COMPANY RESEARCH AND ANALYSIS REPORT

Startia Holdings Inc.

3393

Tokyo Stock Exchange First Section

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Index

Summary

The existing businesses' stable growth is covering the investment to grow the new businesses. Aiming to accelerate growth through a holding-company structure.

Startia Holdings Inc. <3393> (hereafter, also "the Company") provides digital marketing-related software and one-stop solutions for IT-related services for medium and small enterprises (SMEs) with 300 or fewer employees that cannot afford to hire an IT manager and which are not served by large system integration companies and network equipment dealers. The Company is working on establishing a stable income model through recurring services.

1. Both business segments performed steadily and achieved higher sales and profits. Net sales were a new record high.

The Company achieved higher sales and profits in the FY3/18 results, of net sales of ¥11,058mn (up 7.5% year-on-year (YoY)) and operating income of ¥358mn (up 35.1%). Net sales were a new record high. In the Digital Marketing segment, products and services including Web promotions consulting, the AR software COCOAR, and the MA tool BowNow performed well, and the previous fiscal year's operating loss became operating income. In the IT Infrastructure segment, although sales rose YoY, mainly driven by the sales of MFP and network devices, the Company pushed forward the implementation of promotions in order to acquire customers in the next fiscal period, and therefore operating income declined slightly. The main reason why the results exceeded the forecasts was that advertising costs and costs relating to the transition to the holding company were less than expected.

2. Transitioned to a holding-company structure from April. Is aiming for record high profits from quickly growing the profits of the two new business companies.

On April 1, 2018, the Company transitioned to a holding-company structure. In the future, it will pursue the growth of the Group as a whole by aiming to expand the profits of each Group company, centered on the four main business companies, three in Japan and one overseas. The structure of the business companies is the same as before, with Startia Inc., being responsible for the Infrastructure segment and Startia Lab, Inc. for the Digital Marketing segment. The newly established Startia Raise, Inc. will be responsible for the cloud storage and the RPA business, while Startia Asia Pte. Ltd., will be responsible for the overseas business. Startia Raise and Startia Asia are in an upfront investment period, but the aim is for both to become profitable within three years. If this is achieved, the Company can be expected to have in sight achieving record-high profits.

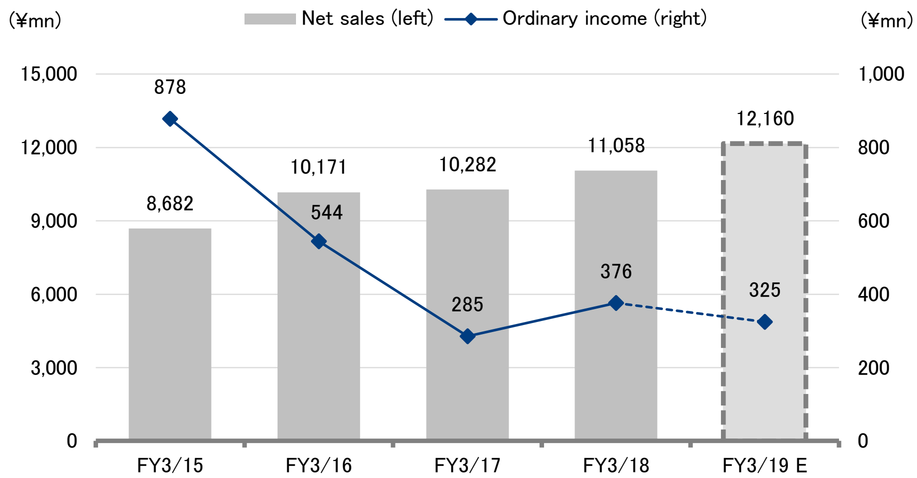
3. Outlook for FY3/19 is for higher sales but lower profits, due to the increase in upfront investment in the two new companies

