

PIPEDO HD, Inc.

3919

Tokyo Stock Exchange First Section

22-Nov.-2018

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<http://www.fisco.co.jp>

Index

Summary	01
1. Operating profit down 59.4% YoY in 1H FY2/19 due to upfront investments, but within expected range...	01
2. Expectations remain unchanged in terms of a 33.4% YoY decline in FY2/19 operating profit due to investing in personnel ahead of the following fiscal year	01
3. Medium-term plan goals unchanged at ¥7,300mn in net sales and ¥1,700mn in operating profit in FY2/20	01
Company profile	02
1. Company profile.....	02
2. History	02
3. Business overview	03
Results trends	10
● Summary of 1H FY2/19 results	10
Business outlook	14
● FY2/19 outlook.....	14
Medium- to long-term growth strategy	15
1. Medium-Term Business Plan 2020 goals unchanged.....	15
2. Priority measures	16
3. Fund-raising initiative.....	17
Shareholder return policy	18

Summary

Medium-term plan targets ¥7,300mn in net sales and ¥1,700mn in operating profit in FY2/20

PIPEDO HD, Inc. <3919> (hereafter, also “the Company”) is a pure holding company, and PIPED BITS Co., Ltd., its main consolidated subsidiary, is a unique IT company that supplies its proprietary SPIRAL® platform (middleware) in a cloud format. The Company provides a platform for national clients and other large companies, mid-sized companies, and smaller system integrators and also sells proprietary applications for specific industries (such as beauty and construction industries) and engages in businesses that utilize these applications.

1. Operating profit down 59.4% YoY in 1H FY2/19 due to upfront investments, but within expected range

In 1H FY2/19, the Company reported ¥2,623mn in net sales (up 4.2% YoY), ¥176mn in operating profit (down 59.4%), ¥173mn in recurring profit (down 59.8%) and ¥75mn in profit attributable to owners of parent (down 74.1%). These results slightly undershot the forecasts from the start of the fiscal year, but are not a cause for concern. The primary reason for the drop in profit was aggressive investment (hiring of personnel), but this had been planned since the start of the fiscal year and is targeting FY2/20 and beyond. Starting from FY2/19, the Company has reorganized its business segments into the “Function-based Segment,” which targets many companies and organizations overall, and the “Field-based Segment,” which targets specific sectors.

2. Expectations remain unchanged in terms of a 33.4% YoY decline in FY2/19 operating profit due to investing in personnel ahead of the following fiscal year

The Company’s FY2/19 forecast targets ¥5,800mn in net sales (up 12.8% YoY), ¥500mn in operating profit (down 33.4%), ¥490mn in recurring profit (down 34.6%), and ¥300mn in profit attributable to owners of parent (down 34.5%). While this forecast envisions healthy expansion of net sales, the Company expects significant decline in earnings because of proactive investments, mainly in personnel, toward the final year of the three-year plan. However, these are constructive outlays aimed at realizing robust gains in the final fiscal year of the medium-term plan, and it is not a reason for concern.

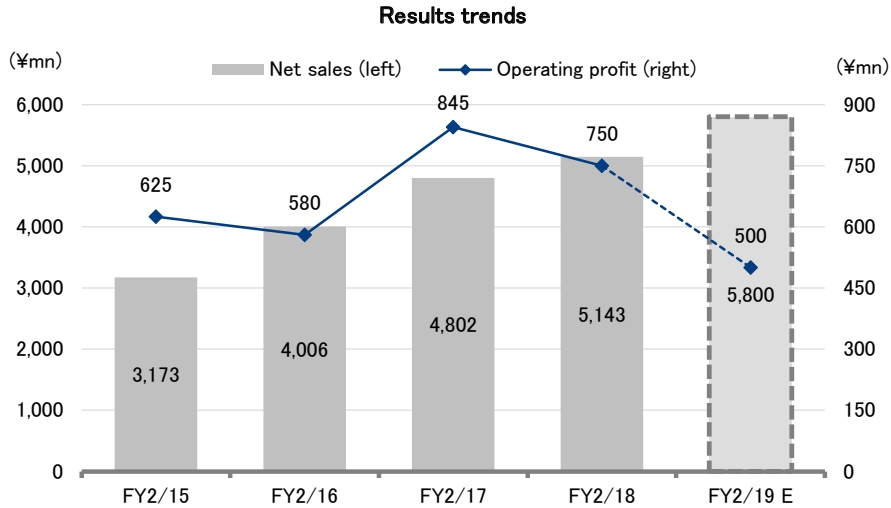
3. Medium-term plan goals unchanged at ¥7,300mn in net sales and ¥1,700mn in operating profit in FY2/20

The Company’s three-year medium-term business plan targets ¥7,300mn in net sales and ¥1,700mn in operating profit in FY2/20. It maintains the initial plan goals because personnel hired in the first two years of the plan period (FY2/18 and FY2/19) should contribute significantly to the final fiscal year. We expect larger profit change rates if the medium-term business plan proceeds as envisioned, thus we will be closely monitoring these trends going forward.

Key Points

- Conducts businesses that primarily leverage the proprietary SPIRAL® platform
- Forecasts a decline in FY2/19 profit, though it is not a concern because spending is aimed at driving results in the following fiscal year
- Medium-term plan goals unchanged at ¥7,300mn in net sales and ¥1,700mn in operating profit in FY2/20

Summary



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

Company profile

Conducts businesses that primarily leverage the proprietary SPIRAL® platform

1. Company profile

The Company is a pure holding company established through a transfer of shares from PIPED BITS on September 1, 2015. It has 14 consolidated subsidiaries and one equity-method affiliate as of September 30, 2018.

2. History

PIPED BITS was established in April 2000 by Nobuaki Satani, the current President of PIPEDO HD. For most companies, data acquired in the course of business including customer attributes and email addresses form important "information assets," so PIPED BITS commenced operations with services to effectively use them at the same time as managing them securely. What was developed in-house in order to carry out this business was the proprietary SPIRAL® platform for data management. (Details to follow.) Subsequently, the company developed a range of applications based around SPIRAL® and has been engaged in rolling out these business applications.

