

Ai Holdings3076 Tokyo Stock Exchange
First Section

15-Oct.-14

Important disclosures
and disclaimers appear
at the end of this document.FISCO Ltd. Analyst
Noboru Terashima**■ Double-digit growth of sales and profits continued in FY6/14; three growth engines to lead further profit growth**

Ai Holdings is a pure holding company for 17 operational companies, including Dodwell BMS Ltd. and Graphtec Corp. These companies engage in seven businesses. The security equipment business and the peripheral computer equipment business in the US have been the main profit growth drivers. From FY6/15 onwards, the company expects its new label printer business to also drive profit growth.

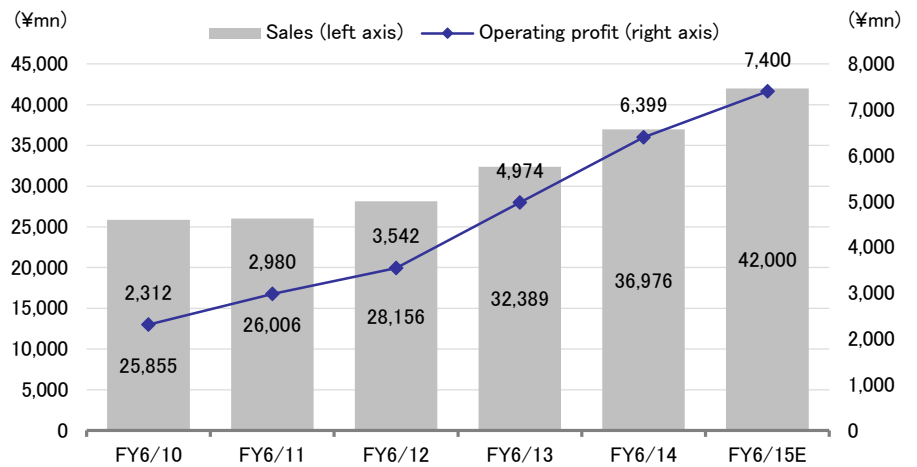
In FY6/14, Ai Holdings recorded consolidated sales of ¥36,976mn, up 14.2% year-on-year (y-o-y), consolidated operating profit of ¥6,399mn, up 28.6% y-o-y, consolidated recurring profit of ¥6,553mn, up 29.0%, and consolidated net profit of ¥4,043mn, up 36.0%. For FY6/15, Ai Holdings forecasts consolidated sales of ¥42,000mn, up 13.6% y-o-y, consolidated operating profit of ¥7,400mn, up 15.6% y-o-y, consolidated recurring profit of ¥7,500mn, up 14.4%, and consolidated net profit of ¥4,800mn, up 18.7%. Based on the current state of the company's businesses, its forecasts for FY6/15 appear conservative and its forecasts may be revised upwards.

All the company's businesses are profitable, but profit growth in FY6/14 was led by the security equipment business and the sale of cutting machines for retail customers in the US. In FY6/15, Ai Holdings plans to enter the business of producing label printers and expects this business to generate strong profit growth. These three businesses are likely to propel profit growth for several years. The company aims to maintain a dividend payout ratio of 30%. Given the promising prospects for profit growth, it will probably increase its dividend in coming years.

■ Check Point

- Double-digit sales and profit growth in FY6/14 was led by the security equipment and peripheral computer equipment businesses
- The company projects sales and profit growth for FY6/15, but we expect it to exceed its projections
- From FY6/15, growth is likely to be led by three businesses: security equipment, Silhouette America Inc., and the new label printing business

Consolidated Sales and Operating Profit



■ Company Outline

Established as a holding company in 2007, the company has grown through M&A and establishing subsidiaries

(1) Company History

Established in 2007, Ai Holdings Corp. encompasses 17 operational companies, of which, 14 are consolidated subsidiaries, 2 are non-consolidated subsidiaries, and 1 is an equity method affiliate. Given that Dodwell BMS Ltd. and Graphtec Corp., are the main operational companies, the history of these two subsidiaries is outlined below.

Established in 1950 as Typewriter Service Co., Ltd., this company subsequently reorganized as a public stock company and renamed itself Dodwell BMS Ltd. In the early 1990's, Dodwell BMS primarily sold and serviced typewriters, franking machines and personal computers, but its profitability languished. In 1994, Mr. Hideyoshi Sasaki, the current Chairman of Ai Holdings, took a 51% stake in the company and became its top executive. Mr. Sasaki established a policy of putting profits ahead of sales, and by 1999, the company's profits had recovered enough to register its shares on the over-the-counter market.

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.
1994	Mr. Hideyoshi Sasaki took a 51% stake in the company and became its president
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
2005	Entered a business agreement with Graphtec Corp.
2007	Merged with Graphtec Corp. to form Ai Holdings Corp.

The other main operational company is Graphtec Corp. 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 CAD (computer-aided design) and operated globally. In the early 1990's, however, as a consequence of Hewlett-Packard Inc., of the US, introducing ink-jet printers, the demand for pen plotters rapidly declined and corporate performance continued to deteriorate. Despite reducing offices nationwide and managing to survive, restructuring led to a deterioration of customer service. The company hoped for a recovery from a business alliance with Dodwell BMS.

History of Graphtec

1949	Established as Watanabe Laboratories
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 a subsidiary in California, USA, now called Graphtec America Inc.
2005	Established business agreement with Dodwell BMS
2007	Merged with Dodwell BMS to form Ai Holdings Corp.
2014	Established Graphtec Digital Solutions, Inc.

Soon after its establishment in 2007, Ai Holdings Corp. listed its shares on the First Section of the Tokyo Stock Exchange. Since then, the company has grown rapidly by acquiring and setting up new subsidiaries.

