Hottolink,Inc.
3680 TSE Mothers

12-Apr.-16

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Plans for active investment, including M&As, for Asian development in FY12/16

Hottolink (3680) (hereafter, also "the Company") is developing businesses centered on a cloud service that provides useful information for corporate marketing strategies and risk management by gathering and analyzing data posted on Twitter, blogs, and other social media. In January 2015, Hottolink made U.S. company Effyis.inc. (hereafter, Effyis) a subsidiary, establishing its position as the world's leading social big data distribution company.

In the consolidated results for FY12/15 (January to December 2015), net sales increased by 2.4 times year on year (yoy) to ¥2,439mn, and operating income rose 11.0% to ¥126mn, primarily due to Effyis becoming a subsidiary. Compared to the increase in net sales, the growth in operating income seems low, but this was mainly due to the increases in M&A related costs and depreciation and amortization expenses in conjunction with Effyis becoming a subsidiary, and EBITDA (operating income before amortization) rose 2.3 times yoy to ¥488mn, for a major increase in earnings.

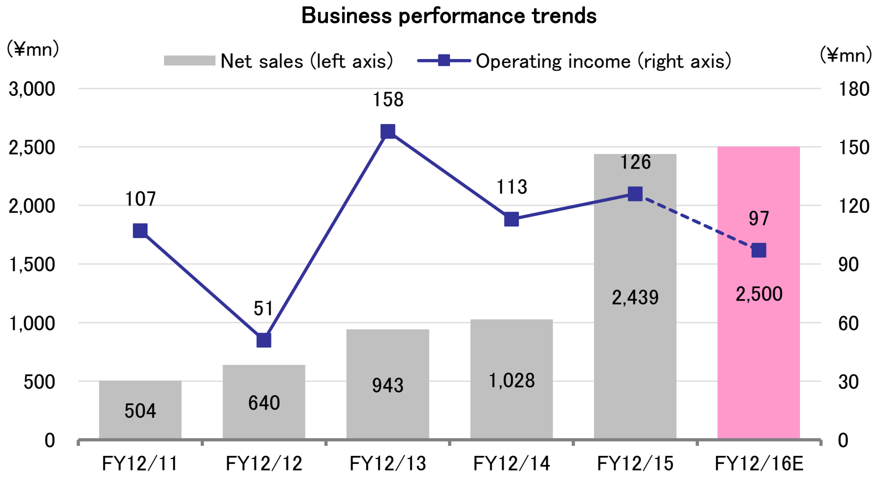
The Company is forecasting conservative results for FY12/16, with net sales to rise 2.5% yoy to ¥2,500mn, but operating income to decline 22.9% to ¥97mn. This is because it is planning active investment, including M&As, for Asian development in FY12/16, so results may vary depending on how this plan develops.

The Company's medium-term targets for FY12/20 are net sales of ¥10.0bn, with an overseas sales ratio of 80%. The strategy is to develop domestically and overseas its trend analysis service for inbound consumption. Specifically, in 2016 the Company will horizontally develop its Visualized China Trend EXPRESS service to Asia, and launch domestically the service to analyze the consumption trends of non-Chinese tourists. In addition, in 2017 Hottolink plans to expand its service to Asia to analyze consumption trends of non-Chinese tourists. The Company will need to invest around ¥800mn in these businesses, and as the funds for this, it issued new shares and share acquisition rights in January 2016 through a third party allocation, from which Hottolink is scheduled to raise a total of ¥1,600mn.

The utilization of social big data is becoming increasingly important within companies' management strategies, and the Company has great prospect for developing this business from a domestic to a global one. The Company is currently in a phase of upfront investment, but it is steadily building the business foundations toward future growth, and future developments will probably attract attention.

Check Point

- Established its position as the world's largest social media distribution company
- Major increase in sales while making Effyis a subsidiary and steadily launching new services
- Business development in FY12/16 from the launch of "social media × tourism"



*Consolidated figures from FY12/13
*FY12/14 and FY12/15 results, and the FY12/16 results forecasts, are based on IFRS

Business overview

Established its position as the world's largest social media distribution company

(1) Business description

Hottolink has developed tools for gathering and analyzing postings on a variety of social media, such as Twitter, 2channel, Weibo, and various blogs. It provides services that put this information to good use in corporate marketing strategies, risk management, and other functions.

