FreeBit Co., Ltd.
3843 Tokyo Stock Exchange First Section

10-Jan.-17

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FISCO Ltd. Analyst
Hideo Kakuta

Upbeat Momentum on Steady Growth in Mobile and Ad Technology Businesses, Entering the Health Tech Field After Acquiring EPARK Healthcare as a Consolidated Subsidiary

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

Tone mobile inc., a joint venture with Culture Convenience Club Co., Ltd. (hereafter, “CCC”) and equity-method affiliate of the Company, is currently focusing on expansion of smartphone business, including through provision of TONE proprietary smartphone service. The Company’s listing was reassigned to the First Section of the Tokyo Stock Exchange in July 2016.

In 1H FY4/17 consolidated results (May-Oct 2016), the Company reported sharply higher net sales and operating income with gains of 40.1% y-o-y in net sales to ¥18,689mn, 32.3% in operating income to ¥1,118mn, and 41.9% in ordinary income to ¥839mn and a 12.1% decline in profit attributable to owners of parent to ¥192mn. Primary drivers of the steep sales increase exceeding 40% were healthy advances in the Mobile Business and Ad Technology Business. Operating income benefited from a large gain in Ad Technology Business profits. Ordinary income posted a 41.9% increase thanks to the steep upturn in operating income offsetting a larger equity-method investment loss related to expansion of the Tone mobile business. The decline in profit attributable to owners of parent is temporary and reflects a rise in the corporate tax and other adjustments value compared to the previous fiscal year and non-recurrence of the previous year’s profit from selling a fixed asset.

Progress rates in 1H toward FY4/17 guidance (¥35,000mn in net sales, ¥2,000mn in operating income, and ¥250mn in profit attributable to owners of parent) are 53.4% in net sales, 55.9% in operating income, and 76.8% in profit attributable to owners of parent. These levels are well above the same term of previous year and indicate upbeat momentum in recent results. We think the Company is clearly on track to attaining FY4/17 targets via effective portfolio management with the Broadband Business, Ad Technology Business, and Cloud Business generating profits and the Mobile Business driving growth and steady additions to net sales and profits in all of areas because of the repeat nature of these businesses.

Health Tech*3 is a major focus area in the SiLK VISION 2020 medium-term business policy. The Company acquired shares in EPARK Health Care, Inc., a subsidiary of HIKARI TSUSHIN, INC. <9435> Group’s EPARK, Inc. that offers a range of services targeting the pharmacy industry that includes operation of the EPARK Kusuri-No-Madoguchi comprehensive pharmacy portal site, and converted this entity to a consolidated subsidiary in September 2016. This initiative aims to enhance the media platform that connects end users (patients) and pharmacies using FreeBit Group’s technology capabilities and provide information as well as highly convenient reservation and delivery services to help pharmacies with end-user retention. While the service already has a network of about 8,000 pharmacies, the market still offers substantial opportunities considering the roughly 58,000 pharmacies that exist nationwide. The business is currently in an investment phase and allocating funds to pursuit of sustained growth in media PV, customer draw, and alliance pharmacy volumes. The Company expects a loss for this business in 2H. It consolidated the balance sheet at the 2Q and plans to consolidate income from 3Q.

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

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

*3 Aims to drive reforms in the health care field through “health x IT” and create a next-generation health management method.

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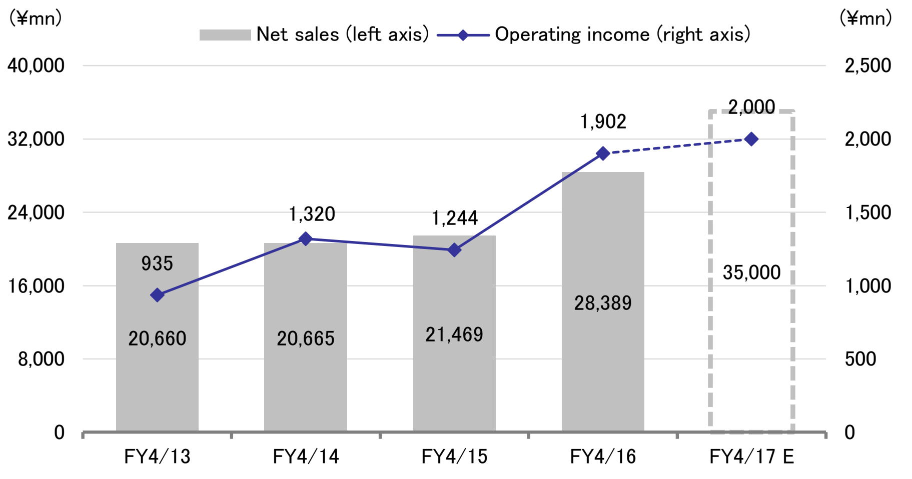
Check Point