History of Ai Holdings

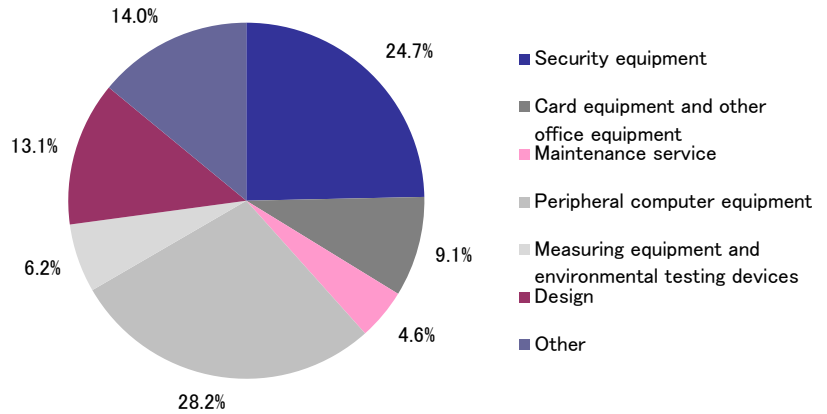
April 2007	Established through the merger of Dodwell BMS and Graphtec. Listed shares on the First Section of the Tokyo Stock Exchange.
July 2008	Purchased Neuron Co., making it a subsidiary.
January 2009	Purchased Shiomi Sekkei Co., making it a subsidiary.
July 2009	Established subsidiary Ai Engineering Co., Ltd.
September 2009	Established Silhouette America Inc.
July 2010	Shiomi Sekkei Co. changed its name to Ai Sekkei Co.

7 primary businesses are conducted by 17 group companies

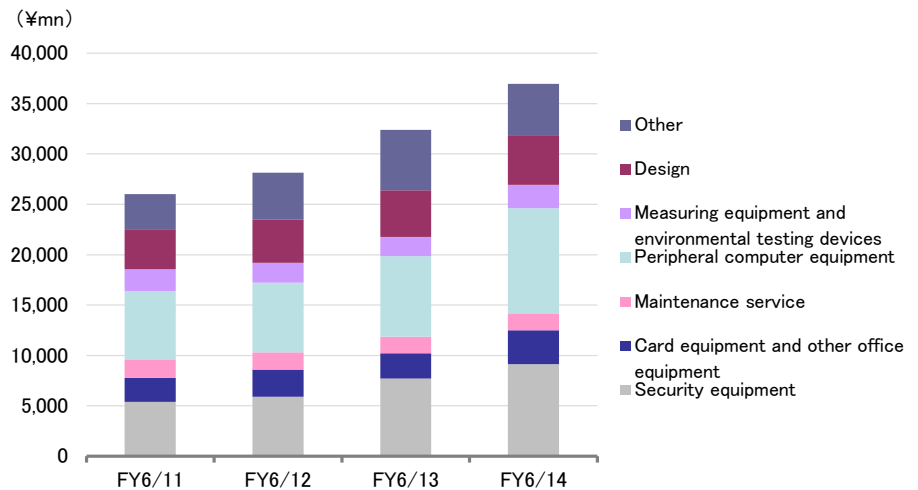
(2) Description of Businesses

As mentioned above, Ai Holdings is a pure holding company encompassing 17 operational companies, of which, 14 are consolidated subsidiaries, 2 are unconsolidated subsidiaries, and 1 is an equity method affiliate. These operational companies engage in seven businesses. In FY6/14, the sales and sales contributions of each business were as follows: security equipment ¥9,117mn (24.7%), card equipment and other office equipment ¥3,364mn (9.1%), maintenance service ¥1,708mn (4.6%), peripheral computer equipment ¥10,443mn (28.2%), measuring equipment and environmental testing devices ¥2,306mn (6.2%), design ¥4,845mn (13.1%), and other businesses ¥5,188mn (14.0%). Sales generated by each business over the past four fiscal years are summarized in the bar chart below.

Sales Contributions by Seven Businesses in FY6/14
(Total FY6/14 Sales ¥36,976mn)

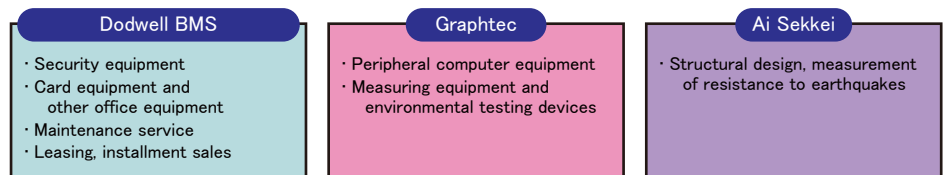


Sales by Seven Businesses



Ai Holdings has 14 consolidated subsidiaries. The three main ones are Dodwell BMS, Graphtec, and Ai Sekkei. The businesses they engage in are summarized in the figure below. From FY6/15, the peripheral computer equipment business of Graphtec will produce label printers on a full scale.

Main operational company and description of business



(a) Security Equipment

Security equipment includes security cameras and recorders. Most of these products are imported from South Korea, but Ai Holdings is deeply involved in determining the specifications for the purchased products. This equipment derived from South Korean military technology, so it incorporates advanced functions, relative to its price, and provides higher cost performance than similar equipment made by Japanese competitors.

Ai Holdings also provides comprehensive services for its security equipment, including maintenance service. The equipment is sold to a wide range of customer industries, including condominium buildings, banks, securities companies, and other financial institutions, government agencies, commercial areas, and retail store chains. In recent years, sales to existing condominium buildings have grown especially rapidly. When the company started its security equipment business, most sales were made by agencies to general corporations, but in recent years, the company has strategically expanded its direct sales, particularly to existing condominium buildings.

(b) Card Equipment and Other Office Equipment

Card equipment includes machines for issuing patient registration cards for medical institutions, machines for the automatic recording of return visits by patients to medical institutions, equipment for immediately issuing and handling IC cards for financial institutions and distributors, and other equipment. Sales to hospitals are not growing rapidly, but the company foresees steady demand from hospitals. Some regional banks have begun using the company's equipment for immediately issuing IC cards and some megabanks have decided to use them. This trend bears observation, as detailed below.

The main product in other office equipment is equipment for the computer-aided design of steel structures. The market for this equipment is a niche market, so it is not expected to grow rapidly, but the company anticipates steady replacement demand for the equipment.

(c) Maintenance Service

This business maintains security equipment, card equipment, and other equipment. In the past, it also maintained equipment produced by other companies to sustain the efficiency of its workforce, but in recent years, it has concentrated on maintaining equipment produced or sold by Ai Holdings, so the sales weighting of maintenance service for other companies has been declining.