Looking at Hottolink's core services, in the SaaS* Business, the Company offers services such as kuchikomi@kakaricho and e-mining, for which it enters into license agreements with customers. In the Solution Business, Hottolink provides analysis tools and data to systems integrators and tool vendors, along with Visualized China Trend EXPRESS, which is an inbound tourism consumption analysis report service. Moreover, the Solution Business also includes the business of Effyis, which the Company made into a subsidiary in January 2015. Each business segment is described below.

○ **SaaS Business**
The SaaS Business is comprised of two services; kuchikomi@kakaricho, which is a social big data analysis tool, and e-mining, which is a risk monitoring tool. The price structure for each of these services consists of an initial registration fee of ¥100,000 and a monthly usage fee, starting from ¥100,000 for kuchikomi@kakaricho and ¥130,000 for e-mining. The monthly usage fee is calculated based on the number of usable IDs, the number of media subject to analysis, data capacity, and other factors. Some large corporate customers spend up to ¥1mn a month on usage fees.

The number of corporate subscribers is over 1,900 for the two services combined on a cumulative basis (over 900 for kuchikomi@kakaricho and over 1,000 for e-mining). Of these, there are currently approximately 500 active corporate subscribers. The industry breakdown shows that the corporate subscribers span a wide range of sectors, from consumer goods manufacturers to the services and finance sectors. Approximately 80% of the corporate users are major corporations.

kuchikomi@kakaricho has the following features. It possesses Japan's largest social media coverage and it is easy to operate and to perform real-time searches, such as trend analysis and attribute analysis. It also has functions such as cross-media analysis spanning television, web news sites, and other media, plus a data import analysis function to perform text mining of data held internally by corporate customers (questionnaires and call logs, etc.)

* SaaS (Software as a Service): A software service in which software is provided to customers over communication networks. Customers are able to use the software when needed by accessing the network. It is a stock-type business model that generates recurring revenues from a fixed customer base by collecting monthly usage fees.

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Notably, Hottolink has a dominant advantage in Japan in terms of the sheer volume of social data it possesses and covers approximately 90% of all blogs in Japan. In addition, the Company holds all historical data on the 2channel bulletin board site and has entered into a marketing agency agreement with Gnip, Inc., which markets Twitter data worldwide.

The kuchikomi@kakaricho tool can be applied promptly to a company's marketing initiatives through real-time features such as trend analysis. For this reason, kuchikomi@kakaricho is being steadily adopted primarily by major corporations as a support tool that helps to improve return on investment (ROI) for marketing departments.

Meanwhile, e-mining is a tool that automatically collects data from Twitter, 2channel, and other sources according to pre-set risk-related keywords. The e-mining service provides alert functions that enable companies to promptly detect any developments of risk. Monitoring covers approximately 2,000 media and goes beyond 2channel and Twitter, extending to blogs and various news sites. Each day, e-mining monitors approximately 13 million web pages and reports the search results by category.

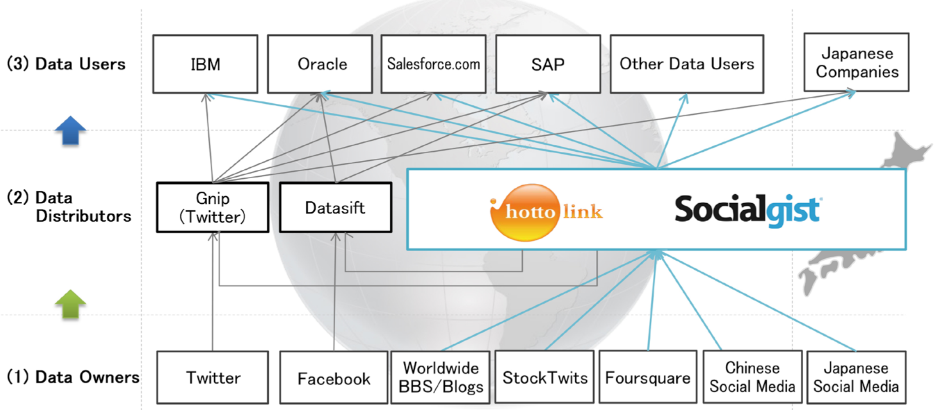
Recently, there has been a notable increase in incidents, such as food contamination problems, in which rumors and statements on issues have spread via postings on social media. So there is a growing need to promptly identify these risks and to implement response measures at an early stage. Accordingly, e-mining is being adopted primarily by major corporations.

