominium buildings. The companies that design or construct new condominium buildings determine the suppliers of security systems for these buildings and usually chose systems made by large companies, such as Panasonic, Mitsubishi Electric, and Hitachi, as these companies are considered reliable. Anyway, systems for new condominium buildings are generally very price-competitive, providing low profit margins, so they are not attractive to Dodwell BMS.

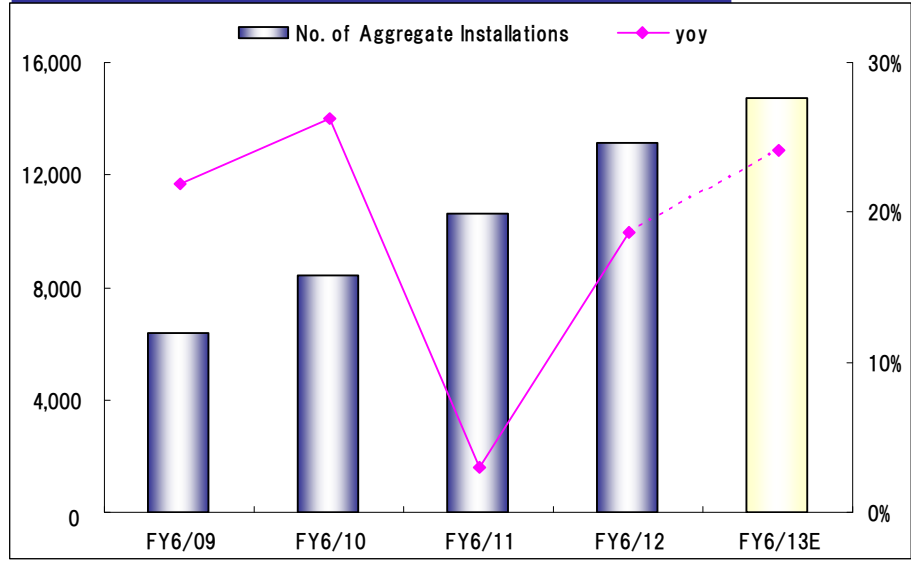
Dodwell BMS estimates that there are about 140,000 existing condominium buildings in Japan to which it could sell its security equipment and several tens of thousands of existing apartment buildings that could be targeted. To date, the company has installed security equipment in about 14,000 existing condominium buildings, and its near-term target is 20,000 buildings. Although Dodwell BMS has entered business agreements with several leading building management companies, as of May 2012, the company had installed only about 14% of the equipment in buildings managed by 15 of the largest companies. Thus, it should be able to expand this business notably. Dodwell BMS' s main condominium developer customers are the Daikyo Group (8840), the Haseko group (1808), the Nippon Housing group (4781), and the Tokyu Community group (4711).

Currently, 90% of the security equipment sales to condominium buildings by Dodwell BMS are made through lease contracts. Dodwell BMS relies on Mitsubishi UFJ Lease & Finance Co. (8593) for most of these contracts. The management union of each condominium building signs a six-year contract with the lease company calling for 72 equal monthly payments. During the lease period, Dodwell BMS maintains and guarantees the equipment. When a lease contract expires, the condominium building can continue to use the security equipment according to annual contracts under identical conditions. Alternatively, as the expiration date of a lease contract approaches, Dodwell BMS may propose the replacement of the installed security system with a new system. The technology for digital video cameras and recorders advances rapidly, improving their function. Thus, most condominium buildings prefer to replace older systems with new ones. For Dodwell BMS, replacing a system is more profitable than installing a new system. Therefore, the company plans to increase the sales weight of system replacement hereafter, thereby raising profitability. Dodwell BMS started lease sales of security equipment to condominium buildings on a full scale in 2006, and the initial contracts are now expiring, providing an opportunity for more replacement work. In H1 FY6/13, the company concluded 337 lease contract renewals for condominium buildings, of which, 68% were for equipment replacement, 22% were for the continued use of older equipment, and 10% were other types of contracts.