The maintenance service business supplies a small proportion of Ai Holdings' total sales, but it is an important business. Most of the security equipment and card equipment sold by Ai Holdings is leased, rather than purchased outright, and requires periodic maintenance. Other companies selling this kind of equipment usually require two lease contracts, one for the equipment and the other for maintenance. However, Ai Holdings concludes a single lease contract called the Anshin Security System Pack for both the equipment and maintenance service. Therefore, the sales and profits of the maintenance service business are linked to the sales of the equipment. Sales and profits in the maintenance business are steady over the long term because maintenance is required at regular time intervals. Furthermore, this business supports the sales of security equipment and card equipment because customers can rest assured of proper after-sale service. Thus, the maintenance service business is a hidden source of sales and profits.

(d) Peripheral Computer Equipment

Peripheral computer equipment includes cutting machines and scanners handled by Graphtec. The company's cutting machines were developed based on Graphtec's original technology for plotters. These machines cut displays at widths from size A4 to 1,600 mm and are sold mainly to companies that make outdoor advertisements and signs.

In recent years, sales of small cutting machines to consumers in the United States and Europe for use in hobbies, mainly paper craft, have been growing rapidly. These machines are made in China and Vietnam and sell for ¥10,000–20,000 each. The company also organizes buyers of these small cutting machines into an association and sells them computer content, mainly patterns, and supplies. This business is conducted primarily by Silhouette America Inc., as detailed in a later section. The company's scanners for commercial use scan documents of up to A0 in size. Some of these scanners are manufactured on an OEM basis for large makers of precision equipment.

In May 2014, Ai Holdings announced plans to start producing label printers. This business will be conducted by Graphtec and will be part of the peripheral equipment division, as detailed below.

(e) Measuring Equipment and Environmental Testing Devices

Measuring equipment electronically records a wide range of variables, including electric voltage, temperature, humidity, and electric pulse. Environmental testing devices check the performance of electronic components, printed circuit boards, etc. under various conditions, such as high or low temperature. At the request of customers, the company customizes its environmental testing devices. Measuring equipment and environmental testing devices are inspection equipment, for which the demand is not growing rapidly, but this equipment affords steady profits.

(f) Design

Ai Sekkei Co., called Shiomi Sekkei when it was purchased by Ai Holdings, Chuo Sekkei Co., and Tanabe Sekkei Co. engage in design. These three consolidated subsidiaries employ more than 200 engineers with expertise in structural design. They mainly appraise the earthquake resistance of buildings and design earthquake-resistant buildings. They also provide comprehensive consulting service in the area of construction, especially in structural design and the design of equipment and devices requiring advanced technological knowledge. The design business is also a source of steady profits.

(g) Other Businesses

This segment comprises primarily the leasing and installment sales of the company's security equipment and card equipment. When necessary, this business also leases and sells on installments equipment produced by other companies.

Strong leadership and rapid decision-making are major strengths

(3) Distinctive Traits and Strengths

Each of the company's products and services possesses distinctive characteristics and strengths, but the main strengths of Ai Holdings are those discussed below.

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(a) Strong Leadership

The greatest strength of Ai Holdings is the leadership and management capability of Chairman and CEO Sasaki. As stated earlier, Mr. Sasaki acquired a controlling interest in Dodwell BML in 1994, and since then, he has built up Ai Holdings through a series of mergers and acquisitions. Mr. Sasaki has amassed a history of successful M&A transactions by adhering to strict principles for such transactions for the past 30 years. For example, he does not try to enter a business that yields a small gross profit. He also avoids businesses engaged in large markets that can easily be entered by large companies. This unwavering approach to business has supported accelerated profit growth.

(b) Rapid Decision-making

Mr. Sasaki makes management decisions and takes action rapidly. For example, he rapidly assessed business prospects in the US and purchased Silhouette America Inc. when the overall US economy was weak during the financial crisis following the collapse of Lehman Brothers. If an acquisition or alliance fails to deliver the desired result, he quickly sells the business or terminates the alliance and seeks more promising opportunities.

(c) Strong Marketing Capability

Ai Holdings has a strong marketing capability, particularly in the sale of security equipment. In recent years, the company has hired more women for sales of security equipment, prepared persuasive sales presentations, and switched its sales targets from financial institutions, schools, public facilities, and commercial complexes to existing condominium buildings, where the merits of the company's security equipment are apparent.

To prosper in this operating environment, the company has put more effort into recruiting and training employees. Mr. Sasaki has personally intervened in the hiring of new university graduates for the sales department of the security equipment business to promote the hiring of young people with unique personalities. These young people are then trained in the company's sales approach, which encourages sales people to use both their intelligence and a positive, empathetic attitude. The growth of sales of security equipment to existing condominium buildings in recent years has been supported as much by this approach as it has been by the functions and price of the equipment. This successful sales approach should support the growth of new businesses in the future.

(d) Reliable After-sale Support

Ai Holdings retains an in-house capability to offer maintenance and other after-sale support services. This has been an important factor in promoting the sale of office equipment and cutting machines to professional users. American consumers who have purchased the company's small cutting machines have also appreciated the after-sale services provided by Silhouette America Inc. The ability to directly offer maintenance service is a strength that has supported the sale of security equipment and card equipment. Most likely, the company will offer similar support services for its new label printer business.

■ Business Trends

Double-digit sales and profit growth, led by security equipment and peripheral computer equipment

(1) FY6/14 Results

(a) Sales and profits

In FY6/14, Ai Holdings' consolidated sales rose 14.2% y-o-y to ¥36,976mn, operating profit grew 28.6% y-o-y to ¥6,399mn, recurring profit advanced 29.0% y-o-y to ¥6,553mn, and net profit increased 36.0% to ¥4,043mn.