○ **Solution Business**

The Solutions Business is comprised of the social media data sales business of Effyis (brand name: Socialgist), which was made into a subsidiary in January 2015, and the service to analyze the consumption trends among foreign tourists to Japan developed by its subsidiary Trend Express. The Solution Business also includes the data platform service that provides systems integrators and other customers with the data and analysis engines that make up kuchikomi@kakaricho.

Effyis collects social big data from sources such as blogs, bulletin boards, Q&A, and review sites worldwide, which it sells to customers that include the world's major social big data analysis firms and marketing platforms, as well as business intelligence (BI) and other tool vendors. Effyis particularly possesses overwhelming strength in social big data in China; for example, it is the world's only company to acquire a marketing license with full access rights to the data of a Chinese social media major. Effyis' main clients include global IT companies such as Salesforce.com and IBM, and it also has a track record of sales to financial and government institutions.

Sales of social big data



Source: Company materials

Also, within the services to analyze the consumption trends of foreign tourists to Japan, in May 2015 the Company launched the Visualized China Trend EXPRESS service, which analyzes the consumption trends of Chinese tourists to Japan for a monthly fee of ¥80,000. Hottolink also provides customized research services according to the needs of customers.

(2) Hottolink's strengths

Hottolink's strength lies in having established its position as the world's leading social media distribution company through making Effyis a subsidiary. In addition, by combining its world class big data analysis technologies with Effyis' advanced data streaming technologies, it has put a system in place for providing even more advanced analysis services.

Financial results trends

Major increase in sales while making Effyis a subsidiary and steadily launching new services

(1) Overview of financial results in FY12/15

In the FY12/15 consolidated results that the Company announced on February 12, net sales increased 2.37 times yoy to ¥2,439mn, operating income grew 11.0% to ¥126mn, income before income taxes decreased 57.1% to ¥60mn, and net income attributable to the owners of the parent company fell 75.4%. Through the inclusion of Effyis' results, both sales and profits increased to the extent that an operating income was recorded. But income before income taxes declined, mainly due to the deterioration of financial income in order to cover the borrowing for the acquisition of Effyis (¥2,695mn). In conjunction with the change in accounting standards in this fiscal year from Japanese accounting standards to IFRS (International Financial Reporting Standards), the results from the previous fiscal year have also been converted to IFRS for the comparisons.

FY12/15 consolidated results

(unit: ¥mn)

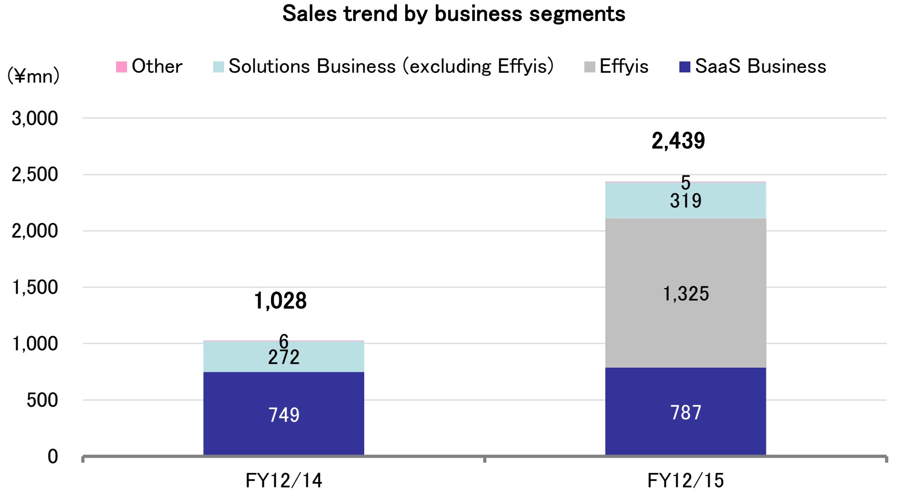
	FY12/14		FY12/15			
	Actual	Relative to sales	Initial target	Actual	Relative to sales	y-o-y change
Net sales	1,028	-	2,423	2,439	-	137.3%
Cost of sales	435	42.3%	-	1,190	48.8%	173.7%
SG&A expenses	460	44.8%	-	1,121	46.0%	143.5%
Operating income	113	11.0%	208	126	5.2%	11.0%
Income before income taxes	140	13.7%	-	60	2.5%	-57.1%
Net income attributable to the owners of the parent company	76	7.5%	106	18	0.8%	-75.4%
EBITDA	213	20.8%	-	488	20.0%	128.8%