- Achieving steady growth in the Mobile Business and Ad Technology Business and posted sharply higher net sales and operating income in 1H FY4/17
- Progress rates in 1H toward FY4/17 guidance at 53.4% in net sales and 55.9% in operating income, clearly on track to attaining full-year target with support from having many businesses with repeat income
- Acquired EPARK Health Care as a consolidated subsidiary in September 2016 and actively investing in development of a media platform in the Health Tech field

Results trends



Financial results trends

Achieving steady growth in the Mobile Business and Ad Technology Business and posted sharply higher net sales and operating income in 1H FY4/17

(1) 1H FY4/17 consolidated results

In 1H FY4/17 consolidated results, the Company reported sharply higher net sales and operating income with gains of 40.1% y-o-y in net sales to ¥18,689mn, 32.3% in operating income to ¥1,118mn, and 41.9% in ordinary income to ¥839mn and a 12.1% decline in profit attributable to owners of parent to ¥192mn.

Review of consolidated results for 1H FY4/17

(¥mn)

	FY4/16 1H		FY4/17 1H		
	Result	Relative to sales	Result	Relative to sales	y-o-y change
Net sales	13,344	-	18,689	-	40.1%
Cost of sales	9,421	70.6%	14,349	76.8%	52.3%
Gross profit	3,922	29.4%	4,339	23.2%	10.6%
SG&A expenses	3,077	23.1%	3,221	17.2%	4.7%
Operating income	844	6.3%	1,118	6.0%	32.3%
Ordinary income	591	4.4%	839	4.5%	41.9%
Profit attributable to owners of parent	218	1.6%	192	1.0%	-12.1%

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

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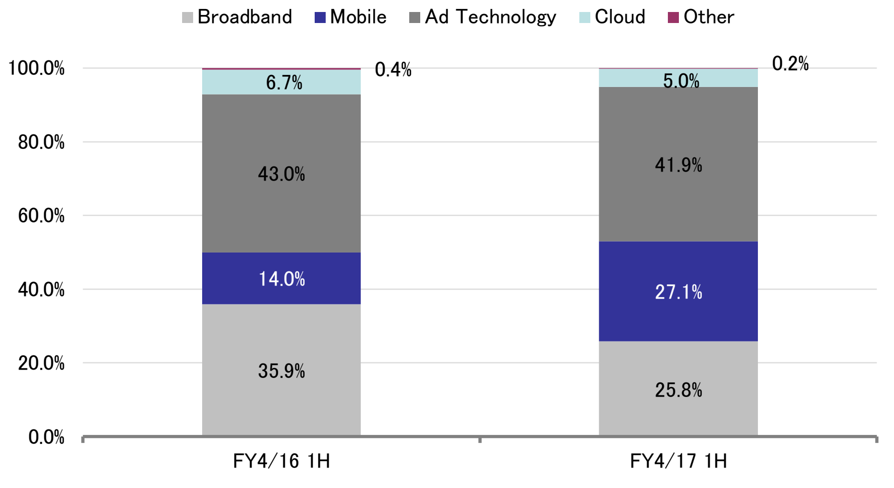
Primary drivers of the steep sales increase exceeding 40% y-o-y were healthy advances in the Mobile Business (sales gains of ¥1,491mn in freebit MVNO Pack/SIM and other products and ¥1,714mn in smartphone handsets) and Ad Technology Business (sales increase of ¥2,087mn at Full Speed Inc. <2159> Group). Gross profit margin dropped by 6.2 percentage points from the previous year's 29.4% to 23.2% because of an increase in cost of sales by 52.3% to ¥14,349mn because of higher network-related costs. While SG&A expenses rose 4.7% to ¥3,221mn due to higher personnel expenses and other spending related to expansion of business scale, the SG&A expenses ratio fell by 5.9 percentage points to 17.2% because expense growth was slower than sales expansion and advertising/promotional costs and sales promotion costs declined on lower fixed-line network customer acquisition incentives. Operating income hence increased 32.3%. It benefited from a large gain in Ad Technology Business profits.