Summary Income Statement, FY6/13-FY6/14

	FY6/13		FY6/14		y-o-y change	
	Amt.	Ratio	Amt.	Ratio	Amt.	Rate
Sales	32,389	100.0%	36,976	100.0%	4,587	14.2%
Gross profit	13,043	40.3%	15,796	42.7%	2,753	21.1%
SGA cost	8,069	24.9%	9,396	25.4%	1,327	16.4%
Operating profit	4,974	15.4%	6,399	17.3%	1,425	28.6%
Recurring profit	5,080	15.7%	6,553	17.7%	1,473	29.0%
Net profit	2,974	9.2%	4,043	10.9%	1,069	36.0%

The company originally forecasted an operating profit of ¥5,500mn for FY6/14. When it announced its results for H1 FY3/14, it raised this forecast to ¥6,000mn, and when it announced its results for Q3 FY3/14, it lifted the forecast to ¥6,400mn. It virtually achieved its latest forecast for several reasons. Sales of security equipment grew strongly to both condominium buildings and corporations. Sales of card equipment to financial institutions and distributors increased. Sales by Silhouette America of compact cutting machines to general consumers for paper craft and other hobbies advanced, and revenues from the structural design of buildings and the appraisal of earthquake resistance rose. Results by business are detailed below.

Breakdown of Sales by Business, FY6/13-FY6/14

	FY6/13		FY6/14		y-o-y change	
	Amt.	Ratio	Amt.	Ratio	Amt.	Rate
Security equipment	7,713	23.8%	9,117	24.7%	1,404	18.2%
Card equipment / other office equipment	2,487	7.7%	3,364	9.1%	877	35.2%
Maintenance service	1,655	5.1%	1,708	4.6%	53	3.2%
Peripheral computer equipment	8,005	24.7%	10,443	28.2%	2,438	30.4%
Measuring equipment / environmental testing devices	1,904	5.9%	2,306	6.2%	402	21.1%
Design	4,618	14.3%	4,845	13.1%	227	4.9%
Other businesses	6,002	18.5%	5,188	14.0%	(814)	-13.6%

Breakdown of Operating Profit by Business, FY6/13-FY6/14

	FY6/13		FY6/14		y-o-y change	
	Amt.	Ratio	Amt.	Ratio	Amt.	Rate
Security equipment	2,291	47.1%	2,727	43.8%	436	19.0%
Card equipment / other office equipment	570	11.7%	946	15.2%	376	66.0%
Maintenance service	115	2.4%	173	2.8%	58	50.4%
Peripheral computer equipment	809	16.6%	1,091	17.5%	282	34.8%
Measuring equipment / environmental testing devices	198	4.1%	315	5.1%	117	59.2%
Design	715	14.7%	771	12.4%	56	7.9%
Other businesses	165	3.4%	207	3.3%	42	25.5%

Note: Operating profit shown above is before the elimination of corporate costs and other adjustments

● Security Equipment

Sales in the security equipment business grew 18.2% y-o-y in FY6/14 to ¥9,117mn, while operating profit surged 19.0% to ¥2,727mn. Sales to existing condominium buildings increased 17.1% to ¥6,117mn, and sales to corporations also rose strongly.

Two-thirds of FY6/14 sales of security equipment were made to existing condominium buildings. The business increased its contracts to more than 4,000. Both new contracts and contract renewals grew, accounting for 70% and 30%, respectively, of the total contracts.

Sales of security equipment to corporations and institutions climbed 19.2% y-o-y to ¥3,062mn. The company believes that corporate demand may have been stimulated by well-publicized incidents, such as the introduction of toxins at the plant of a leading food manufacture and the leaking of information about customers of a leading educational services company. Furthermore, the company notes that schools have been installing more security equipment along routes traveled by their students, as well as in the schools themselves.

● Card Equipment and Other Office Equipment

In FY6/14, sales of card equipment and other office equipment grew 35.2% y-o-y to ¥3,364mn and operating profit expanded by 66.0% to ¥946mn. Operating profit from the sale of card equipment increased 38.0% to ¥444mn, reflecting an increase in sales of machines for issuing credit cards to large regional banks and distribution companies.

Sales of other office equipment climbed, due in part to sales of a software program for the computer-aided design of steel structures launched two years ago. As a result, operating profit from the sale of this equipment jumped 102.2% y-o-y to ¥502mn.

● Peripheral Computer Equipment

In FY6/14, the peripheral computer equipment business increased its sales by 30.4% y-o-y to ¥10,443mn and its operating profit by 34.8% to ¥1,091mn. As in FY6/13, business growth was mainly attributable to Silhouette America. As mentioned previously, Silhouette America organizes the buyers of its compact cutting machines into customer associations, to which it sells content for these machines, such as patterns. The machines account for the bulk of Silhouette America's sales, but content provides significant profit. In other words, the business model for the compact cutting machine business is similar to the business model for makers of game machines, whereby an increase in the sales of games leads to an increase in the number of associated customers, which supports greater sales of software, which increases profits.

Silhouette America extended its sales by 58.4% y-o-y to US\$50.09mn in FY6/14, and made a large contribution to the profits earned by the business. It greatly increased its sales of compact cutting machines and supplies and content for these machines, primarily through online sales channels, such as Amazon and through large hobby specialist stores.

● Design

In the design business, sales increased by 4.9% y-o-y to ¥4,845mn and operating profit grew 7.9% y-o-y to ¥771mn. Orders received for evaluating the earthquake-resistance of buildings were strong. The target for improving earthquake resistance is shifting from public facilities to large buildings in the private sector, so the demand for the services of the design business is likely to increase. However, sales and profits in this business are not likely to grow strongly because the business cannot rapidly increase the number of its construction engineers.

(b) Financial Condition

In FY6/14, the company's cash and deposits increased by ¥2,635mn, its sales and promissory notes receivable grew by ¥915mn, its inventories expanded by ¥733mn, and its intangible fixed assets declined by ¥163mn, mainly because its goodwill fell by ¥169mn, and its long-term investments and other long-term assets increased by ¥458mn. As a result of these changes, the company's total assets increased by ¥4,589mn to ¥37,621mn.

Total liabilities increased by ¥1,456mn in FY6/14 to ¥11,015mn. Among current liabilities, trade accounts and promissory notes payable grew by ¥821mn, while fixed liabilities increased by ¥548mn.

Total equity increased by ¥3,133mn in FY6/14 to ¥26,605mn. Retained earnings increased by ¥3,002mn, reflecting the addition of most of the company's net profit earned during the year. The company also posted a valuation gain of ¥132mn on its securities holdings. The company's equity ratio at the end of FY6/14 stood at 70.7%. Company management commented that it planned to use its ¥4,690mn of treasury stock (9,226,814 shares) at the end of FY6/14 for M&A in the future.