For the FY3/19 full year, the Company is forecasting higher sales but lower profits, of net sales of ¥12,160mn (up 10.0% YoY) and operating income of ¥325mn (down 9.3%). As previously mentioned, it will be a period of upfront investment for two companies, Startia Raise and Startia Asia, which is the reason for the forecast of lower profits. Startia Raise is aiming to take on the new challenge of the early launch of the RPA business, and its policy is to accelerate the development of software and systems. Startia Asia will progress the expansion of Global Gateway (GG), which is a high-speed communication line service between Japan and China operated by a subsidiary, Startia Shanghai. In addition, it is aiming to capture business seeds through the VC business, mainly in Southeast Asia. Both these two companies are recording operating losses, but due to the stable growth of the two preceding firms, Startia and Startia Lab, the outlook is for operating profit to be secured on an all-company basis.

Key Points

- Results in the Digital Marketing segment bottomed-out and are recovering. Achieving profitability from the strong sales of COCOAR and BowNow. Recurring sales are also steadily growing
- Aiming to realize growth for the Group as a whole through the growth of each of the four domestic and overseas companies
- In FY3/19, profits at the two preceding companies will cover for the upfront investment in Startia Raise and Startia Asia to secure operating profit on an all-company basis

Result trends



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

Result trends

Achieved higher sales and profits through the steady progress of the IT Infrastructure segment and the return to profitability of the Digital Marketing segment

1. Overview of 1H FY3/18 results

In FY3/18, the Company achieved record-high sales and an increase in profits, with net sales of ¥11,058mn (up 7.5% YoY), operating income of ¥358mn (up 35.1% YoY), ordinary income of ¥376mn (up 31.9% YoY), and profit attributable to owners of parent of ¥613mn (compared to profit of ¥5mn in the previous fiscal year).

The Company upwardly revised its results forecasts on December 29, 2017, and ultimately the results greatly exceeded these revised forecasts. Profit attributable to owners of parent grew to ¥613mn due to temporary factors, including the recording of a gain on the sale of investment securities and a reduction in the tax burden on the recording of deferred tax assets.

Overview of FY3/18 results

(¥mn)

	FY3/17			FY3/18					
	1H	2H	Full year	1H	2H	Full year (E)	Full year	YoY	Vs. initial forecast
Net sales	4,774	5,508	10,282	5,372	5,686	11,000	11,058	7.5%	0.5%
Operating income	-119	385	265	221	137	270	358	35.1%	32.6%
Operating income margin	-2.5%	7.0%	2.6%	4.1%	2.4%	2.5%	3.2%	-	-
Ordinary income	-110	396	285	235	142	270	376	31.9%	39.3%
Profit attributable to owners of parent	25	-19	5	210	403	415	613	-	47.7%

Note: FY3/18 forecast is the revised forecast announced on December 29, 2017.
Source: Prepared by FISCO from the Company's financial results

In the two business segments, of the Digital Marketing segment and the IT Infrastructure segment, sales of the main products grew steadily and both secured increases in sales YoY. In the other business also (which is the corporate venture capital business, hereafter abbreviated to the CVC business), dividend income of ¥1mn was acquired. Due to these results, net sales achieved a new record high.

In profits, the Digital Marketing segment regained profitability in FY3/18 from the operating loss recorded in the previous fiscal year. In the IT Infrastructure segment, profits declined slightly YoY due to the pushing forward of the implementation of promotions to acquire customers in the next fiscal period. But even so, profits of around the same level as the previous fiscal year were secured. Due to these results, the operating loss in the CVC business was absorbed and operating income on an all-company basis increased significantly, up 35.1%.

Compared to the operating income forecast of ¥270mn that the Company announced on December 29, 2017, the result was 32.6% above forecast. The reasons for this were that as a result of the efficient use of advertising costs and personnel costs and that the estimates of the costs relating to the transition to the holding company structure were conservative, each of these three cost items were less than expected. Basically the entire amount of the costs relating to the holding company were incurred during FY3/18.