PIPEDO HD, Inc. | 22-Nov.-2018
 3919 Tokyo Stock Exchange First Section | <https://www.pipedohd.com/#>

Company profile

PIPEDO HD history

Sep. 2015	PIPEDO HD was established by a single transfer of shares from PIPED BITS Co., Ltd. and listed on the Tokyo Stock Exchange First Section (PIPED BITS Co., Ltd. was delisted in August 2015). PIPEDO HD acquired the shares of the four subsidiaries of PIPED BITS by a property dividend, converting them into its own subsidiaries.
Dec. 2015	Made additional investment into Current Inc., converting it into a subsidiary
Mar. 2016	Established GONDOLA CO., LTD., FRIENDIT Inc., and BIREKI Co., Ltd.
Oct. 2016	Established BLOOM NOTES, INC.
Mar. 2017	Established VOTE FOR, INC. and I LOVE, INC.
Dec. 2017	Established L Coin, Inc.

Source: Prepared by FISCO from the Company's website

PIPED BITS history

Apr. 2000	Established as K.K. Sahara in Tokyo's Setagaya Ward, aiming at e-mail based marketing support software, after receiving a capital investment from Current Inc. (Tokyo, Setagaya Ward)
Oct. 2000	Developed e-mail marketing platform "SPIRAL Messaging Place®".
Dec. 2000	Spun-off to become independent via an MBO, and relocated headquarters to 1-12-15 Jinnan, Shibuya Ward, Tokyo.
Jan. 2001	Changed trade name to PIPED BITS Co., Ltd.
Feb. 2001	Launched SPIRAL Messaging Place® service
Apr. 2001	Introduced a sales agent system to SPIRAL Messaging Place®
Dec. 2001	Introduced SLA (Quality Certification System) to SPIRAL Messaging Place®
Dec. 2006	Listed on the TSE Mothers exchange
Apr. 2009	Changed the service name from SPIRAL Messaging Place® to SPIRAL®.
Jan. 2010	Acquired certain operations, namely the CMS and EC businesses from HIDESIGNS Inc.
Apr. 2010	Launched apparel EC platform "SPIRAL EC®".
Dec. 2010	Started to tackle the Internet advertising and Internet media-related areas. Launched Media EC operations.
Mar. 2011	Acquired the Apparel web solution business from Gras CORPORATION. Launched E-Commerce Business to operate, manage and develop e-commerce sites tailored to the apparel and fashion space.
Sep. 2011	Increased capital via a third party capital allotment to United Ventures Inc., Acquired "Net de Kaikai®", a cloud-based accounting business, from Business Online Co., Ltd.
Mar. 2012	Acquired "Biyoshimeikaikan", a hair catalogue publication business, from SAMURAI PROJECT CORPORATION. Made PaperlessStudio co., Ltd. a subsidiary.
Mar. 2014	Made AsBase Inc. a subsidiary via a stock swap.
Feb. 2015	Invested in Sprinklr Japan KK
Mar. 2015	Subscribed to a third party allocation of shares by Current, Inc. Invested in Sprinklr, Inc. (United States)
May 2015	Established Publica Co., Ltd.
Jul. 2015	Established WEARHEART Inc.

Source: Prepared by FISCO from the Company's website

3. Business overview

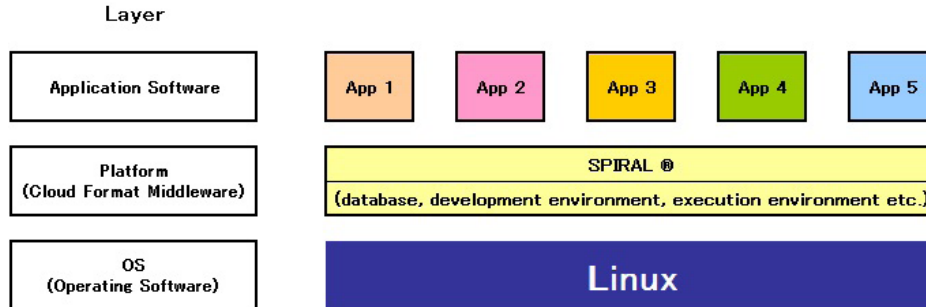
(1) Product overview

The Group's flagship business is its proprietary platform SPIRAL®, and the provision to users of related applications, not by way of outright sales but rather in a rental format (a monthly fee method). Within the layers of software, SPIRAL®'s position may be referred to as a cloud-based middleware.

PIPEDO HD, Inc. | 22-Nov.-2018
 3919 Tokyo Stock Exchange First Section | <https://www.pipedohd.com/#>

Company profile

Positioning of SPIRAL®



Source: Prepared by FISCO from Company website and materials

Generally, when developing operational and other systems, the majority of companies need to purchase the hardware required to develop and run the system, the operating system (OS), development environment (tools), database(s), middleware and other elements themselves (or outsource development), and by combining them, develop the base (platform) in order to run the system. Additionally, they must also bear the burden (cost) of maintaining its post-development. As SPIRAL® developed by PIPED BITS is already equipped with development tools. Not only does this enable easier development of different kinds of applications, but also customer data and other data stored in SPIRAL® can be shared and used with other applications due to the platform’s built-in database. Furthermore, these applications and data may be easily reproduced and delivered. This provides a significant advantage over package software.

As a result, corporate customers may easily and holistically operate with (use) and manage data, and at the same time greatly reduce application development costs by using SPIRAL®. Additionally, given that it is a pay-for-use monthly fee format platform, it further helps to reduce costs. Starting with major financial institutions, the companies that have introduced SPIRAL® include many preeminent corporations.

Recently in the IT industry, the majority of services are provided in a cloud format, with them being described in a variety of ways depending on the content of the particular cloud format service. SPIRAL® belongs to the area generally called PaaS (Platform as a Service), in other words, not only applications used in various business operations, but it is also the field of providing the platforms that run these applications on a cloud format.

(2) Main product content and prices

The Company’s flagship product SPIRAL® is a platform environment. Accordingly, the main customers using it range from large companies which internally develop operating systems and other software to SME-sized system integrators that undertake development of systems for SMEs, and also web production and web development companies. By using SPIRAL®, the Company is also able to internally develop applications aimed at specific industries and users, and then also sell these applications. These types of core products are not sold as a package (outright sales) but are sold entirely in an ASP format. Below are the major products and their monthly pricing (minimum fees).

It goes without saying that in the Company’s business model, increases in active (fee-based) accounts is linked to sales growth. However, the fees mentioned below are only basic or minimum fees and the actual fees change depending on data volumes (pay-for-use). Therefore, sales do not simply equal the number of accounts multiplied by the basic fee. But in order to view sales trends, the number of active accounts is an important indicator.