Summary Balance Sheet at 6/13 and 6/14

(Unit: ¥mn)

Account	FY6/13	FY6/14	y-o-y change
Cash & deposits	12,565	15,200	2,634
Sales and promissory notes receivable	4,706	5,621	914
Lease assets	701	785	84
Inventories	3,229	3,962	733
Other current assets	2,567	2,403	-164
Current assets	23,768	27,971	4,203
Tangible fixed assets	6,156	6,247	91
Intangible fixed assets	768	605	-163
Investments, etc.	2,339	2,797	458
Fixed assets	9,263	9,649	386
Total assets	33,032	37,621	4,588
Trade accounts and promissory notes payable	3,658	4,479	821
Taxes due	976	1,173	196
Other current liabilities	2,198	2,088	-110
Current liabilities	6,832	7,740	908
Fixed liabilities	2,727	3,275	548
Total liabilities	9,560	11,015	1,455
Shareholders' equity	23,625	26,626	3,001
Treasury stock	-4,688	-4,690	-2
Other comprehensive cumulative profit	-153	-20	133
Total equity	23,472	26,605	3,133
Total liabilities and equity	33,032	37,621	4,588

(c) Cash Flow

As shown in the table below, the company's operations provided ¥4,151mn of cash in FY6/14, while its investment activity used ¥430mn and its financing activity used ¥1,116mn. As a result, the balance of cash and cash equivalents increased by ¥2,626mn to ¥15,166mn.

Summary Cash Flow Statement for FY6/13 and FY6/14

(Unit: ¥mn)

	FY6/13	FY6/14
Cash flow from operations	3,937	4,154
Cash flow from investments	570	-430
Cash flow from financing	-920	-1,116
Change in cash & cash equivalents	3,755	2,625
Year-end balance of cash & cash equivalents	12,540	15,166

Company projects higher sales and profits for FY6/15, and upward revisions of these forecasts are likely

(2) Company Forecasts for FY6/15

For FY6/15, the management of Ai Holdings projects a 13.6% y-o-y increase in consolidated sales to ¥42,000mn, a 15.6% rise in operating profit to ¥7,400mn, a 14.4% upturn in recurring profit to ¥7,500mn, and an 18.7% rise in net profit to ¥4,800mn. The company consistently announces conservative forecasts, and given the current strength of the company's businesses, it will probably attain these forecasts. In fact, it will probably raise its forecasts.

Company Results in FY6/14 and Forecasts for FY6/15

	(Unit: ¥mn)					
	FY6/14		FY6/15E		y-o-y change	
	Amt.	Ratio	Amt.	Ratio	Amt.	Rate
Sales	36,976	100.0%	42,000	100.0%	5,024	13.6%
Operating profit	6,399	17.3%	7,400	17.6%	1,001	15.6%
Recurring profit	6,553	17.7%	7,500	17.9%	947	14.4%
Net profit	4,043	10.9%	4,800	11.4%	757	18.7%

The company's forecasts for its main businesses in FY6/15 are explained below.

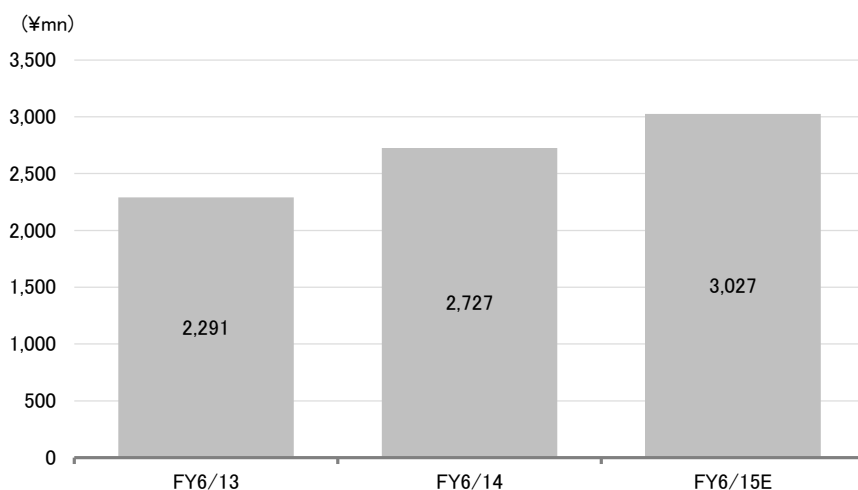
● Security Equipment

The company projects that operating profit from the security equipment business should grow by 11.0% y-o-y in FY6/15 to ¥3,027mn. It foresees obtaining 4,600 contracts for this equipment from condominium buildings in FY6/15, 3,000 new contracts and 1,600 contract renewals. It projects that its cumulative contracts with condominium buildings will reach 20,000 in November 2014.

A growing number of companies are installing security cameras, reflecting the impact of the previously mentioned incidents of toxins being introduced into the plant of a leading food processing company and of a large private educational services company leaking information about its customers. Furthermore, financial institutions that have already installed security equipment are increasing the number of cameras installed. Consequently, the company projects that sales of security equipment to corporations and institutions are likely to grow briskly in FY6/15.

Based on the number of new contracts with condominium buildings that the company projects for FY6/15, it appears that operating profit in the security equipment business could surpass the company's forecast.