■ Company Outline

Aggregate Installations of Security Equipment by Dodwell BMS



Source: Company

Note: figure for FY6/13 is estimated by FISCO, yoy rate shows growth rate of yearly sales of security equipment.

Sales of compact cutting machines for hobbies grew rapidly in the US and Europe

(b)Peripheral Computer Equipment

As stated above, Graphtec Corp. developed Japan’s first X-Y plotter, and then developed a pen plotter for computer-aided design which was a commercial success until the early 1990’s, when Hewlett-Packard introduced inkjet printers. Subsequently, the demand for pen plotters shrank rapidly, so Graphtec replaced the pens of its pen plotter with cutters to produce cutting machines, which cut the sheets of paper on which computer printouts are made. These cutting machines are targeted for use in the sign and advertizing markets. Graphtec estimates that it holds a 30% share of the global market for commercial cutting machines, the largest share. Competitors include Roland DG (6789) and Mimaki Engineering (6638).

Graphtec Cutting Machines



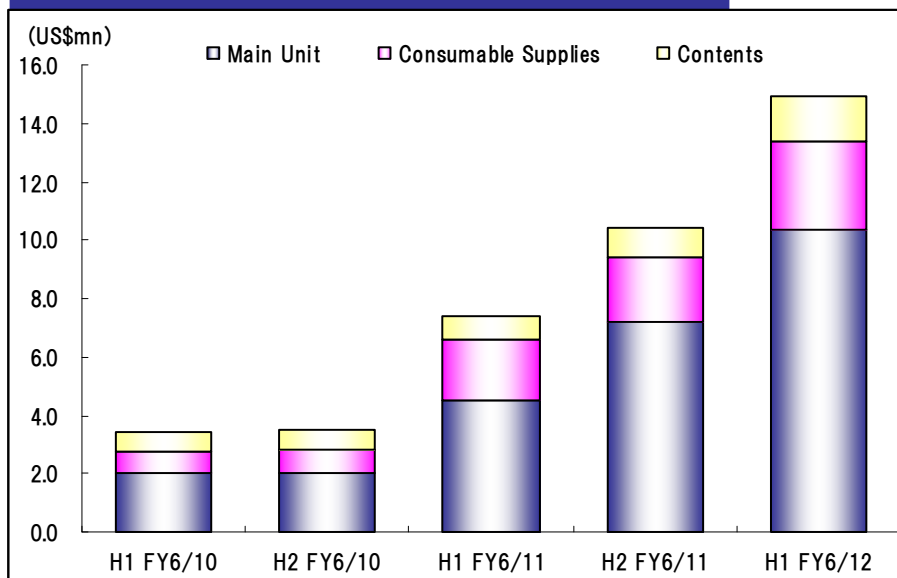
Source: Company



■ Company Outline

The peripheral computer equipment business is not a core business at present, but sales of compact cutting machines to general consumers for paper craft and other hobbies are growing rapidly. A Graphtec cutting machine for commercial use costs several tens of thousands of yen, but Silhouette America Inc. has applied Graphtec’s cutting machine technology to develop a small cutting machine that costs only about ¥10,000-20,000. It also sells supplies and digital content for these machines. In H1 FY6/13, Silhouette America’s sales doubled y-o-y to US\$14.89mn (¥1.34 bn at an exchange rate of ¥90 = US\$1). Of these sales, 70% came from small cutting machines, 20% from supplies for these machines, and 10% from content. Silhouette America has contracted with outside parties who have created more than 33,000 designs for cut materials. When a user purchases a design, he or she is charged each time he or she downloads it. The small cutting machines are manufactured cheaply in China and Vietnam, so they can be sold at low prices, yet profitably. Silhouette America’s strategy is to promote the rapid expansion of machine sales, then induce machine users to buy the highly profitable designs. Until recently, about 60% of the cutting machines sold to consumers in North America were supplied by Amazon.com. However, in October 2012, Silhouette America introduced its low-priced Portrait model of small cutting machine, and the company is now aiming to sell this machine through mass retailers such as Walmart.