The factors pushing up net profit were the recording of a gain on the sale of investment securities and also a decline in the income tax adjustment amount of ¥110mn on the recording of deferred tax assets (this decline had a positive impact on profits). The recording of deferred tax assets was in relation to Startia Lab, which is responsible for the Digital Marketing segment. In this sense, it would seem that there is the prospect of Startia Lab achieving stable profits in the future.

Results by segment

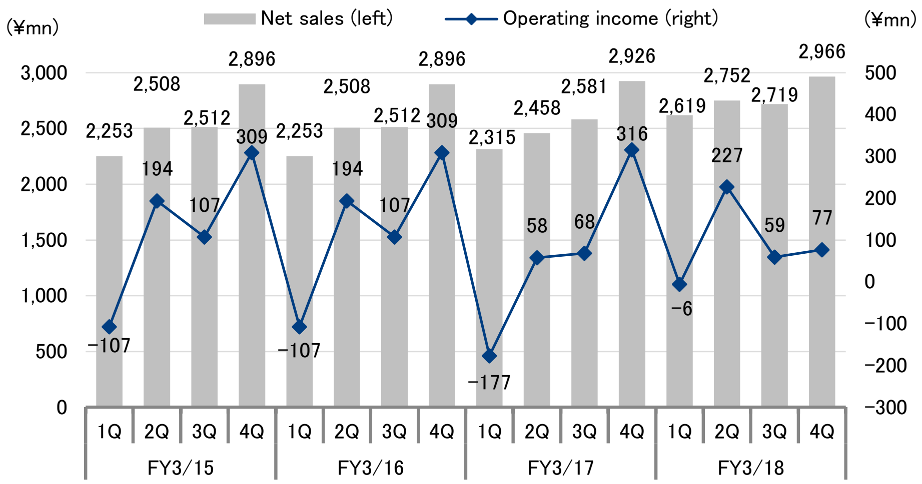
(¥mn)

	FY3/17				FY3/18					
	2Q	1H	2H	Full year	1H	YoY	2H	YoY	Full year	2H
Net sales	2,458	4,774	5,508	10,282	5,372	12.5%	5,686	3.2%	11,058	7.5%
Digital Marketing segment	446	795	1,015	1,810	868	9.1%	996	-1.8%	1,864	3.0%
IT Infrastructure segment	2,016	3,988	4,501	8,489	4,513	13.2%	4,720	4.9%	9,233	8.8%
Others segment	0	-	-	-	-	-	1	-	1	-
Net sales before adjustment	2,462	4,783	5,516	10,300	5,381	12.5%	5,718	3.6%	11,099	7.8%
Adjustment amount	-4	-9	-8	-18	-8	-	-32	-	-41	-
Operating income	58	-119	384	265	221	-	136	-64.4%	358	35.1%
Digital Marketing segment	0	-99	97	-2	32	-	68	-29.7%	101	-
IT Infrastructure segment	66	-3	311	308	200	-	104	-66.5%	305	-1.0%
Others segment	-7	-16	-17	-33	-12	-	-33	-	-45	-
Operating income before adjustment	58	-119	391	272	221	-	139	-64.3%	361	32.6%
Adjustment amount	0	-	-7	-7	-	-	-2	-	-2	-

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

Looking at how the results trended on a quarterly basis, net sales performed steadily across Q4, which is the demand period. There were two reasons why operating income did not grow in Q4 compared to in a typical year; the first was that the costs relating to the transition to the holding company structure were incurred in Q4, and the second was that, as is explained below, profit growth in the IT Infrastructure segment was sluggish due to the pushing forward of the implementation of promotions to acquire customers in the next fiscal period. Both are temporary factors and at FISCO, we think that profits in the Company's two existing business segments have clearly returned to a growth track.