Note: EBITDA is calculated as operating income + amortization

The main factors behind the increase in net sales was the contribution of ¥1,325mn from Effyis after it was made a subsidiary, and that sales from existing businesses rose 8.3% yoy to ¥1,113mn. Within the existing businesses, the SaaS Business is making progress in acquiring new customers from the effects of releasing new versions of kuchikomi@kakaricho and e-mining with improved functions, and its sales trended strongly, rising 5.1% to ¥787mn. In addition, within the Solutions Business, sales from the existing business excluding the contribution of Effyis increased by double digits, by 17.4% to ¥319mn. This was mainly due to the steady launch of new services to analyze the inbound consumption trends of Chinese tourists.

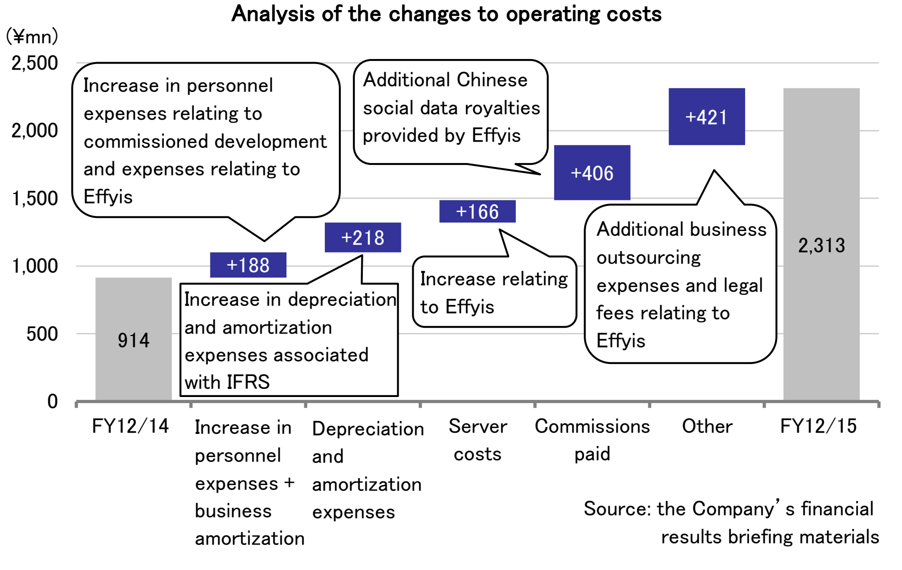
Effyis net sales increased in the region of 10% yoy on a dollar basis, and it continues to achieve double-digit sales growth. In FY12/15, Effyis has advanced sales license agreements with several major social media companies in China, and it would seem that the growth in sales of social big data in China is the main reason for the increase in sales. Effyis also concluded licensing agreements with companies such as StockTwits, which is a shares-related social media, and Foursquare, which operates a positional information-linked SNS, and in these ways further strengthened its foundations as a social big data distribution company.

■ Financial results trends



Although the increase in operating income of 11.0% yoy is small compared to the sales growth rate, this was due to the increases in depreciation and amortization expenses and personnel expenses arising from making Effyis a subsidiary, and also higher temporary costs associated with the M&A. Looking on an EBITDA (operating income + depreciation and amortization expenses) basis, it increased by 2.3 times to ¥488mn, and the EBITDA margin trended at 20.0%, which is about the same level as the previous fiscal year. The cost of sales ratio rose from 42.3% in the previous fiscal year to 48.8%, but this was primarily due to the increase in costs to purchase data from social media associated with making Effyis a subsidiary.