Breakdown by Product Line of Fiscal Half-Year Sales (US\$m) by Silhouette America Inc., H1 FY6/10 - H1 FY6/13



■ Company Outline

According to the US Craft & Hobby Association, the North American market for crafts and hobbies amounted to US\$30.3bn (¥2.7trn at an exchange rate of ¥90 per US\$) in 2011. The market for paper and memory crafts was US\$3.5bn (¥315bn), and the market for artistic crafts was US\$3.1bn (¥279bn). Silhouette America targets these two markets for its small cutting machines. Thus, the potential market for these machines is about ¥600bn per year. It is difficult to determine whether the Japanese market for paper crafts is this large, but scrapbooking is a popular pastime among housewives in the US and Europe. Many of these housewives still cut out articles and photographs with scissors and paste them into scrapbooks manually, but by using personal computers and the cutting machines and designs provided by Silhouette America they could produce scrapbooks of higher quality than traditional ones. As Silhouette America has just entered the market for small cutting machines, it is difficult to project whether the company can maintain its current rapid rate of growth. However, for FY6/16, the company targets sales of US\$114mn (¥10.3bn at an exchange rate of ¥90 per US\$) and a gross profit of US\$51mn (¥4.6bn), whereas for FY6/13, it projects sales of US\$38mn (¥3.4bn) and a gross profit of US\$14mn (¥1.3bn).

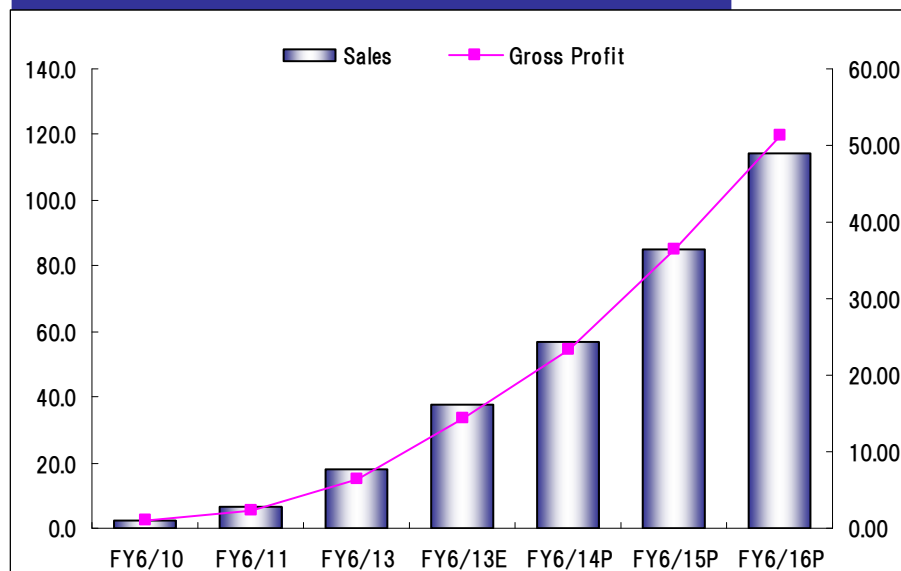
Examples of Craft and Hobby Activity



Source: Company

■ Company Outline

Silhouette America's Sales and Gross Profit (US\$m) in FY6/10-FY6/12, Forecasts for FY6/13 and Targets for FY6/14-FY6/16



Orders brisk, reflecting growing demand for evaluation of earthquake resistance since Great East Japan Earthquake

(c)Design

On December 25, 1995, shortly after the Kobe Earthquake, which killed about 6,000 people, Japan implemented a new law to promote the reinforcement of buildings against earthquake motion. In 1996, the predecessor of Ai Sekkei entered the business of evaluating the earthquake resistance of buildings. Now, Ai Sekkei and two other consolidated subsidiaries of Ai Holdings, Tanabe Sekkei and Chuo Sekkei, employ more than 200 technicians and have established a reputation as one of Japan's leading groups in the design of earthquake-resistant buildings.