Company profile

a) SPIRAL®

This is the Company's main product. The core platform is equipped with a database, development environment, execution environment, and other features. While it is often utilized in email distribution, seminar management, and questionnaire form creation applications, this product offers many other functions as well. Furthermore, it flexibly coordinates with services from other companies and customization can substantially broaden the scope of applications. The monthly fee starts at ¥25,000.

b) SPIRAL PLACE®

Cloud format groupware possessing website creation and updating functions, and at the same time linked to SNS. As groupware, SPIRAL PLACE® enables calendar and file-sharing while using simple (manual) operations to enhance and update web content, as well as traffic analysis. It can also be linked to Facebook and Twitter. It is highly regarded by retail chain stores and others that employ large numbers of staff. Basic fees start at ¥6,000/month.

c) SPIRAL EC®

An e-commerce (EC) platform focused on apparel. It is highly received by the industry for resolving a number of issues, such as simplifying update procedures and maintaining a low budget, while also pursuing a sophisticated brand image for EC sites for apparel. Fees are pay-for-use up to 5% of the transaction amount.

d) SPIRAL Affiliate®

A holistic ASP affiliate management service that reduces the issues and costs associated with introducing and operating affiliate marketing for advertisers. It includes special offers for SPIRAL® users, such as no upfront costs.

e) Other

There are also applications aimed at specialist fields and industry sectors. Further, through alliances with various specialist companies, the Company aims to expand the use and applications of SPIRAL®.

(3) Business segments

Up until FY2/18, the Company had four business segments – the information asset platform business, the advertising business, the solutions business, and the social innovation business. From FY2/19 the Company has established three main segments: the “Function-based Segment,” the “Field-based Segment,” and “Group Common Segment.” The Company's businesses have been sorted into these three main segments.

The main segments are divided according to target client. The Function-based Segment comprises businesses utilizing the cloud and other IT platforms to target companies and organizations expected to have room for improvements in operating efficiency in CRM, sales promotions, and EC. These are businesses in which sales activities can be carried out horizontally. The Field-based Segment includes businesses that target specific industries and fields for which innovation through new information-sharing models utilizing the cloud and other IT platforms can be expected. These businesses involve vertical sales. The Group Common Segment includes the management costs of the pure holding company, which were previously allocated to business areas, and costs related to Group hiring and development.

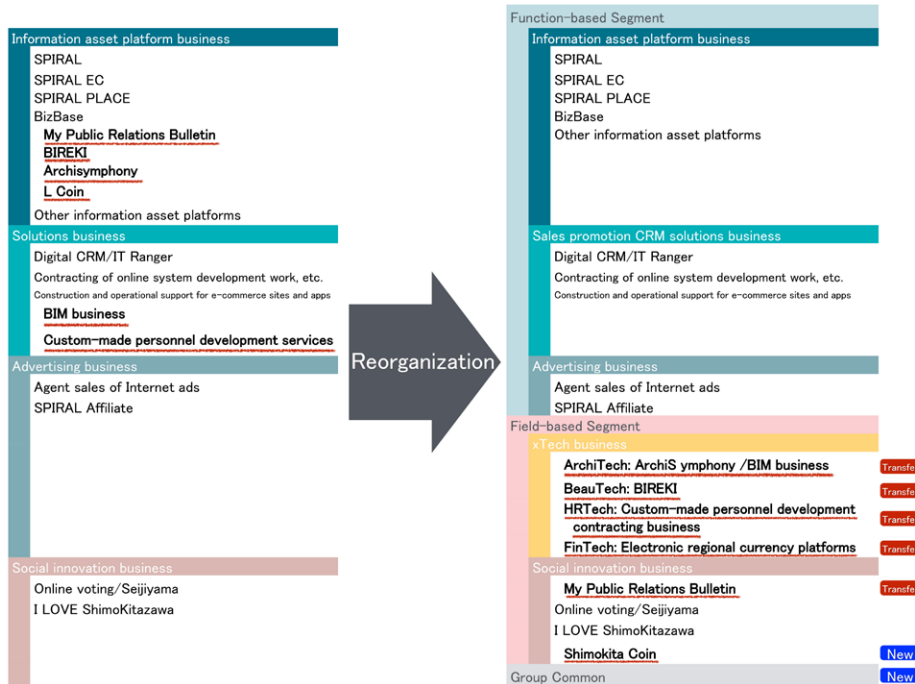
Company profile

Segment reorganization (Main segments/segment details)

<p>Function-based Segment</p> <p><u>Information asset platform business</u></p> <p><u>Sales promotion CRM solutions business</u></p> <p><u>Advertising business</u></p>	<p>Businesses utilizing the cloud and other IT platforms to target companies and organizations expected to have room for improvements in operating efficiency in CRM, sales promotions, and EC</p> <p>Development and provision of systems that assist clients in reducing costs and improving business efficiency to help solve issues in society, where there is a shortage of manpower</p> <p>Provision of services utilizing IT to optimize operations and create contact opportunities with customers as well as enhance these contact points; development of optimal IT systems for clients according to their needs</p> <p>Planning of promotions tailored to customers' objectives; production, development and management of advertising contents; agency sales of online ads</p>
<p>Field-based Segment</p> <p><u>xTech business</u></p> <p><u>Social innovation business</u></p>	<p>Businesses targeting specific industries and fields for which innovation through new information-sharing models utilizing the cloud and other IT platforms can be expected</p> <p>Business expected to create innovative services in the industry by utilizing IT to share information across company and organizational lines</p> <p>Business engaging in activities with public benefits, aiming not to help individual companies and industries solve internal problems, but to solve broader societal issues</p>
<p>Group Common</p>	<p>The pure holding company's management costs, costs related to Group hiring and development, etc.</p>

Source: The Company's results briefing materials

Segment reorganization (changes in segment by product and service)



Source: The Company's results briefing materials

(4) Other consolidated subsidiaries and their business overview

In addition to the mainstay businesses (PIPED BITS' SPIRAL®), the Company also operates various related businesses via the following subsidiaries.

Company profile

a) PaperlessStudio co., Ltd.