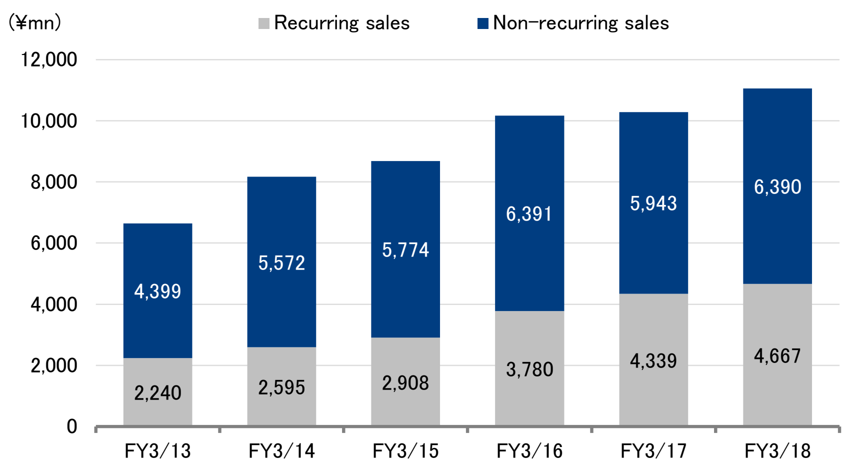
Result trends by quarter



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

For recurring sales, which the Company is focusing on growing, the main form of sales in the Digital Marketing segment has been changed from single-payment sales to cloud services, and they are steadily accumulating. In FY3/18, recurring sales increased 7.6% YoY to ¥4,667mn for a new record high. Also, the percentage of recurring sales to total net sales (the recurring ratio) was unchanged on the previous fiscal year at 42.2%.

Recurring sales and non-recurring sales



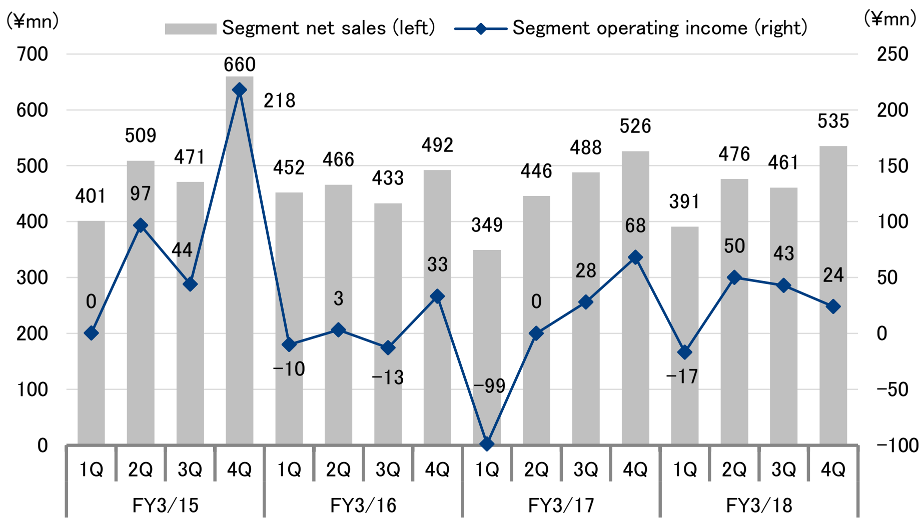
Source: Prepared by FISCO from the Company's results briefing materials

Achieved profitability through the strong sales of COCOAR and BowNow. Recurring sales continue to grow.

2. Digital Marketing segment

In the Digital Marketing segment, net sales were ¥1,864mn (up 3.0% YoY) and operating income was ¥101mn (compared to a loss of ¥2mn in the previous fiscal year).