Ordinary income posted a 41.9% y-o-y increase thanks to the upturn in operating income offsetting a larger equity-method investment loss related to expansion of the Tone mobile business. The decline in profit attributable to owners of parent reflects a rise in the corporate tax and other adjustments value compared to the previous fiscal year and a one-time impact from non-recurrence of the previous year's profit from selling a fixed asset (specifically, BEKKOAME INTERNET, Inc.'s sales of the Kaminarimon Building).

○ **Segment conditions**

The segment sales breakdown consists of the Broadband Business at 25.8% (vs. 35.9% in the previous year), Mobile Business at 27.1% (vs. 14.0%), Ad Technology Business at 41.9% (vs. 43.0%), and Cloud Business at 5.0% (vs. 6.7%). Mobile Business significantly increased its presence in overall sales on contributions from smartphone handsets and freebit MVNO Pack.

Percentages of net sales by segment

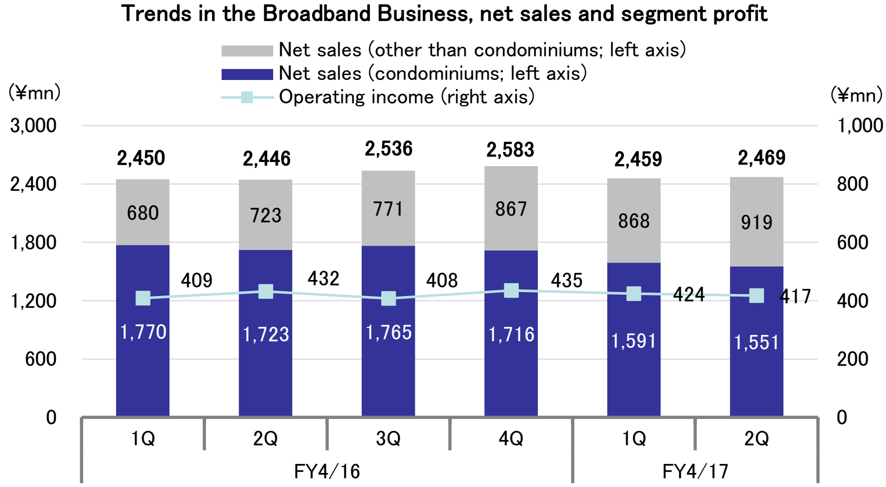


Source: Prepared by FISCO Ltd. from the Company's financial results summary

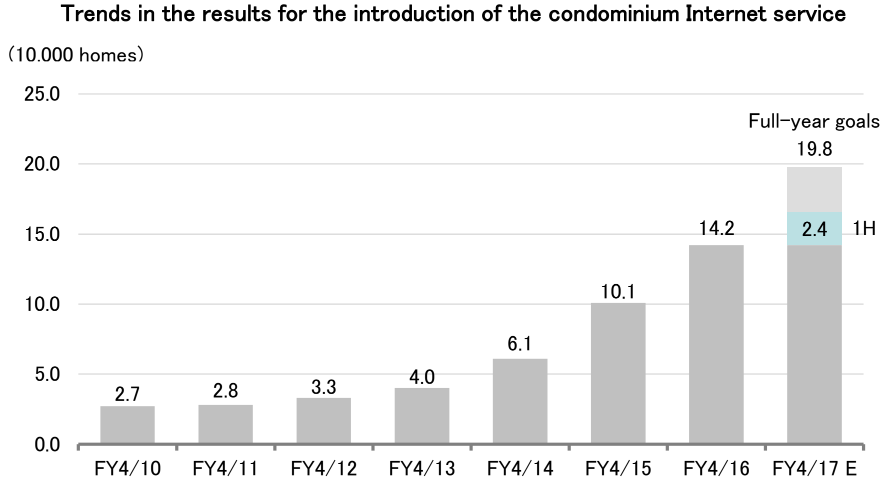
a) Broadband Business

The Broadband Business delivered slightly higher net sales and profits in 1H FY4/17 with increases of 0.7% y-o-y to ¥4,929mn in net sales and 0.1% to ¥842mn in segment profit. Segment profit improved on higher profit linked to stronger sales in GIGAPRIZE Co., Ltd.'s <3830> Internet service for condominiums (up ¥168mn) and a boost from healthy expansion of Internet service for individuals with successful Hikari Collaboration measures at DREAM TRAIN Internet INC. (below, DTI) (up ¥106mn). Installations are accelerating in the Internet service for condominiums thanks to beginning collaboration with multiple top-tier home builders, and