Since the Great East Japan Earthquake and accompanying tsunami of March 11, 2011, which killed about 20,000 people, the demand for the evaluation of earthquake resistance has increased and the design business has been receiving many orders. However, current law simply encourages the owners of buildings to evaluate their earthquake resistance and to strengthen them if necessary. It does not oblige owners to do so. Thus, although most public buildings have been strengthened, only about 60% of the large buildings in the private sector have been. Therefore, the Japanese government plans to tighten regulations. Anti-earthquake standards for buildings were strengthened in 1981. For buildings with 5,000 square meters or more of floor space built before 1981, the government plans to require strengthening, if needed, by 2015, and will subsidize such strengthening. Building owners who fail to evaluate their buildings and strengthen them, if needed, will be fined.

■ Company Outline

The evaluation of the earthquake resistance of a building and the design of earthquake-resistant buildings require expertise, and with more than 200 technicians, in H1 FY6/13, the design business received enough orders for the evaluation of the earthquake resistance and the design of earthquake-resistant buildings to keep busy for the entire fiscal year. However, management does not intend to hire more personnel or otherwise increase the work capacity of this business, as it is content with the stable cash flow provided by the business.

In H1 FY6/13, the design business increased its sales by 11.2% y-o-y to ¥2,155mn. Of this amount, 40% came from the appraisal of the earthquake resistance of buildings.

In H2 FY6/13, the business will start supplying machines to a large regional bank

(d) Card Equipment and Other Office Equipment

As stated previously, Dodwell BMS has been involved in this business for a long time and now holds a dominant share of the Japanese market for machines that issue patient registration cards for hospitals and medical clinics. Dodwell BMS and other members of the Ai Holdings group supply a vast array of machines to medical facilities, ranging from small clinics to large hospitals. Among these are machines that manage patient information and return visits to medical facilities, automatic payment machines, machines that dispense receipts for laboratory tests performed, machines that display the order in which patients are treated or administered, and machines that label laboratory specimens. This business also produces machines that issue and process IC cards for financial institutions, allowing these institutions to serve their customers quickly, improving customer satisfaction. In FY6/12, this business delivered about 350 IC card issuing machines to the Fukuoka Bank group. In H1 FY6/13, the business did not deliver so many machines, so its sales and profits declined y-o-y. In H2 FY6/13, however, the business will start supplying many machines to a large regional bank, so it is likely to increase sales and profits y-o-y in FY6/13.

A Card-Issuing Machine Produced by Ai Holdings and an Example of a Card Issued by Such a Machine



Source: Company

Business Trends

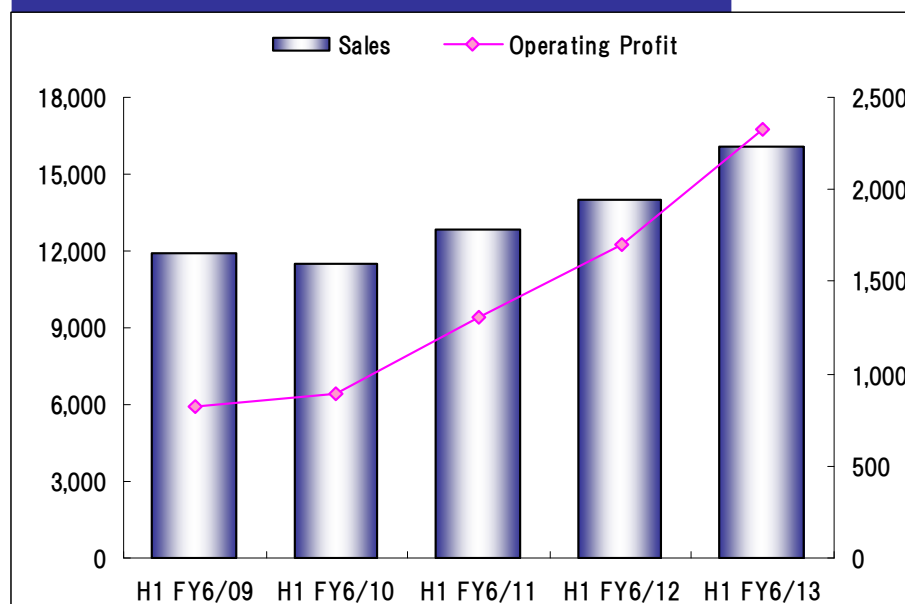
FY6/13 results likely to exceed company forecasts