Result trend in the Digital Marketing segment

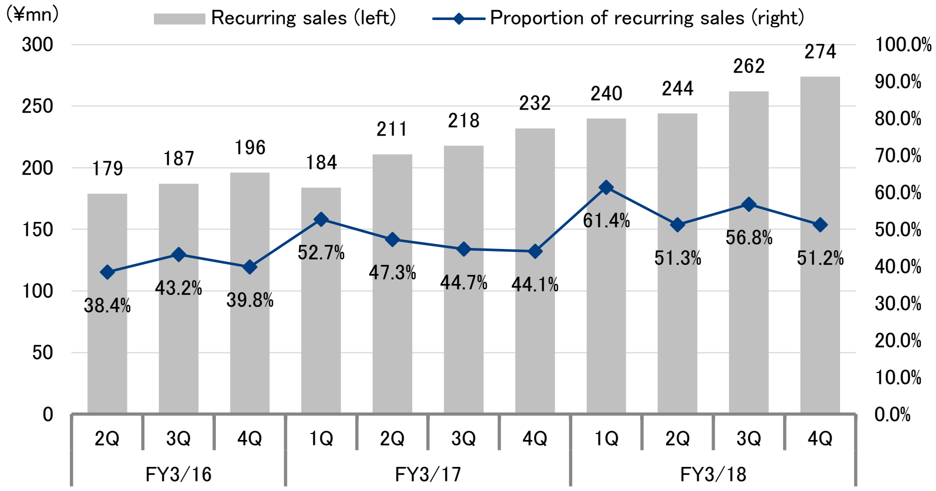


Source: Prepared by FISCO from the Company's financial results

In FY3/18, the strong performances of products and services, including consulting on Web promotions, the AR (Augmented Realty) creation software COCOAR, and the MA (Marketing Automation) tool BowNow, resulted in a recovery in profits. In particular, BowNow contributed to profits as the Company was able to create a sequence of first providing the freemium version and then working to convert users to paid members. The Company introduced the freemium version as the sales method from FY3/18, and it can be said that its effectiveness has been proven.

With the goal of stabilizing profits, the Company is aiming to grow recurring income from all the Group companies. In the same way, in the Digital Marketing segment also it has changed the main software sales method from completed sales to cloud-based sales. The transition to cloud-based sales also overlaps with the changes to the customer groups and alongside this, to their needs. Against this backdrop, the Digital Marketing segment's recurring income is continuing to grow steadily.

Trend in recurring sales in the Digital Marketing segment



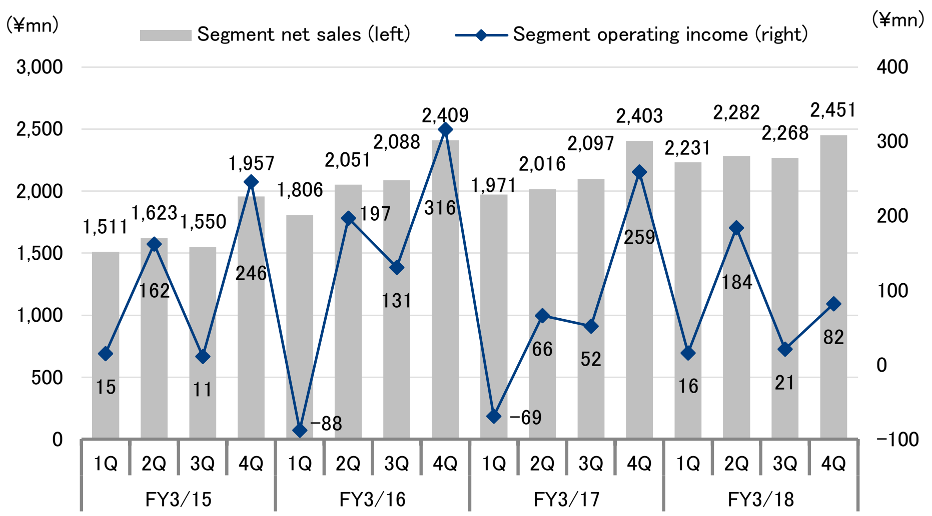
Source: Prepared by FISCO from the Company's results briefing materials

Net sales are steadily growing, driven by sales of MFP and NW devices. Operating income declined slightly due to the pushing forward of the implementation of promotions to acquire customers in the next fiscal period.

3. IT Infrastructure segment

The IT Infrastructure segment posted higher sales but slightly lower profit, with net sales of ¥9,233mn (up 8.8% YoY) and operating income of ¥305mn (down 1.0% YoY).