PaperlessStudio is involved in the construction project planning and management and BIM (Building Information Modeling) consultant businesses. The company also runs BIM and CIM (Construction Information Modeling) personnel workshops for people working in design and construction. In May 2012, the company started providing the BIM construction information platform ArchiSymphony®. It also released ArchiSymphonyVBP, the first cloud service exclusively for BIM/CIM collaboration in Japan, in September 2017.

b) Publica Co., Ltd.

A specialist company for providing services using open data from local governments and government agencies. Publica promotes the availability of data held by government agencies, local governments, and private-sector businesses and develops services that make use of the data to enable it to be managed autonomously. The company has developed a system for Internet distribution of local government public relations bulletins—the “My Public Relations Bulletin” system.

c) GONDOLA CO., LTD

GONDOLA was formed by the corporate split of the Media Strategy Company on March 1, 2016. The company is active in the three service domains of advertising solutions, web solutions, and social management. By combining an original service line-up in planning, production, system development, and operation, with IT utilizing information management platforms such as SPIRAL Affiliate®, SPIRAL® and Sprinklr, the company enables one-stop solutions for corporate management issues and business activity optimization.

d) FRIENDIT Inc.

FRIENDIT provides comprehensive support for e-commerce-related system implementation, online shop management, and omni-channels at the strategic level. Assisting customers with the common issues of personnel shortages and experience gaps, the company produces marketing activities that directly boost sales volume and value, from IT-based administration optimization through to promoting use of data on products, members, and purchasing. The company was formed on March 1, 2016 by a corporate split-off from the in-house Apparel and Fashion Company.

In April 2018, FRIENDIT took over SPIRAL EC® and SPIRAL PLACE®, which were owned by PIPED BITS, and also carried out an absorption merger of AsBase Inc., which had been providing the ASP/SaaS type call center platform service BizBase®. With these moves, the company will develop new services integrating SPIRAL EC®, SPIRAL PLACE®, and cloud computer-telephony integration (CTI).

e) BIREKI Co., Ltd.

BIREKI provides IT services centered on the digital record app “BIREKI®” for beauty salons. The company’s business activities aim to enrich the lives of people by helping to increase the value of as many people working in the beauty industry as possible and making beauty treatments more accessible and enjoyable. The company was newly established on March 1, 2016 through a corporate spin-off from the previous Bireki Company.

f) Current, Inc.

Current’s core businesses involve web access improvement and digital CRM for developing loyal users (implementation services such as communication and data management design, message creation and construction, message delivery, and effect verification) while integrating information assets and implementing optimal messaging to users. Aiming to generate business synergies between PIPED BITS, which has expertise in information asset utilization and IT solutions, and Current, with its strengths in stationed marketing support, the Company increased its equity stake in Current in December 2015 and converted it into a subsidiary.

Company profile

g) BLOOM NOTES, INC.

The Company spun off its division in charge of in-house human resource development and education as a subsidiary on October 3, 2016 in order to provide similar education services to external customers. It organized knowhow into a structured program to resolve issues related to human resource development at SMEs and also operates a human resource development agent business to support implementation.

h) VOTE FOR, INC.

The Company established this entity in Mach 2017 to facilitate Internet-based voting. It aims to build voting systems that utilize blockchain and other new technologies. It also continues to operate the Seijiyama® political and election information website that existed internally.

i) I LOVE, INC.

The Company created this entity in Mach 2017 to make further progress in the “I LOVE ShimoKitazawa” local revitalization project and pursue development of a new transaction format for single-coin donations, tips, and other small-sum transactions employing electronic regional currency.

j) L Coin, Inc.

The Company invested 70% in L Coin, which was established in December 2017, as a consolidated subsidiary. L Coin builds payment systems for local governments, companies, and local financial institutions using an electronic regional currency platform that applies blockchain technology and thereby promotes cashless transactions in local communities. It can also issue unique electronic regional currencies at low cost through the platform and supports smooth development of payment systems and store point systems.

k) Shimokita Coin, Inc.

This company was established in March 2018 as a subsidiary of L Coin. Using an electronic regional currency platform provided by L Coin, the company issues electronic regional currency limited to the Shimokitazawa area. Also, the company is working with I LOVE to attract investment and member stores among local shops, and aims to energize the local economy.

SPIRAL®'s primary feature is flexible customization

(5) Special characteristics and strengths**a) Ease of system construction**

SPIRAL®'s greatest distinguishing feature is its ability to be freely customized. As explained above, the Company itself combines SPIRAL®'s functions to develop applications for its own operational systems and specific customers (areas). Apart from areas such as financial institutions, which require extremely high reliability, almost any operational system could be created by combining SPIRAL®'s functions. These operational systems have been generally developed by operators known as system integrators. However, it is possible to replace the majority of the work traditionally done by system integrators through a combination of SPIRAL® functions, with corporate customers able to easily undertake a range of development and system creation themselves. For this reason, SPIRAL® is attractive not only to large corporations, but also SMEs that are unable to bear the high cost of systems development, as the platform is affordable and easy to use.

Company profile

b) Every type of application can be linked

SPIRAL® possesses a broad range of functions. However, the most basic function is that it enables, for example, a corporate customer managing databases over the Internet to easily engage in various tasks, from database creation through to data manipulation (such as registration, updating and deletion), batch data registration, and downloading. Specifically, in cases in which companies undertake online surveys, market research or new product evaluations, by using SPIRAL® the company can very easily create a survey, deliver it to targeted and prospective customers, have them complete the surveys, and then collect them. If a customer satisfaction questionnaire is linked to the customer database, it becomes possible to analyze them according to customer attributes, and conduct follow-up in order to enhance satisfaction levels. Survey results may be aggregated in real time, and compiled into a report. Via SPIRAL®, this series of actions between different applications may all be easily undertaken with simple operations.

In the same way, with regard to creating forms, such as for gift promotions/affinity marketing campaigns, recruitment application forms, inquiry forms, seminar applications, account openings, and information requests, it is possible via SPIRAL® to expeditiously undertake actions such as form creation; the recording, updating, and deletion of member attributes; and login verification. For example, in a case such as holding seminars, even if hypothetically multiple seminars are proceeding simultaneously, the taking of multiple applications and management of cancellations can be carried out instantaneously, making the holding of the seminar more efficient. It is also easy to develop this data in a search form tabulating it, having a yes or no Q&A questionnaire, or creating a summary chart or graph. Also, given the addition of services from AsBase (now FRIENDIT) that possesses voice (telephone) solutions, and an alliance with Sprinklr Japan KK, whose strength is systems for SNS, it is expected that customer convenience will be enhanced further.