(1)H1 FY6/13 results

On February 14, 2013, Ai Holdings announced its business results for H1 FY6/13. Consolidated sales rose 15.1% y-o-y to ¥16,079mn, operating profit grew 36.7% y-o-y to ¥2,326mn, recurring profit advanced 23.8% y-o-y to ¥2,442mn, and net profit increased 17.0% to ¥1,327mn. These figures substantially surpassed the company's forecasts, of ¥15,000mn, ¥1,900mn, ¥1,950, and ¥1,050, respectively. The security equipment business performed especially well, reflecting an increase in demand for the replacement of old equipment at condominium buildings and more new contracts than the company had expected. The peripheral computer equipment business also grew, with an outstanding contribution from Silhouette America, which greatly expanded its sales of compact cutting machines to general consumers for paper craft and other hobbies. In US dollars, the sales and profits of Silhouette America doubled y-o-y. The design business continued to expand its evaluation of earthquake-resistance, and obtained enough orders to keep it fully occupied in H2 FY6/13.

In H1 FY6/13, Ai Holdings recorded 52% of the sales the company forecast for the entire fiscal year and 55% of the operating profit it projected for the full year. Normally, it derives more sales and profit in H2 than in H1. Therefore, it seems likely that the company will exceed its forecasts for the full fiscal year.

Half Fiscal-year Sales and Operating Profit (¥mn)
of Ai Holdings, H1 FY6/09 - H1 FY6/13



■ Business Trends

**Half Fiscal-year Income Statement (¥mn) of Ai Holdings,
H1 FY6/09 - H1 FY6/13**

	H1 FY3/09	H1 FY3/10	H1 FY3/11	H1 FY3/12	H1 FY3/13
Sales	11,939	11,525	12,847	13,965	16,079
(yoy)	-	-3.5	11.5	8.7	15.1
Cost of sales	7,358	7,163	8,055	8,788	9,958
(Cost-of-sales ratio)	61.6	62.2	62.7	62.9	61.9
SGA cost	3,757	3,471	3,480	3,475	3,795
(SGA cost ratio)	31.5	30.1	27.1	24.9	23.6
Operating profit	824	890	1,311	1,701	2,326
(yoy)	-	8.0	47.2	29.8	36.7
(Margin)	6.9	7.7	10.2	12.2	14.5
Non-operating income	272	331	267	291	143
Non-operating costs	34	38	29	20	27
Recurring Profit	1,061	1,183	1,548	1,973	2,442
(yoy)	-	11.5	30.9	27.4	23.8
(Margin)	8.9	10.3	12.0	14.1	15.2
Extraordinary gains	299	19	50	0	14
Extraordinary losses	172	57	144	135	286
Pretax profit	1,188	1,145	1,454	1,837	2,170
(yoy)	-	-3.6	27.0	26.3	18.1
(Margin)	10.0	9.9	11.3	13.2	13.5
Income taxes	543	234	439	703	843
(Effective tax rate)	45.7	20.4	30.2	38.3	38.8
Minority interest	-	-	-	-	-
Net profit	645	911	1,015	1,134	1,327
(yoy)	-	41.3	11.4	11.7	17.1
(Margin)	5.4	7.9	7.9	8.1	8.3
[Other important data]					
Earnings per share (¥)	11.75	16.60	18.51	20.73	28.03
Dividend per share (¥)	8.0	10.0	8.0	8.0	10.0
Book value per share (¥)	368.06	371.41	397.29	438.38	466.17

Operating profit margin rose 14.1 percentage points y-o-y to 28.6%

(2) Business trends by division

Security Equipment

Reflecting brisk sales to condominium buildings and, through sales agents, to corporations, sales in the security equipment business grew 39.2% y-o-y in H1 FY6/13 to ¥3,742mn, or 23% of total sales by Ai Holdings, while operating profit surged 158.3% to ¥1,072mn, or 46% to total operating profit earned by Ai Holdings. The operating profit margin in the security equipment business jumped to 28.6%, from 14.5% in H1 FY6/12.