Result trend in the IT Infrastructure segment



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

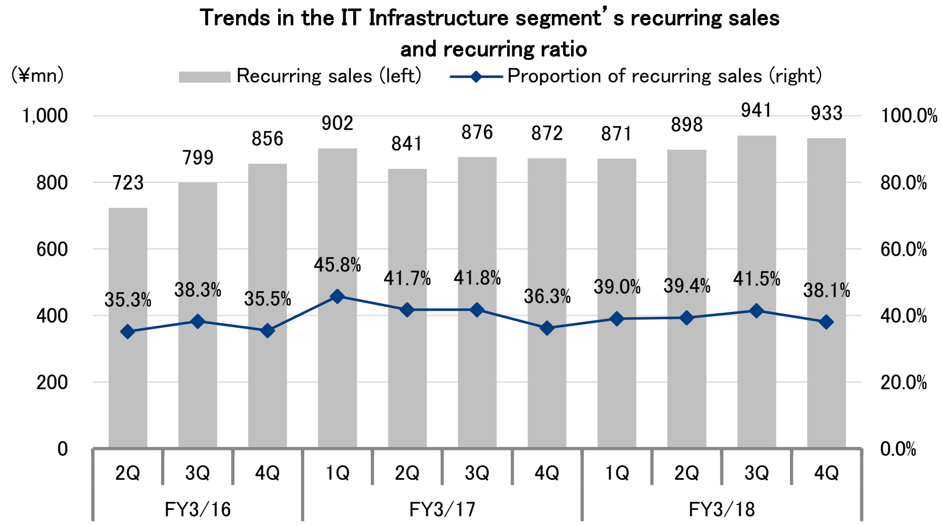
In FY3/17 under the slogan of "the customer 1st," the Company changed its sales structure in the IT Infrastructure segment from a product-orientated structure to a customer-orientated structure. In order to raise customer satisfaction, it judged it was necessary to allocate a single account manager to each customer as the point of contact and provide them with a one-stop solution. On its initial introduction, there was a phase of turmoil accompanying this change of structure and sales fell, but this turmoil had basically been eliminated by FY3/17 Q4.

FY3/18 became a fresh start from the change to the sales structure getting on track, and both sales and profits made steady progress from Q1 to Q3. By product, the mainstay MFP (multifunction printers) and NW (network) devices-related drove the segment's results.

From January 2018, the Company launched BiziSUKE as a new product. In January 2018, it began providing the new service, BiziSUKE, which is the comprehensive provision of several of the Company's products and services with the main aim of being "useful for business." Its biggest feature is the provision of the products in the IT Infrastructure segment, which are mainly provided by Startia itself, and the digital marketing-related products mainly provided by Startia Lab, in the form of a single package that crosses the segment. (The details on BiziSUKE are provided in the previous report of February 26, 2018.)

The Company has positioned BiziSUKE as one of its core products, and it pushed forward to Q4 the implementation of promotions toward the fully fledged acquisition of customers from the next fiscal period. This was one of the reasons for the slump in operating income in Q4. At FISCO, we think that this proactive measure by the Company is fully persuasive when considering that BiziSUKE is a product that symbolizes the pursuit of synergies between Startia, which is responsible for the IT Infrastructure segment, and Startia Lab, which is responsible for the Digital Marketing segment. Up to the present time, it has worked to grow sales through deeply cultivating diverse products vertically or developing them horizontally. But we think there is still plenty of room for further expansion, and we expect BiziSUKE to play the role of providing new points of entry for this.

Recurring sales declined temporarily on a quarterly basis due to the details described above, but they have been trending upward alongside the expansion of the customer base. But on the other hand, the Company also has many sources of flow income, such as from sales of NW devices. So depending on the period, the growth in flow income can be higher than that of recurring income, and therefore the recurring ratio continues to trend at around 40%.