In the Effyis results, sales were ¥1,325mn, while it achieved an operating income of ¥23mn, despite recording higher personnel expenses of ¥60mn in accordance with the incentive plan linked to the acquisition (continuing for three years) and temporary costs of ¥30mn associated with the processing of a loss on uncollectible receivables.



Source: the Company's financial results briefing materials

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The profitability of its main business is not worsening

(2) Financial position

Looking at the financial position of Hottolink as of the end of December 31 2015, current assets were ¥1,977mn, down ¥949mn from December 31, 2014. The main reason for this was the decrease in cash and deposits associated with the acquisition of Effyis. Non-current assets rose by ¥3,446mn to ¥3,796mn, of which ¥2,693mn was due to an increase in goodwill following the Effyis acquisition, and in addition intangible assets climbed ¥764mn due to the capitalization of software development costs. As a result, total assets were ¥4,745mn, up ¥1,469 million from December 31 2014.

Total liabilities were ¥3,284mn, up ¥1,390mn from December 31, 2014. This mainly reflected an increase in interest-bearing debt of ¥1,030mn associated with the borrowing for the acquisition of Effyis. Total equity was ¥1,461mn, up ¥78mn, due to an increase in retained earnings from the recording of net income of ¥18mn, and also an increase in capital and the capital reserve from the exercise of stock options.

Looking at the key financial indicators, the indicators of financial soundness slightly declined as the equity ratio and interest-bearing debt ratio deteriorated slightly following the increase in interest-bearing debt. Also in the indicators of profitability, ROA declined due to the recording of goodwill and the deterioration of financial income, while ROE and the operating income ratio also fell. But as previously mentioned, the EBITDA margin trended practically unchanged from the previous fiscal year, and it is not the case that profitability worsened on a main-business basis.

Consolidated balance sheet

(unit: ¥mn)

	FY12/14	FY12/15	Change
Current assets	2,927	949	-1,977
(cash and deposits and cash equivalents)	2,772	611	-2,160
Non-current assets	349	3,796	3,446
(goodwill)	197	2,891	2,693
(intangible assets)	32	797	764
Total assets	3,276	4,745	1,469
Total liabilities	1,893	3,284	1,390
(interest-bearing debt)	1,700	2,730	1,030
Total equity	1,382	1,461	78
(indicators of financial soundness)			
Equity ratio	42.2%	30.8%	
Interest-bearing debt ratio	122.9%	186.8%	
(indicators of profitability)			
ROA (ratio of income before income taxes to total assets)	5.9%	1.5%	
ROE (return on equity attributable to owners of the parent company)	5.8%	1.3%	
Operating income on sales	11.0%	5.2%	

■ Outlook for the future

Business development in FY12/15 from the launch of “social media × tourism”

(1) Outlook for the FY12/16 results

The Company’s targets for FY12/16 consolidated results are conservative, with net sales forecast to increase 2.5% yoy to ¥2,500mn, operating income to decline 22.9% to ¥97mn, and net income attributable to the owners of the parent company to rise 8.7% to ¥20mn.

The reason we consider the net sales forecast conservative is that the Company has not incorporated the contribution of new services planned for the domestic and overseas markets in this fiscal year. Results are expected to be unchanged from FY12/15 in the domestic business, with the anticipated increase coming from the growth in the Effyis overseas business. The forecasts assume that the yen will appreciate 3% against the dollar, from ¥116 to the dollar to ¥120 to the dollar. Looking on a dollar basis, it is estimated that the Effyis sales growth rate will be in excess of 8%.

Operating income is expected to decline, as continuing on from the previous fiscal year, the Company plans to actively carry out upfront investment for recruitment, to develop new products, and to open-up new markets toward business expansion. But on an EBITDA basis including depreciation and amortization expenses, the forecast is for a 7.0% increase. The Company plans to recruit around 10 new employees in FY12/16, and it also plans to recruit several new employees for Effyis.

(2) The business strategy and investment plan

The business strategy for FY12/16 is to focus on business development from the launch of “social media × tourism”. From the current to the next fiscal year, the Company plans to continue its initiatives of the last fiscal year, of enhancing the menu of services for analyzing trends in inbound consumption and expanding its business in Asia.