cumulative installations were up by 24,000 units from the end of FY4/16 to 166,000 units at end-1H FY4/17 and made steady progress toward the end-FY4/17 target of 198,000 units. A major setback, meanwhile, was the decline in sales for existing fixed lines (down ¥221mn). While network-related costs are trending upward, operating income remains healthy with support from the growing Internet service for condominiums.

■ Financial results trends



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

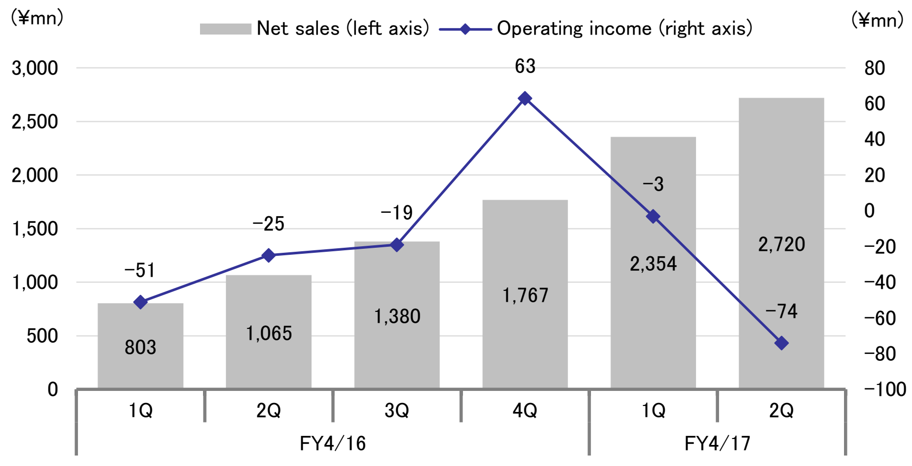


Source: Prepared by FISCO from the Company's financial results briefing materials

b) Mobile Business

Net sales in the Mobile Business rose sharply in 1H with an increase of 171.5% y-o-y to ¥5,074mn. Key drivers were 1) healthy user acquisitions by U-NEXT Co., Ltd. <9418> and other MVNO operators that use freebit MVNO Pack and expansion of MVNO bandwidth wholesale business, 2) upbeat prepaid SIM sales and router rentals to foreign tourists visiting Japan (prepaid SIM sales since February 2015 surpassed 710,000 units), 3) steady user growth in DTI's DTI SIM mobile high-speed data communications service for individuals fueled by new plans and campaign activities, and 4) expansion of the number of stores, including TSUTAYA and others, selling equity-method affiliate Tone mobile's TONE m15 smartphone handsets to 55 sites and increases in handset shipments and bandwidth sales. While net sales moved sharply higher, many of the services are still in rollout and early growth phases and require forward investments to launch operations and raise market share. Segment loss recorded a ¥78mn (vs. a ¥76mn loss in the previous year; -1.5% operating margin). Profitability is within reach, though income fell in 1H.