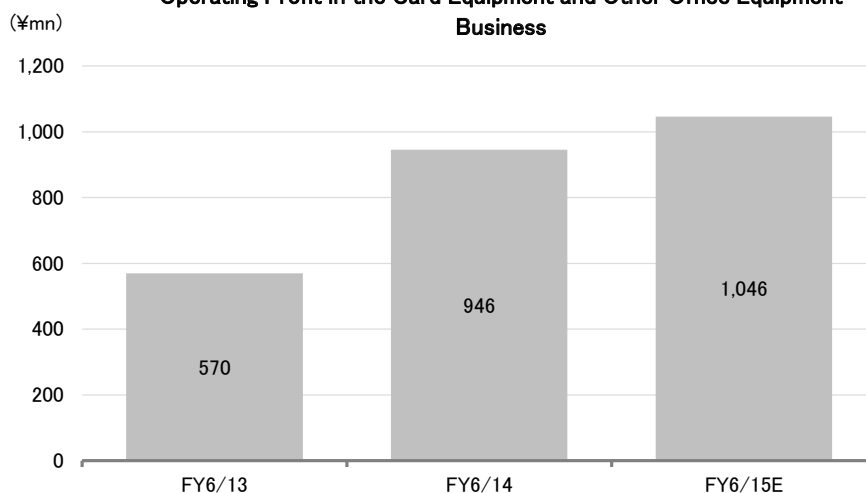
Operating profit in the Security Equipment Business



● Card Equipment and Other Office Equipment

The company forecasts a 10.6% y-o-y rise in operating profit from this business in FY6/15 to ¥1,046mn. Almost 90% of the sales of card machines to date have been to hospitals, for such purposes as issuing patient registration cards. Therefore, a large increase in sales of these machines is unlikely, but they should grow steadily. As mentioned earlier, sales of card machines to financial institutions have been growing recently because regional banks and large city banks have begun to install machines for the immediate issuance of cash cards. At the beginning of 2014, Ai Holdings received an order for card machines from a large city bank, and sales of these machines will be recorded in FY6/15.

Operating Profit in the Card Equipment and Other Office Equipment Business

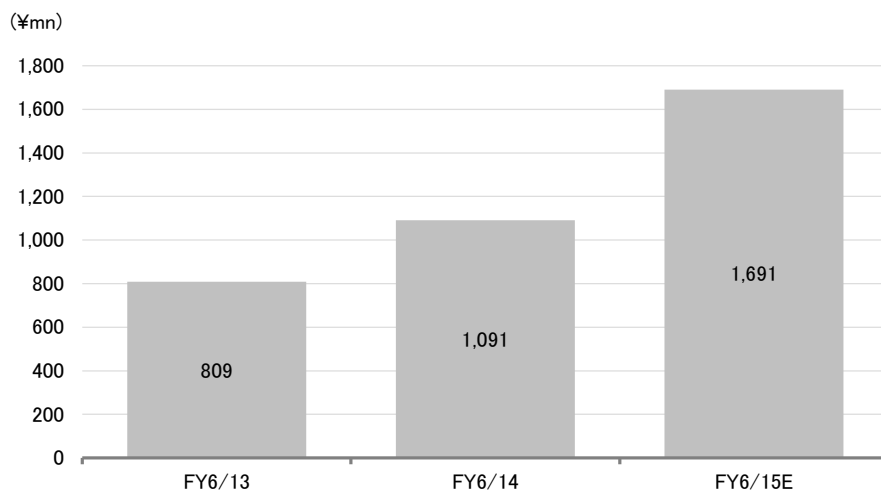


● Peripheral Computer Equipment

The company expects growth in this business to continue to be led by Silhouette America’s cutting machines for the consumer market. It projects that Silhouette America will raise its sales by 58.5% y-o-y I FY6/15 to US\$79.4mn and its operating profit by 56.9% to US\$13.1mn. The number of customers participating in Silhouette America’s association is increasing rapidly, contributing to greater sales of content for the company’s compact cutting machines. Furthermore, Silhouette America will launch sales of a new product, the CAMEO 2 cutting machine, this fiscal year, which should boost sales of compact cutting machines.

This fiscal year, the new business of producing label printers will be added to the peripheral computer equipment division, but the new business will probably not record sales until H2 FY6/15 and it will probably contribute little to profit this fiscal year. In FY6/14, R&D cost in the peripheral computer equipment division increased by ¥305mn y-o-y to ¥640mn, and this cost is likely to remain about ¥640mn in FY6/15 as the company is developing competitive next-generation equipment. Nonetheless, the company forecasts a 55.0% y-o-y rise in operating profit to ¥1,691mn in the peripheral computer equipment division for FY6/15.

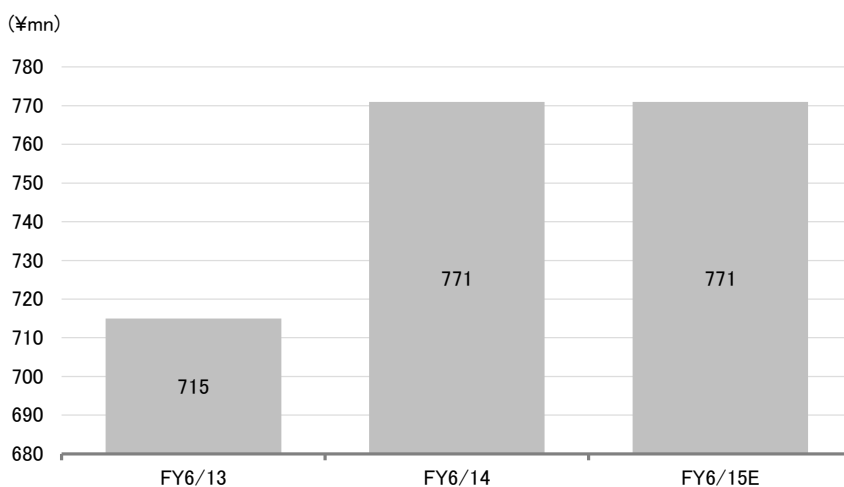
Operating profit in the Peripheral Computer Equipment Business



● Design

The company projects an operating profit of ¥771mn for the design business in FY6/15, unchanged from the operating profit earned in FY6/14. Accompanying legal changes, the company foresees an increase in the demand for the evaluation of the earthquake-resistance of large buildings in the private sector in FY6/14, whereas national government facilities have been the main source of demand previously. However, growth in this business will continue to be limited by the size of the workforce.

Operating profit in the Design Business



We believe that the company's forecasts for each of its businesses are conservative. The company routinely announces conservative forecasts, so there is a good chance that it will again surpass its current forecasts. However, FY6/15 results will depend on many factors, especially the development of the new label printer business.

■ Growth Prospects over the Medium-to-long Term

Profit growth to be led by the security equipment business, Silhouette America, and the label printer business

Ai Holdings lifted its consolidated operating profit from ¥2,980mn in FY6/11 to ¥6,399mn in FY6/14, and it will probably increase its operating profit more than this over the next three fiscal years because the two main drivers of profit growth in the past three years, the security business and Silhouette America, should expand their profits and their contributions will be supplemented by profit from the new label printer business.