In terms of enhancing the domestic service menu, the Company plans to sell Korean and Thai versions of Visualized China Trend EXPRESS. For the launch of these services, Hottolink is investigating the acquisition of social media distribution companies within South Korea and Thailand, or concluding data sales licensing agreements with major social media companies. At the same time, the Company plans to acquire local social big data analysis companies. Hottolink is also considering developing these businesses independently if it is unable to realize acquisitions.

Moreover, in addition to a Chinese version of Visualized China Trend EXPRESS, in this fiscal year the Company plans to develop overseas versions for Thailand, Singapore, Dubai, and South Korea, which receive many Chinese tourists. Toward this, Hottolink is proceeding with system development (multilingual support) and with the development of analysis engines compatible with each country’s social media. For overseas services, it is planning a Trend Express service targeting non-Chinese tourists for the next fiscal year.

In addition, Hottolink is aiming to further expand its business using Chinese social big data, and during 2016 the Company plans to make a wholly owned subsidiary of Ideal Marketing Strategist Co., Ltd., which produces Visualized China Trend EXPRESS and in which the Company made a capital investment for a 19.9% stake in the previous fiscal year. Moreover, as a new service, the Company is proceeding with the research and development of the Signs Discovery System, which discovers the products and services expected to be hits in the future through an analysis of social big data.

Business investment plan (February 2016 to January 2018)

Investment to acquire data marketing rights and to expand data collection capabilities in China and Southeast Asia
Hottolink plans to acquire one social big data distribution company in China and Southeast Asia (acquisition price, ¥300mn). If the Company is unable to realize this acquisition, it will form business alliances with social media companies (4 companies) and intends to spend a total of ¥250mn on data marketing license fees and ¥50mn on system-development costs.
¥60mn for system development costs, including to acquire social media in specific areas (positional information, video, audio, etc.), sensor data (human body data, traffic data, etc.), and government related data.
Investment to develop new products and services for the inbound consumption market
The Company plans to acquire South Korean and Thai social analysis companies for enhancing its “○○ Trend Express” lineup for the domestic market. A total of ¥200mn. If not feasible, it plans to develop the business in-house.
¥50mn system development costs (multilingual analysis engine) to provide overseas versions of China Trend Express (China, Thailand, Singapore, Dubai, and South Korea) and ¥50mn for the systems development of analysis engines compatible with each country’s social media.
Plans to make Ideal Marketing Strategist (Shanghai) a subsidiary during 2016. ¥93mn to acquire its shares.
¥50mn for the research and development of the Sign Discovery System, which analyzes social big data to discover products and services expected to be big hits in the future.

Source: prepared by FISCO from Company presentation materials

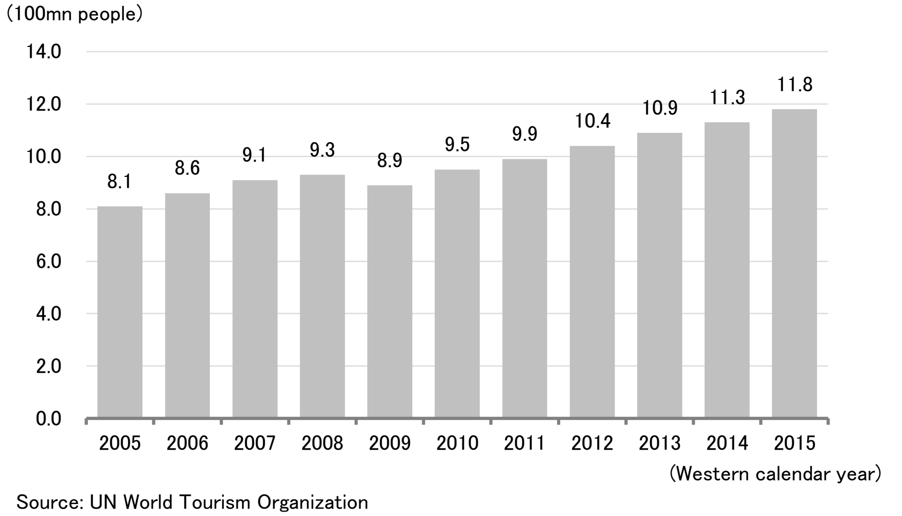
Hottolink anticipates investing a total of ¥800mn over the next 2 years to expand these businesses. The Company plans to raise the funds for this investment amount through an issuance of new shares and share acquisition rights by a third party allocation carried out in January 2016. ¥505mn has already been raised from the issuance of new shares, and if all of the stock acquisition rights are exercised in the future, the Company will be able to raise a total of ¥1,600mn. Within this amount, ¥800mn is scheduled to be allocated to the repayment of interest-bearing debt (March 2016), and business investment will proceed with the remainder of the funds raised. As the exercise price for the share acquisition rights has been fixed at ¥545, it is possible the exercise will not proceed as planned due to share-price trends but ¥295mn's worth of the rights are expected to have been exercised by the end of March. If all of the share acquisition rights are exercised, there will be an increase of 3.12 million shares, and shareholder value per share will be diluted by 31.6%.