■ Business Trends

The growth in sales of security equipment to condominium buildings was a result of the business cultivating closer ties with building management companies and of greater experience by the business' s approximately 150 sales representatives. Sales to condominium buildings rose 37.1% y-o-y to ¥2,412mn, as the business garnered 1,580 contracts, 1,243 new contracts, more than the target of 1,000 new contracts, and 337 contract renewals. SGA costs in the business were contained due to the greater efficiency of sales personnel and to an increase in the sales weighting of high-margin replacement work. Consequently, the profitability of the business improved notably.

For FY6/13, the business targets 2,000 new contracts and 880 contract renewals for condominium buildings, for a total of 2,880. Based on its results in H1, however, it appears likely that the business will achieve more than 3,000 contracts in the full fiscal year.

Sales of security equipment to corporations increased 19.8% y-o-y to ¥1,330mn in H1 FY6/13. Business partner Fuji Xerox sold more equipment, not only to prevent crime, but also but also to monitor production lines for box lunches sold to convenience stores and to monitor the conditions at facilities for the care of the aged. Sales of security equipment to financial institutions also started to recover.

Peripheral Computer Equipment

In H1 FY6/13, sales of cutting machines for commercial use declined y-o-y, but sales of compact cutting machines by Silhouette America increased enough to more than offset this decline. Thus, totals sales of peripheral computer equipment were up by 13.4% y-o-y to ¥3,760mn, or 23% of total sales by Ai Holdings, and operating profit in this business grew 19.2% y-o-y to ¥366mn, or 16% of group operating profit. The operating profit margin of the business rose to 9.7%, from 9.3% in H1 FY6/12. Silhouette America led growth in this business, increasing its sales to US\$14.89mn from US\$7.27mn in H1 FY6/12, and its operating profit to US\$2.2mn, from US\$1.1mn a year earlier. Of Silhouette America' s total sales, 70% came from cutting machines, 20% from supplies for these machines, and 10% from software content for them. Although the sales weight of software content is low, this content yields a high operating profit margin. Thus, Silhouette America aims to rapidly increase the number of cutting machines sold, then to sell more content for them. The implementation of this strategy will require the company to expand its sales network in North America.

Design

Reflecting brisk work in evaluating the earthquake-resistance of buildings, sales in the design business grew 11.2% y-o-y in H1 FY6/13 to ¥2,155mn, or 13% of group sales, while operating profit grew 25.7% to ¥318mn, or 14% of group operating profit. The operating profit margin rose to 14.8% from 13.1% in H1 FY6/12. However, as stated earlier, management does not plan to increase the work force in this business or otherwise improve its work capacity, as it is satisfied with the stable cash flow provided by the business.



■ Business Trends

Card Equipment and Other Office Equipment

In FY6/12, this business delivered about 350 IC card issuing machines to the Fukuoka Bank group. In H1 FY6/13, the business did not deliver so many machines, so its sales fell 20.0% y-o-y to ¥1,208mn, or 8% of group sales, and its operating profit declined 24.3% y-o-y to ¥262mn, or 11% of group operating profit. The operating profit margin decreased to 21.7% from 22.9% in H1 FY6/12. In H2 FY6/13, however, the business will start supplying many machines to a large regional bank, so it is likely to increase sales and profits y-o-y in FY6/13.

■ Negative Risks to Business**Rapid growth of compact cutting machines in the US and Europe has a key to further growth**

The company's business could be adversely affected by any of the three factors described below.