Net sales and segment profit/loss trends in the Mobile Business



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

c) Ad Technology Business

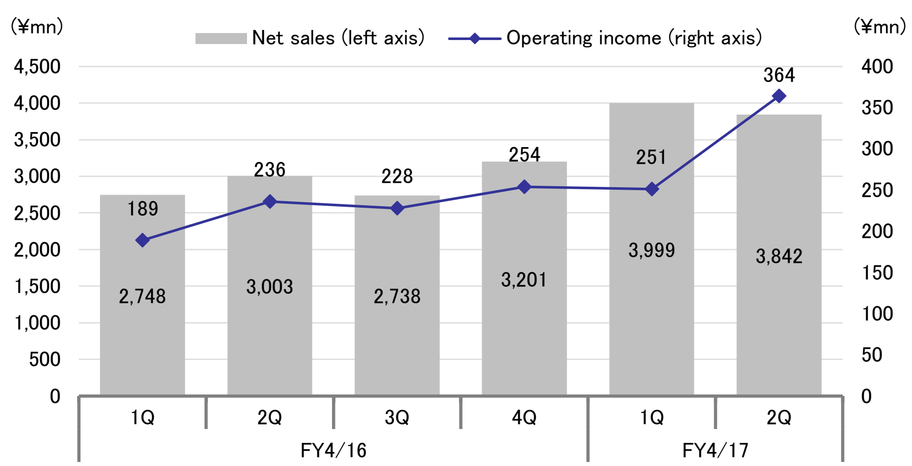
The Ad Technology Business generated sharply higher net sales in 1H with a 36.3% y-o-y increase to ¥7,841mn. Segment profit climbed 44.4% to ¥615mn, even with the negative impact of higher personnel expenses, SG&A expenses, and provision of an allowance for doubtful accounts by the Full Speed Group, thanks to the large profit contribution from stronger sales. The Company increased new deal volume recruited through distributors in the AdMatrix proprietary advertising management comprehensive platform, a focus area, thanks to increases in distributors and closer collaboration. Affiliate-service "Affiliate B" *2, an affiliate service provider (ASP)*1, is highly rated for its unique functionality and was selected as the No.1 ASP in media usage satisfaction for a second straight year. The Company also plans to establish an offshore development site on Cebu Island (Philippines) to bolster its development base, a medium-term business policy, in January 2017. It intends to accelerate developments of proprietary ad technology content, Go Japan*3 media for visitors, and other future strategies.

*1 Service provider that distributes ads with performance-based fees

*2 Network of over 550,000 partner sites. Utilizing PC knowhow to deploy services to tablets, smartphones, and mobile devices

*3 Has over 600,000 download users (mainly Chinese people). App that supports pre-trip planning to searches and information provision (distribution) during visits with the aim of maximizing enjoyment of Japan by visitors

Net sales and segment profit trends in the Ad Technology Business



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Progress of Ad Technology Business

AffiliateB

Affiliate B affiliate platform
No.1 ASP in media usage satisfaction

Satisfaction rate by ASP, user satisfaction

*Affiliate Marketing Association (NPO)

FORiT's affiliate-platform Affiliate B, which marked 10 years since the service launch on 22 November, 2016, selected as the No.1 ASP in media usage satisfaction

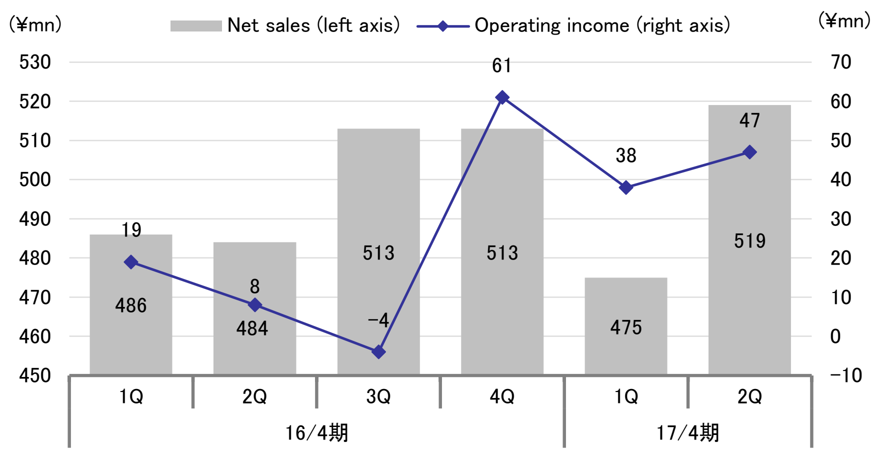
Source: The Company's financial results briefing materials