One of the Company's competitors is salesforce.com, Inc. <CRM> of the United States, but this company has grown through repeated acquisitions of other companies. Therefore, its various applications were developed by the different companies it acquired, so each application was not created on the same platform. Consequently, when a client needs to link multiple applications, in many cases this requires additional development costs and time. On this point, SPIRAL® is considerably superior to salesforce.com's product, as its applications are on the same platform and as a result, each of the applications can be easily (inexpensively and quickly) linked.

c) Superiority in installation costs and security

Further, because SPIRAL® is not sold as package software, but provided as a pay-as-you-go cloud service, a distinctive feature is that client companies may themselves build requisite systems rapidly and at low cost, without taking and incurring unnecessary time and expenses. That is, even in the initial period when the system is installed, it can be developed from just a small investment without incurring major costs.

In addition to its superiority in terms of costs, the Company also provides guarantees, maintenance and monitoring functions on the security front, which is extremely convenient, particularly for SME-sized system integrators. For example, in the event that vulnerability is identified in the SSL (Security Sockets Layer), which is the most widely used communication cryptographic technology on the Internet, normally it is necessary for each system integrator to individually deal with this vulnerability. But if SPIRAL® is used, the Company is able to take all necessary actions and the issue is resolved on SPIRAL®, eliminating the need for the system integrators to deal with it individually. Use of SPIRAL®, meanwhile, reassures end customers about security.

Many SMEs cannot afford the expenses required for system development and security. The Company's products solve these issues in a one-stop manner, thus the Company's products are attractive not only to large corporations but to SMEs in particular.

Company profile

d) Installation case studies

One example of a successful installation of the Company's SPIRAL® was the case of Asahi Fire and Marine Insurance Co., Ltd. The company introduced SPIRAL® as a customer service system. By linking client attributes with various types of data, the number of requests for information materials increased by 130 times, and the work time needed from receiving to answering a customer request was reduced from the usual time of around 30 minutes to just 2 or 3 minutes, thereby realizing a 10-fold increase in efficiency. Moreover, when introducing the system, the Company competed with other system integrators to win the account and the Company's quote was only about 1/10th the cost of its competitors. Although every case is different, this example clearly demonstrates the competitive advantages of SPIRAL®.

Results trends

1H earnings undercut forecasts, but not a cause for concern

● Summary of 1H FY2/19 results
(1) Profit-and-loss conditions

In 1H FY2/19, the Company reported ¥2,623mn in net sales (+4.2% YoY), ¥176mn in operating profit (-59.4%), ¥173mn in recurring profit (-59.8%) and ¥75mn in profit attributable to owners of parent (-74.1%). Although net sales fell slightly short of the initial forecast, upfront investments were executed as planned, so profits also undercut the initial forecasts. Still, the results were generally within the expected range, and are not a cause for concern.

Summary income statement

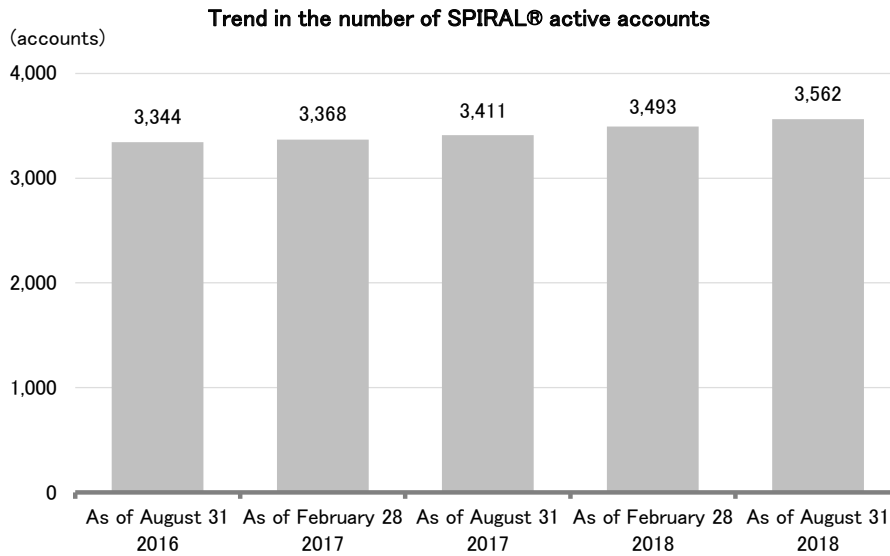
	1H FY2/18		1H FY2/19		(Change)	
	Amount	% of total	Amount	% of total	Amount	%
Net sales	2,517	100.0	2,623	100.0	106	4.2
Function-based Segment	2,403	95.5	2,509	95.7	106	4.4
Information asset platform business	1,707	67.8	1,801	68.7	94	5.5
Sales promotion CRM solutions business	608	24.2	504	19.2	-104	-17.1
Advertising business	88	3.5	204	7.8	116	130.5
Field-based Segment	112	4.4	112	4.3	0	0.0
xTech business	85	3.4	75	2.9	-10	-11.8
Social innovation business	27	1.1	37	1.4	10	39.1
Gross profit	1,770	70.3	1,840	70.1	70	4.0
SG&A expenses	1,336	53.1	1,664	63.4	328	24.6
Operating profit	433	17.2	176	6.7	-257	-59.4
Function-based Segment	677	-	513	-	-164	-24.2
Information asset platform business	611	-	489	-	-122	-20.0
Sales promotion CRM solutions business	81	-	-10	-	-91	-
Advertising business	-15	-	34	-	49	-
Field-based Segment	-26	-	-47	-	-21	80.8
xTech business	-9	-	-30	-	-21	-
Social innovation business	-17	-	-17	-	0	-
Company-wide costs	-217	-	-289	-	-72	-
Recurring profit	431	17.2	173	6.6	-258	-59.8
Profit attributable to owners of parent	292	11.6	75	2.9	-217	-74.1