M & A

Ai Holdings has expanded its business through many mergers or acquisitions of other companies with solid balance sheets, respectable histories, and strengths in niche markets, even if they were temporarily unprofitable. However, these successful mergers and acquisitions depended largely on the skill and experience of chairman Sasaki. Certainly, Mr. Sasaki deserves praise for his long record of business growth, including some restructurings. However, there is no guarantee that he will remain so successful. Furthermore, potential acquisitions that satisfy the above qualifications and can be bought cheaply may not arise, or Ai Holdings could miss the timing for such deals. Finally, some mergers and acquisitions fail because of liabilities at the acquired company that were found after the acquisition.

Silhouette America

Silhouette America is attempting to develop a new market in North America and Europe, one in which its compact cutting machines and designs sold online produce scrapbooks and other forms of paper crafts and hobbies to replace traditional products made by hand. To achieve this goal, the company is rapidly expanding its sales network, aiming to expedite sales of compact cutting machines. This expansion may cost more than currently envisioned, and the new market may not grow as fast as currently hoped, leading to significant disappointment, given the high hopes now held for the company.

Litigation

As a global company, Ai Holdings is vulnerable to legal challenges in Japan and overseas. In fact, in 2008, Graphtec was sued in Japan for patent infringement by Mimaki Engineering, a competitor in the manufacture of cutting machines for commercial use, and in 2009, Graphtec counter-sued Mimaki Engineering for patent infringement. In 2011, these companies settled their claims with little impact on Graphtec's business. However, similar suits may arise hereafter.



■ Growth Strategy

Aims to expand existing businesses and launch new ones through M&A

Ai Holdings plans to expand through aggressive M&A, but it does not announce medium-term plans or other targets because it does not know what businesses it might acquire, nor when. However, the company does have three criteria for an acquisition target: it must have a solid balance sheet, even if unprofitable it must be strong in a niche market, and it must have a track record. Any company with experience in any industry, except the food industry and the real estate industry, is a potential acquisition target. A company capable of benefitting from Ai Holdings' approximately 50,000 customers and nationwide maintenance network should be able to contribute to the group soon after being acquired. For example, Graphtec had been unprofitable for several years before it was acquired, but it turned profitable within three years of being acquired.

To expand its existing businesses, Ai Holdings will most likely concentrate on security equipment for condominium buildings and Silhouette America's compact cutting machines for paper craft and hobby enthusiasts. Its security equipment has been installed on only about 14,000 of Japan's approximately 140,000 condominium buildings, indicating ample room for expansion. Similarly, this equipment has been installed in about 14% of the condominium buildings managed by 15 leading building management companies, so the company should be able to increase this proportion. As mentioned previously, the roughly 150 employees who sell security equipment to condominium buildings have been systematizing their operations and gaining experience. Thus, sales are accelerating, and the business appears to be on a growth track. Silhouette America is now promoting sales of its compact cutting machines. A US competitor, Provo Craft & Novelty, has annual sales of about ¥25bn, but Silhouette America appears to have superior products and a superior business model, so it should soon generate annual sales of ¥10bn or more.

■ Shareholder Return Policy

As profits grow, the company is likely to increase its dividend

Ai Holdings has announced that it will pay a dividend of ¥20 per share for FY6/13, up from ¥16 for FY6/12. Thus, its dividend payout ratio will rise to about 37.9% in FY6/13, from 35.8% in FY6/12. The company aims to achieve a dividend payout ratio of 40%, so if its profits continue to grow, it will most likely raise its dividend again. In FY6/12, the company bought some of its shares outstanding, and its treasury stock now numbers 9.22 million shares, or about 16% of all shares outstanding. The company plans to use its treasury stock for M&A and does not plan to retire them.



Disclaimer

FISCO Ltd. (the terms “ FISCO ” , “ we ” , mean FISCO Ltd.) has legal agreements with the Tokyo Stock Exchange, the Osaka Securities 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 Osaka Securities Exchange, and therefore all rights to them belong to the Osaka Securities 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.