d) Cloud Business

The Cloud Business reported a 2.5% y-o-y rise in net sales to ¥994mn and a steep 203.8% gain in segment profit to ¥86mn in 1H. While net sales continued to face pressure from revisions to housing, hosting, and other legacy services, segment income rose significantly as higher hybrid cloud* and content sales offset the impact.

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

Net sales and segment profit trends in the Cloud Business



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Progress rates in 1H toward FY4/17 guidance at 53.4% in net sales and 55.9% in operating income, clearly on track to attaining full-year target with support from having many businesses with repeat income

(2) FY4/17 outlook

Progress rates in 1H toward FY4/17 guidance (¥35,000mn in net sales, ¥2,000mn in operating income, and ¥250mn in profit attributable to owners of parent) are 53.4% in net sales, 55.9% in operating income, and 76.8% in profit attributable to owners of parent. These levels are well above the previous year (47.0%, 44.4%, and 39.5% respectively) and indicate upbeat momentum in recent results.

Progress rates through 1H and review of FY4/17 guidance

(¥mn)

	FY4/16			FY4/17						
	1H Result	Relative to sales	Progress rate	1H Result	Relative to sales	y-o-y change	Progress rate	Target	Relative to sales	y-o-y
Net sales	13,344	-	47.0%	18,689	-	40.1%	53.4%	35,000	-	23.3%
Broadband	4,897	36.7%	48.9%	4,929	26.4%	0.7%	44.6%	11,041	31.5%	10.2%
Mobile	1,868	14.0%	37.3%	5,074	27.2%	171.5%	60.0%	8,451	76.5%	68.5%
Ad Technology	5,751	43.1%	49.2%	7,841	42.0%	36.3%	55.6%	14,099	40.3%	20.6%
Cloud	970	7.3%	48.6%	994	5.3%	2.5%	52.4%	1,899	5.4%	-4.9%
Operating income	844	6.3%	44.4%	1,118	6.0%	32.3%	55.9%	2,000	5.7%	5.1%
Broadband	841	17.2%	49.9%	842	17.1%	0.1%	56.4%	1,493	13.5%	-11.4%
Mobile	-76	-4.1%	-	-78	-1.5%	-	-	92	1.1%	-
Ad Technology	426	7.4%	46.9%	615	7.8%	44.4%	53.9%	1,110	7.9%	22.2%
Cloud	28	2.9%	33.2%	86	8.7%	203.8%	110.1%	78	4.1%	-8.4%
Ordinary income	591	4.4%	44.7%	839	4.5%	41.9%	56.0%	1,500	4.3%	13.4%
Profit attributable to owners of parent	218	1.6%	39.5%	192	1.0%	-12.1%	76.8%	250	0.7%	-54.8%

Note: Segment profit ratios to net sales are segment profit margins
Source: Prepared by FISCO Ltd. from the Company's financial results summary and financial results briefing materials

We think the Company is clearly on track to attaining FY4/17 targets due to 1) 1H progress rates at healthy levels that outpaced the previous year, 2) effective portfolio management with the Broadband Business, Ad Technology Business, and Cloud Business generating profits and the Mobile Business driving growth, and 3) steady additions to net sales and profits in all of areas because of the strong repeat nature of these businesses. We expect a negative impact on operating income from consolidating income at EPARK Health Care (explained below) from 3Q because this business is still in an investment phase, but believe it should be within a range that can be offset by upside through 1H and profit increases in other businesses.