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

Results trends

(2) Trends in active accounts

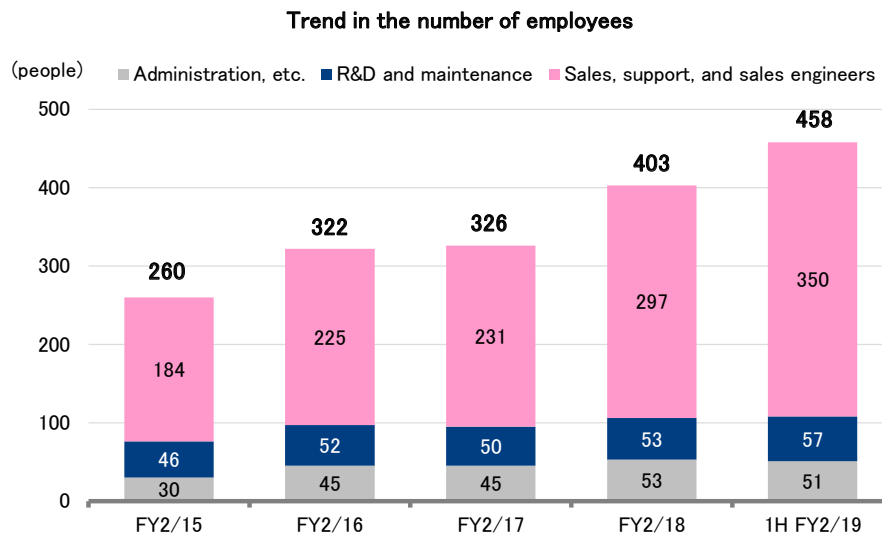
Because the Group's main businesses are cloud-based, the number of active accounts, and particularly the number of active SPIRAL® accounts, influences the Company's results. As of the end of 1H FY2/19, the Company had 3,562 active SPIRAL® accounts (up 69 versus the end of FY2/18, up 151 YoY), so there has been a steady increase in active accounts.



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

(3) Trend in the number of employees

The Company had declared that it would aggressively hire (invest) in FY2/18 and FY2/19 in order to realize goals in the medium-term business plan that lasts through FY2/20, as explained below. In fact, it hired 90 people in FY2/18 and another 76, including new university graduate, in 1H FY2/19. As a result, the number of employees greatly increased to 458 people (an increase of 55 people or 13.6%) by the end of FY2/18.



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

We encourage readers to review our complete legal statement on "Disclaimer" page.

Results trends

(4) Profit and loss by segment

The profit and loss in the Function-based Segment was as follows.

a) Information asset platform business

This business posted ¥1,801mn in net sales (+5.5% YoY), and operating profit of ¥489mn (-20.0%). Despite the increase in net sales, this business saw a decline in profit, as despite placing newly-hired personnel in the field, it took longer than expected for them to contribute to earnings, and there was also a rise in rent and other sales, general and administrative expenses in conjunction with the increase in personnel.

b) Sales promotion CRM solutions business

Net sales were ¥504mn (-17.1%) and there was operating loss of ¥10mn (versus a ¥81mn profit a year earlier). This was due to the impact of a large spot deal acquired in FY2/18, higher operating costs in association with the increase in personnel, and other factors.

c) Advertising business

This business booked ¥204mn in net sales (+130.5%) and operating profit of ¥34mn (versus a ¥15mn loss in the year-earlier period), partly due to efforts to provide multi-faceted proposals to existing clients in order to increase average sales per customer. The Company seconded personnel to Jeki Interactive Communications, which was established in April 2016 through a joint investment, and efforts to secure and expand sales through this company contributed to the acquisition of new deals.

Profit and loss in the Field-based Segment was as follows.

d) xTech business

This business engages in projects expected to create innovative services in the industry by utilizing IT to share information across company and organizational lines. Net sales were ¥75mn (-11.8%), while operating loss of ¥30mn (versus a loss of ¥9mn in the year-earlier period) was recorded. The main services of the business are as follows.

- 1) ArchiTech: BIM construction information platform ArchiSymphony®
- 2) BeauTech: Provides BIREKI®, an app that provides an electronic hair design records for customers and salons
- 3) HRTech: Custom-made personnel development contracting business to innovate company's development of personnel
Started a paid occupational referral business in March 2018 after receiving approval from the Minister of Health, Labour and Welfare
- 4) FinTech: Electronic regional currency platforms

e) Social innovation business

This business engages in activities with public benefits, aiming to not just help individual companies and industries solve internal problems, but to also solve broader societal issues. The business booked net sales of ¥37mn (+39.1%) and a loss of ¥17mn (same as the year-earlier period). My Public Relations Bulletin, a service that helps municipalities open up and utilize their PR magazines, continued to grow steadily, and the number of posting municipalities has already exceeded 521, which covers roughly 30% of the approximately 1,750 total municipalities. In addition, both the online voting-related business and Seijiyama®, the politics and election information website, are both enjoying healthy growth.

Results trends

(5) Financial standing and cash flow conditions

Looking at the financial position at the end of 1H FY2/19, total assets were up ¥369mn from the end of the previous fiscal year to ¥5,476mn. Current assets increased by ¥167mn, with the main factors being an increase in cash and deposits of ¥193mn and a decline in notes and accounts receivable of ¥29mn. Fixed assets increased ¥201mn, primarily due to increases in intangible fixed assets of ¥32mn and investments and other assets of ¥180mn. Total liabilities were up ¥364mn from the end of the previous fiscal year to ¥3,083mn. This was mainly due to an increase in short-term borrowings of ¥500mn. Net assets were ¥2,392mn, up ¥4mn. This was mainly due to an increase in new share warrants of ¥6mn.

Balance sheet

	(¥mn)		
	As of February 28, 2018	As of August 31, 2018	Change
Current assets	3,133	3,301	167
Fixed assets	1,973	2,175	201
Total assets	5,107	5,476	369
Current liabilities	1,831	2,329	497
Fixed liabilities	887	754	-133
Total liabilities	2,718	3,083	364
Net assets	2,388	2,392	4

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

Cash provided by operating activities was ¥196mn, with the main income items being the recording of net profit before income taxes of ¥173mn and depreciation and amortization of ¥105mn. Cash used in investing activities was ¥283mn, with the main expenditure items including the acquisition of intangible fixed assets (largely software) of ¥105mn and of investment securities of ¥159mn. Cash provided by financing activities was ¥280mn, with the main items including ¥366mn for the net increase of borrowings and ¥91mn for the payment of dividends. As a result, during the period, cash and cash equivalents increased ¥193mn, and the balance of cash and cash equivalents at the end of the period was ¥2,109mn.