(1) Security Equipment

● Condominium building market: new contracts alone provide significant growth potential

The security equipment business is concentrating on serving the condominium building market because, as explained below, the growth prospects in this market are promising and because it is more efficient to concentrate its management resources on a single market than to pursue many markets, since the business has limited resources compared to larger sellers of security equipment.

There is ample room for Ai Holdings to increase its sales of security equipment to existing condominium buildings. The company estimates that there are about 120,000 existing condominium buildings in Japan, and it expects to have installed its security equipment in about 20,000 of these buildings by November 2014. Even so, its market share will be only 16 – 17%. It aims to take share away from competitors and ultimately serve 60,000 existing condominium buildings.

● Contract renewals driving growth

Most of the security camera systems that Ai Holdings sells to condominium buildings are leased for a period of six years. The company claims that about 90% of its customers opt to renew their contracts at the end of a lease period, and it projects that most of its existing customers will extend their contracts in the future. Since FY6/12, contract renewals have accelerated the growth in the number of total contracts, as shown in the graph below.



●Sales to corporations and institutions also growing

Although the security equipment business specializes in serving condominium buildings, its sales to corporations and institutions have also been growing, as detailed earlier, and they are likely to increase hereafter.

▲Public facilities

Many crimes, such as robberies and random violence, are solved by analyzing the images captured by surveillance cameras. Therefore, public facilities, such as train and bus stations, airports, and event halls, will probably install more cameras in the future. For the same reason, semi-public facilities, such as commercial zones, downtown areas, parking lots, and condominium buildings, are likely to install more cameras.

▲Corporate facilities

Until recently, most of the companies that have installed security equipment have been small retailers, such as supermarkets and convenience stores. Recently, however, more companies in other industries have been installing surveillance cameras in their offices and plants following incidents of fraud at financial institutions, the intentional introduction of toxins into a food processing plant, and the stealing of personal information. In the past, many organizations and companies were reluctant to install surveillance cameras because of privacy concerns, but in recent years, these concerns have been subordinated to a concern about preventing crime. The security equipment business is benefiting from this shift of attitude.

US sales of small cutting machines for crafts and accompanying content strong, new product to be introduced this fiscal year

(2) Silhouette America (US peripheral computer equipment business)

●Company outline and business model

Silhouette America's main products are small cutting machines (priced at about ¥10,000–20,000 each) for crafts, supplies for these machines, such as blades, mats, and pens, and digital content, mainly designs, for the machines. The company is the largest supplier of digital content for crafts. Its primary markets are the craft market, educational institutions, retailers, and other markets.

Silhouette America manufactures its small cutting machines cheaply in China and Vietnam, so they can be sold at low prices, yet profitably. It organizes its customers into associations and offers them supplies for the machines and more than 57,000 designs for cut materials as of August 2014. When a user purchases a design online, he or she is charged each time he or she downloads it.

According to Silhouette America, digital content is its most profitable product and supplies for its cutting machines are also more profitable than the machines. The format of online data for cutting machines is not compatible with all cutting machines. Therefore, purchasers of Silhouette America's cutting machines benefit by buying online data from the company.



Ai Holdings

3076 Tokyo Stock Exchange
First Section

15-Oct.-14

● **Market size and prospects**

According to the US Craft & Hobby Association, the North American market for all crafts and hobbies amounted to US\$30.3bn (about ¥3.03trn) in 2011, while the combined markets for paper and memory crafts and for artistic crafts, which Silhouette America serves, was about US\$6.5bn (¥650bn). The Japanese market for paper crafts is probably not this large, but scrapbooking is a popular pastime among housewives in the US, and crafts are one of the three largest hobbies in the US, along with travel and sports.

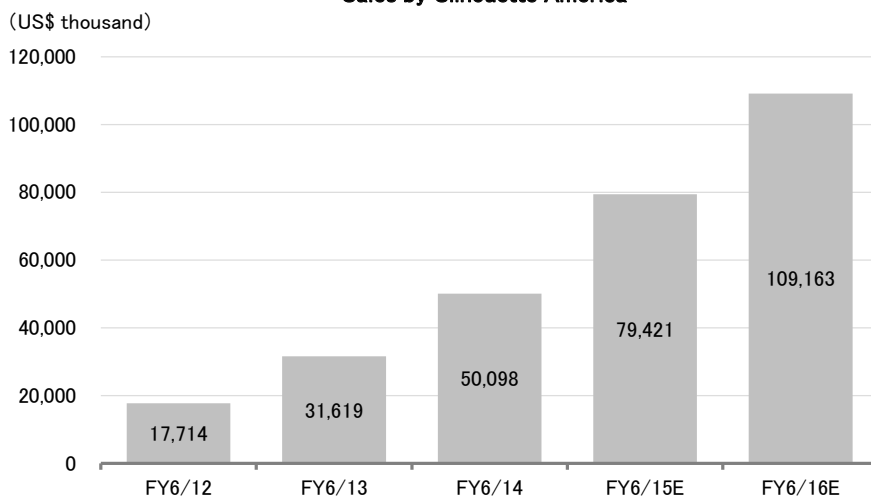
Many US housewives still cut out articles and photographs with scissors and paste them into scrapbooks manually, but a growing number are using personal computers and the cutting machines and designs provided by Silhouette America to produce scrapbooks of higher quality than traditional ones. Silhouette America has made most of its sales through leading teleshopping companies, mainly Amazon, but since December 2013, it has been selling on a full scale to hobby store chains with 1,000 or more stores in the US. Sales through hobby store chains should grow.

In a US\$6.5bn market, it is difficult to predict how many more housewives will switch from manual scrapbooking to machines and content offered by Silhouette America. However, Silhouette America's competitors have amassed annual sales of more than ¥20bn, and consumers who have purchased Silhouette America's products through Amazon evaluate the products highly on a daily basis. Therefore, it appears to have great growth potential.