Growth strategy

Acquired EPARK Health Care as a consolidated subsidiary and actively investing in development of a media platform in the Health Tech field

○ **Entry into media business**

The Company announced SiLK VISION 2020, a four-year medium-term business policy, in June 2016. This plan, which targets ¥500mn in net sales and ¥50mn in operating income in FY4/20, calls for ongoing growth in upbeat existing businesses (Mobile Business and Ad Technology Business) and business expansion in life-related areas (focusing on Health Tech, IoT, and Real Estate Tech).

Health Tech is one of the three focus areas, and the Company acquired shares (47.5% of voting rights) in EPARK Health Care, Inc., a subsidiary of HIKARI TSUSHIN, INC. <9435> Group's EPARK, Inc. that offers a range of services targeting the pharmacy industry that includes operation of the EPARK Kusuri-No-Madoguchi comprehensive pharmacy portal site, and converted this entity to a consolidated subsidiary in September 2016. This initiative aims to enhance the media platform that connects end users (patients) and pharmacies using FreeBit Group's technology capabilities and provide information as well as highly convenient reservation and delivery services to help pharmacies with end-user retention. While the service already has a network of about 8,000 pharmacies, the market still offers substantial opportunities considering the roughly 58,000 pharmacies that exist nationwide. Income sources include media-driven advertising income, fees from patient transfers, and reservation system usage fees. The business is currently in an investment phase and allocating funds to pursuit of sustained growth in media PV, customer draw, and alliance pharmacy volumes. The Company expects a loss for this business in 2H. It consolidated the balance sheet at the 2Q stage and plans to consolidate income from 3Q.

Media Business

- **Starting consolidation of EPARK Health Care income from 3Q after completion acquisition as a subsidiary in September 2016** by purchasing its shares (47.5% of voting rights)
- Expecting a loss in 2H due to being in an investment phase, **though aims to continue growth in media PV, customer draw, and alliance pharmacy volumes**

freebit　EPARK ヘルスケア
EPARK くすりの窓口　処方便　EPARK お薬手帳　みんなのお薬箱

Source: Company materials

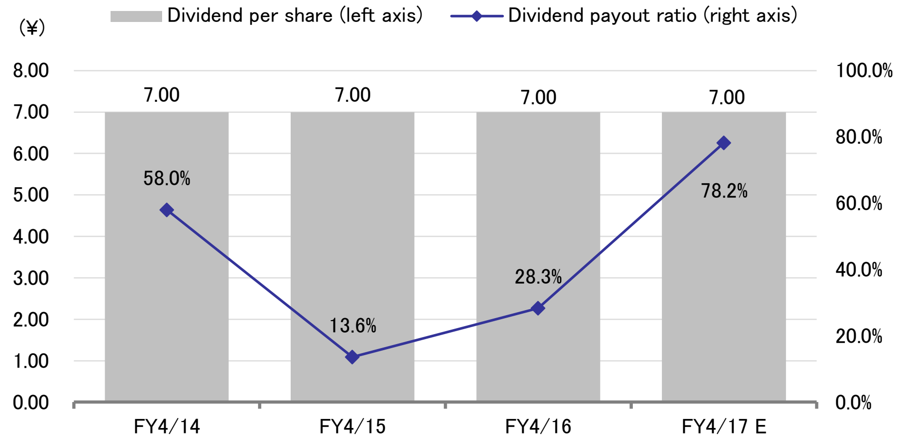
The Company intends to prepare for provision of new services utilizing group technology capabilities and business resources and make seed investments that target future global trends. We will be looking for clarification of activities in IoT and Real Estate Tech areas too.

Returning Profits to Shareholders

Shareholder returns utilize a stable dividend and share buybacks

The Company focuses on reinforcing internal reserves, investing to expand businesses, and continuation profit returns to shareholders. It plans to pay a ¥7 dividend in FY4/17, on par with the previous year, putting the dividend payout ratio at 78.2%. It also conducted share buybacks three times in the past, including FY4/16, and might purchase shares again this time to boost value per share and to implement dynamic capital policy that addresses changes in the business environment.

Dividend per share and dividend payout ratio



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