Cash flow statement

	(¥mn)	
	As of August 31, 2017	As of August 31, 2018
Cash flow from operating activities	399	196
Cash flow from investing activities	-250	-283
Cash flow from financing activities	-217	280
Change in cash and cash equivalents	-68	193
Balance of cash and cash equivalents at the end of the period	2,075	2,109

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

(6) Main policies and topics
a) Subscribed to a third-party allocation of shares by ipoca Inc. (March 2018)

The Company invested ¥150mn in ipoca (3.88% share of voting rights), with the aim of carrying out system coordination between ipoca's NEARLY, and the Group's SPIRAL®, SPIRAL EC®, advertising, and other services. NEARLY is an app that directs customers to retail facilities. The app has been installed in 130 retail facilities in 12 cities nationwide. It posts information on 13,000 stores, and the total number of users has reached 1.05 million.

Results trends

b) Established Shimokita Coin, Inc., which issues electronic regional currency in the Shimokitazawa area

As mentioned earlier, Shimokita Coin was established in March 2018 as a subsidiary of L Coin. Using an electronic regional currency platform provided by L Coin, the company issues electronic regional currency limited to the Shimokitazawa area. Also, the company is working with I LOVE, INC. to attract investment and member stores among local shops, and aims to energize the local economy.

c) SPIRAL® compatibility with LINE 1:1 Talk (March 2018)

LINE 1:1 TALK was added as an optional service for SPIRAL®. This service allows companies and users to talk one-on-one like on the normal LINE service when there is a reply or inquiry from a customer. A proprietary customer service function prevents multiple operators from responding to a customer inquiry, and thereby helps companies enhance their customer service.

d) Merger of FREINDIT and AsBase (April 2018)

As discussed above, subsidiaries FRIENDIT (the surviving company) and AsBase were merged, and will develop new services combining SPIRAL EC®, SPIRAL PLACE®, and cloud CTI.

e) Launch of new SPIRAL® version 1.12.5 (August 2018)

The Company started providing the new version 1.12.5 equipped with the new function SPIRAL® PHP Management, which helps with PHP version upgrade work. With this, users will be able to perform batch syntax checks of PHP programs set within SPIRAL® with the designated version they plan to upgrade to.

f) Successful online voting demonstration test (August 2018)

The Company provided the country's first online voting system utilizing My Number personal identification cards and blockchain technology to the final review in the contest to select the "2018 Tsukuba Society 5.0 Social Implementation Trial Support Project" held by Tsukuba City. The system successfully delivered valid voting, secured the secrecy of votes cast, and offered tamper-proof data.

g) SPIRAL® partners with Capy Puzzle CAPTCHA (August 2018)

As a countermeasure against list-type attacks via bots, SPIRAL® is partnering with unauthorized login prevention tool Capy Puzzle CAPTCHA to make things easier for users with respect to online form registrations and member site logins, and to prevent fraudulent registrations and logins by bots.

Business outlook

Projects a 33.4% decline in FY2/19 operating profit, mainly because of investments aimed at an uplift in FY2/20

● FY2/19 outlook

The Company's FY2/19 forecast targets ¥5,800mn in net sales (up 12.8% YoY), ¥500mn in operating profit (down 33.4%), ¥490mn in recurring profit (down 34.6%), and ¥300mn in profit attributable to owners of parent (down 34.5%). After large-scale hiring (90 people) in FY2/18 and hiring 76 more people in 1H FY2/19 in order to lay the groundwork for achieving goals in the medium-term business plan described below, the Company expects a decrease in FY2/19 profits due to investments in training and educational costs for the new hires.

Business outlook

Forecast

	FY2/18		FY2/19 forecast		Change	
	Amount	% of total	Amount	% of total	Amount	%
Net sales	5,143	100.0	5,800	100.0	656	12.8
Operating profit	750	14.6	500	8.6	-250	-33.4
Recurring profit	749	14.6	490	8.4	-259	-34.6
Profit attributable to owners of parent	457	8.9	300	5.2	-157	-34.5

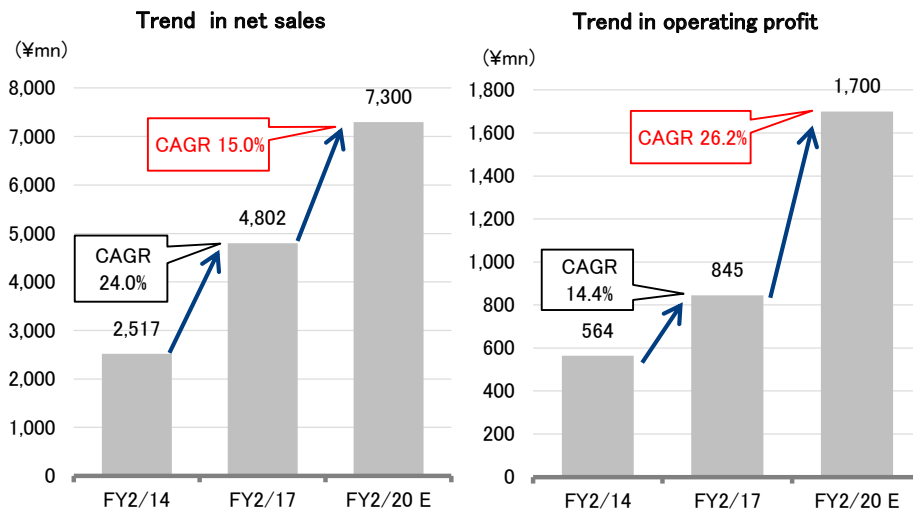
Source: Prepared by FISCO from the Company's financial results and results briefing materials

Medium- to long-term growth strategy

Medium-term plan goals unchanged at ¥7,300mn in net sales and ¥1,700mn in operating profit in FY2/20