(3) Medium-term targets

The Company's medium-term targets for FY12/20 are net sales of ¥10.0bn, with an overseas sales ratio of 80%. In the future, it plans to create a business on a scale of ¥100.0bn.

Toward achieving these targets, Hottolink is developing a business from the launch of "social media × tourism," as previously described. The market for this is not only Asia and it intends to develop inbound consumption trend support services for the entire world. The number of tourists visiting Japan is growing each year, and in 2015 it grew significantly, by 47.1% yoy to 19.73 million people. Throughout the world also, tourist numbers are trending upward each year. Therefore, it is becoming increasingly important for countries to quickly ascertain inbound consumption trends for their marketing strategies for outside of Asia also.

Number of worldwide tourists



Source: UN World Tourism Organization

In particular, it is difficult to create hypotheses on the consumption trends of foreigners due to their different cultures and moreover, trends change rapidly. Therefore, as a method to analyze consumption trends, the most efficient method is said to be analyzing the comments of the many users who post on social media, and demand for this sort of analysis service is expected to further increase in the future. The Company's strategy is to provide high quality services and expand its business scale by combining the ability of Effyis' to collect social big data from throughout the world, Hottolink's own advanced real-time analysis technologies and Ideal Marketing Strategist's data analysis and reporting capabilities.

In terms of its service menu, the Company will provide Trend EXPRESS (a weekly report service for a monthly fee of ¥80,000), customized reports according to customer needs (several million yen × several times a year), and a promotion support service (starting from several million yen). This promotion support service is from a business alliance with an advertising agency to support the promotional activities of Japanese companies within China. In addition, the Company carries out data sales and license sales (starting from several hundreds of thousands of yen per month) for media, such as TV and magazines, and retailers. Also, for its Trend EXPRESS service, the Company is investigating providing a service for consumption trends and demand forecast analysis tools using the SaaS model in the future.

Shareholder returns policy and risk factors

Recognized as in the stage of upfront investment of actively directing funds to business investment

(1) Shareholder returns policy

Regarding the return of profits to shareholders, Hottolink plans to pay out dividends to shareholders in the future. However, Hottolink believes that it is currently in an upfront investment phase where it should actively allocate funds primarily to investment in businesses, and the recruitment and training of talent. Accordingly, the same as in the previous fiscal year, the Company does not plan to pay a dividend in FY12/16.

(2) Risk factors

Looking at business risks, changes in management policy by companies that Hottolink purchases social media data could lead to cancellations of current license agreements and this could have an impact on the Company's financial results. That said, it already has approximately 500 corporate customers in Japan, Furthermore, the amount of data purchased is expected to continue to increase, mainly based on the expansion of services to analyze consumption trends. Therefore, at FISCO we believe that the likelihood that license agreements will be cancelled is extremely low.

Also, if progress is not made in the exercise of the share acquisition rights issued in January, there is the risk that the Company will not be able to conduct business investment as planned. But in this case, Hottolink will investigate raising funds by other means. Also, the Company considers that for the time being, it is in a period of building the foundations toward the global development of its businesses in order to achieve net sales of ¥100bn. For this reason, it is possible that significant improvements in results, such as for profits and profitability, will only appear after it has achieved net sales of ¥100bn.

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