● **Aiming to increase market share with a new cutting machine**

This fiscal year, Silhouette America plans to start selling a new model of small cutting machine, the CAMEO 2, a much improved version of its current machines. The CAMEO 2 is operated with an LCD touch panel screen, incorporates a USB memory, whereas previous machines have used SD cards, and includes a cross cutter. The company intends to attract more new customers with this machine and to replace previous models with it. Consequently, Ai Holdings projects sales of US\$109mn (about ¥10.9bn) for Silhouette America in FY6/16 (see bar chart below). This appears to be a reasonable target. The company estimates that Silhouette America may be able to achieve annual sales of ¥20bn ultimately.

Sales by Silhouette America



Entering label printer business this term

(3) New label printer business

In May 2014, Ai Holdings announced that it would enter the business of producing printers of full color industrial labels. It has developed a printer based on the combined technologies of full color printing using electro photography and cutting, acquired over many years as the world's top maker of cutting plotters. This is the world's first, full-scale printer of full color labels. The printers will be produced by Graphtec and will be considered part of the peripheral computer equipment business.

● Product outline

The printers are all-in-one systems for producing labels. They design the label data, print labels rapidly, laminate them, cut and finish them, and rewind them. They are priced at about ¥4mn each and possess the following characteristics.

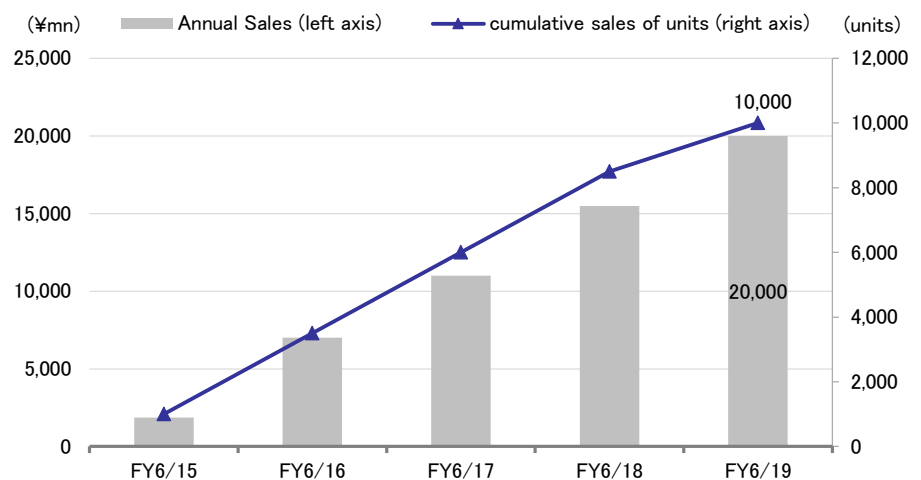
- Rapid delivery time: Since the printers integrate all production steps from label data design to final processing, they produce labels quickly.
- Unmatched label durability: Because color toner is used to print the labels, the labels remain legible despite exposure to water and chemicals more than labels produced by other methods. This is particularly true of GHS labels (see below).
- Low cost: The new printers are much cheaper than comparable printers now on the market
- Full after-sale support: The company will provide a complete line of support for the printers it produces.

● Target market and sales goals

The new printers can be used to print any kind of industrial label, but the company is mainly targeting labels that conform to the Globally Harmonized System (GHS) of Classification and Labeling of Chemicals. This system requires that all chemicals be clearly labeled with the amounts and danger of each component. Japan has already adopted this system and the US and EU plan to implement it fully in 2015.

GHS labels have to remain legible despite exposure to water and chemicals, so the new printers are ideal for producing them. Graphtec plans to sell its new printers primarily to Japanese and US chemical companies. It projects annual sales of ¥20bn in FY6/19, when it foresees cumulative sales of 10,000 units (see bar chart below).

Projected Annual Sales and Cumulative Sales of Label Printers



¥10bn operating profit achievable in FY6/17

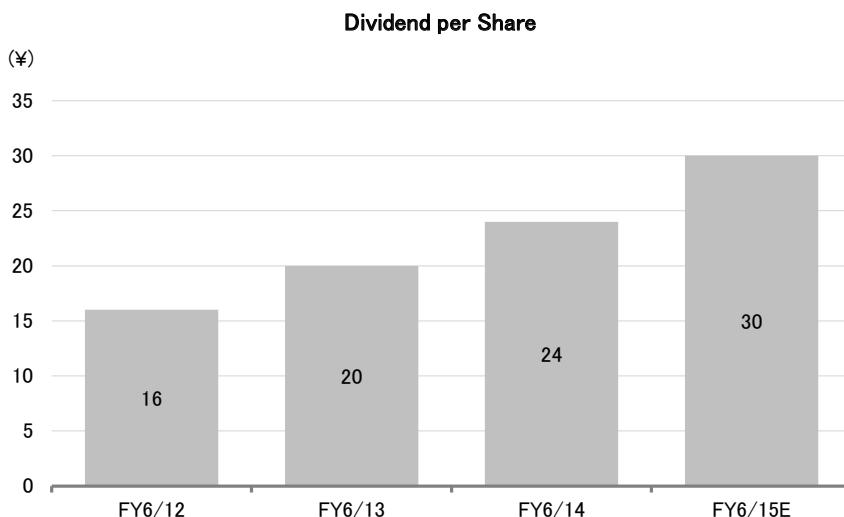
(4) Medium-term Profit Target

The company has never before set quantitative targets for its medium-term plans, but CEO Sasaki has stated that the company could achieve an operating profit of ¥10bn in FY6/17. This projection seems credible for several reasons. None of the company's current businesses are declining. In fact, the security equipment business and Silhouette America remain growth drivers. Finally, the new label printer business is likely to become a third growth driver.

■ Shareholder Return Policy

To keep a 30% dividend payout ratio, the company is likely to raise its dividend as its profits grow

Ai Holdings basically plans to maintain a dividend payout ratio of at least 30%. Based on this principle, it paid a dividend of ¥24 per share for FY6/14, up from ¥20 for FY6/13 and ¥16 for FY6/12, and it plans to pay a dividend of ¥30 per share for FY6/15 (see bar chart below). If its profits grow more than it forecasts for FY6/15, it may pay a dividend of more than ¥30 per share. In addition, it will probably increase its dividend as its profits grow in coming years.



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