1. Medium-Term Business Plan 2020 goals unchanged

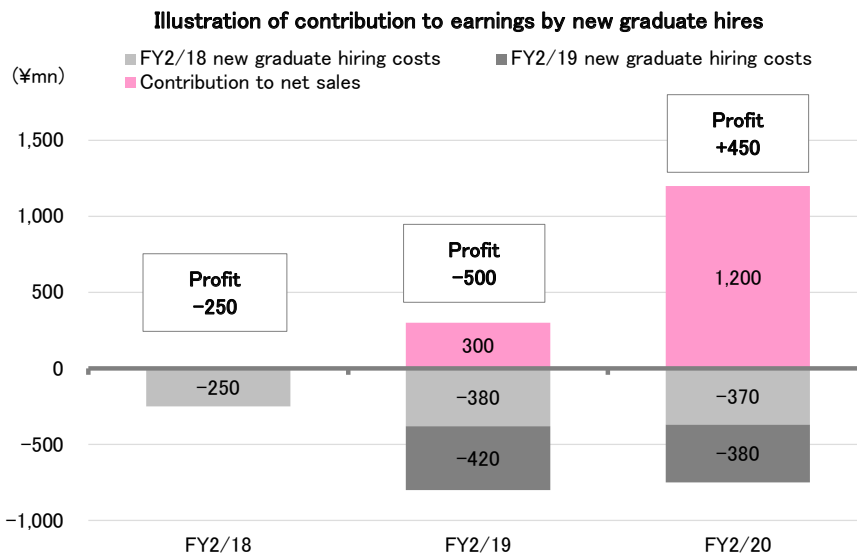
The Company announced the Medium-Term Business Plan 2020, a new medium-term business plan with FY2/20 as the final year, after completing the previous medium-term plan in FY2/17. The new plan sets goals of ¥7,300mn in net sales and ¥1,700mn in operating profit in FY2/20 that work out to compound average growth rates (CAGR) from FY2/17 of 15.0% in net sales (vs. 24.0% in the previous plan) and 26.2% in operating profit (vs. 14.4%).



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

Medium- to long-term growth strategy

The Company has not changed its goals for the medium-term business plan, despite the prospect of a decline in FY2/19 profits. This stance factors in earlier recognition of costs (training and educational costs, etc.) prior to sales contributions from major hiring with 90 people in FY2/18 and 95 people in FY2/19 (planned) aimed at realizing the plan goals. On its website, the Company explains: “Our Group does not immediately assign newly hired people to front-line operations. Instead, after a concentrated training period that lasts about six months in which new hires thoroughly learn our services and systems, we make assignment to Group companies, taking into account the person’s request and suitability. New hires do not contribute to results during the initial six months or so after being hired because of focus just on training. The Group’s investments are hiring costs as well as training and personnel costs in the subject period.” The Company thus expects a steep profit recovery in FY2/20 after a setback in FY2/18 and FY2/19.



Source: Prepared by FISCO from interviews

2. Priority measures

The Company uses a title of “Re-Innovation” for the new medium-term plan and seeks to become a “corporate group that contributes to a rich information lifestyle with a future.” It intends to implement the priority measures covered below to achieve this goal and the above-mentioned numerical targets.

(1) Promote “real × IT”

The Company intends to strengthen the contact point between real business and IT and pursue innovative businesses. The establishment of new subsidiaries was a specific example.

a) VOTE FOR

The Company established this entity in Mach 2017 to conduct “real × IT” business using the Seijiyama® political and election information website that existed internally. It aims to build voting systems that utilize blockchain and other new technologies that facilitate Internet-based voting with emphasis on Seijiyama® and Internet-based voting.

Medium- to long-term growth strategy

b) I LOVE

The Company created this entity to make further progress in the “I LOVE ShimoKitazawa” local revitalization project that had already been taking place internally and apply this knowhow to cultivate “towns capable of delivering enjoyable services on par with shopping malls and theme parks.” Specifically, it will pursue development of a new transaction format for single-coin donations, tips, and other small-sum transactions employing electronic regional currency.

(2) Group hiring and group development

Group companies will conduct common elementary education in the IT field in order to boost the overall knowledge level and reduce time spent on training front-line staff. With a goal of maximizing profits in FY2/20, the Company hired 90 people in FY2/18 (including new university graduates and recent graduates with work experience) and another 76 people in 1H FY2/19. There will be a respite in large-scale hiring after this phase.

Subsidiary BLOOM NOTES (established in October 2016) will support the group hiring and development. This entity’s main business is a customized personnel training service through arrangement of unique knowhow at customer companies into a program and assists in implementation, and the Company plans to harness the same program for development of its own Group personnel.

(3) Effective utilization of information assets at Group companies

The Company intends to further promote customer and product/service matching at Group companies and create new transactions and businesses.

3. Fund-raising initiative

The Company announced the following share buyback and fund-raising plan that targets future growth.

(1) Acquiring its own shares from subsidiaries

The Company acquired 500,000 shares of its stock owned by consolidated subsidiary PIPED BITS for ¥767mn. However, this transaction simply transferred ownership and does not affect consolidated results because it obtained the Company’s own shares held by a consolidated subsidiary. PIPED BITS originally purchased these shares in response to a request from a minority shareholder prior to formation of the holding company.

(2) Issuance of No.5 and No.6 new share warrants

Additionally, the Company adopted a resolution to issue new share warrants (No.5 250,000 shares, No.6 250,000 shares) for third-party allotment to Macquarie Bank Limited.

Key points are a ¥1,800 exercise price for No.5 (with no revisions to the exercise price) and a ¥1,800 bottom in the exercise price for No.6, but an ability to raise this level to over ¥1,800 by Company resolution. This puts the maximum number of shares available for allocation at 500,000 shares and supports a minimum procurement value of ¥900mn. Additionally, total outstanding issuance volume should not increase if warrants are exercised because the Company plans to utilize the above-mentioned treasury shares acquired from the subsidiary (500,000 shares). Existing shareholders hence would not incur dilution.

Furthermore, Macquarie Bank Limited, the recipient of the new share warrants, paid ¥5,872,000 for the warrants and is unlikely to exercise the rights until the shares trade at ¥1,800 or above in order to recoup its outlay. We expect gradual sale of acquired shares in the market after purchase using the warrants and contribution to better liquidity in the stock market once these shares enter the market.

Medium- to long-term growth strategy

While this fund-raising scheme is attractive to all stakeholders (the Company, existing investors, and the warrant recipient), it requires a share price of over ¥1,800. We think the Company hence must attain goals from the above-mentioned medium-term business plan.

■ Shareholder return policy

Maintaining a 30% dividend payout ratio in FY2/19 despite profit decline

The Company is committed to a 30% dividend payout ratio as a shareholder return policy. It paid a ¥21.0 annual dividend in FY2/18, which worked out to a 34.9% dividend payout ratio. While it expects lower profits in FY2/19 as explained above, the Company plans to pay a ¥12.0 dividend in order to keep the payout ratio at 30%.



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