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

Longer-term growth strategies

Aiming to realize growth for the Group as a whole through the growth of each of the three domestic companies and one overseas company

1. Transitioning to a holding company and building a new business structure

On April 1, 2018, the Company transitioned to a holding-company structure. It stated that the aim and purpose of this was "to not lag behind in responding to the changing times in the IT industry, and while keeping a watch on the latest technological trends, to promote timely decision making and flexible management."

In order to put this into practice, the Company reformed its business structure, changing to a structure in which it deploys its businesses through four core companies; three domestic business companies and one overseas company that supervises its Asia business. Specifically, the Company itself has changed its company name to Startia Holdings Inc., and it will concentrate on supervising the entire Group as a pure holding company. The new structure is that beneath it are the four business companies, of Startia (newly established as a business company) that is responsible for the IT Infrastructure segment, Startia Lab that is responsible for the Digital Marketing segment, Startia Raise (newly established) that is responsible for the cloud storage business and the RPA business, and Startia Asia (newly established as a Singapore corporation) that is responsible for the overseas business, and also the other Group companies. Alongside this change of structure, going forward the Company will pursue growth for the entire Group by aiming to expanding profits at each Group company, centered on the four main business companies.

Business domains of the four main business companies

Company name	Business domain	Subsidiaries and affiliates
Startia, Inc.	IT Infrastructure segment (excluding the cloud storage business)	BCMEDIA Co., Ltd., NOS Ltd., three affiliated companies
Startia Lab, Inc.	Digital Marketing segment	Mtame, Inc., Startia Taiwan
Startia Raise, Inc.	Cloud storage business, RPA business	-
Startia Asia Pte. Ltd.	Supervises the overseas business	Startia Shanghai Inc., XI'AN STARTIASOFT INC., Shanghai Find IT Intelligence Technology Co., Ltd.

Source: Prepared by FISCO from the Company's materials

Aiming for further growth by further supplementing the "Customer 1st" approach and increasing recurring income, centered on BiziSUKE

2. Startia

Startia (the new business company) is responsible for the IT Infrastructure segment. Alongside the establishment of Startia Raise, which is described below, the cloud storage services business (Secure SAMBA, as the product) has been separated from the IT Infrastructure segment that it belonged to up until recently. But the main products will be the same as previously and sales will continue as before, including of MFP and accompanying counter services, Startia Hikari, network devices, and business phones. So it seems that the profit structure will remain fundamentally unchanged from before.

Therefore, Startia's growth strategy would seem to be to take over the measures implemented up to the present time. In other words, it will work to improve customer satisfaction by thoroughly implementing the "Customer 1st" approach, and to support this, expand "overlapping sales," or in other words, maximize customers' LTV (lifetime value) per company.

One more growth strategy entails measures to increase recurring income, with the aim of stabilizing profits. It is considered that this will be centered on BiziSUKE, which is a new product that the Company launched in January 2018. BiziSUKE's biggest selling point is that it is able to use the Company's wide range of products comprehensively at low prices across the segment boundaries of the IT Infrastructure segment and the Digital Marketing segment. It has the merits of increasing convenience for customers and realizing synergies between the Company's two segments.

From FY3/19 onwards, the Company will grow profits by thoroughly implementing the "Customer 1st" approach and conducting measures to increase sales of BiziSUKE, in conjunction with strengthening the sales force through enhancing information systems

Service menu for the BiziSUKE new service

	Name of services	Content of services
1	BiziSUKE PC support	Telephone and remote support for devices, such as PCs, and for Office software
2	Special discount flat-rate plan	Provides a new maintenance service "flat-rate plan" at a special fee
3	Service to replace business phones free of charge	Replacement free of charge if there is a problem with the business phone provide by the Company
4	Anti-virus and spyware software	5 security software licenses can be used
5	Educational-support services	Computer schools, 20% off
6	Inexpensive BiziSUKE copy paper	Can purchase copy paper up to 20% off on the website
7	Inexpensive BiziSUKE office supplies	Can purchase office supplies on the smartoffice website at 5% off
8	BowNow Free	Can use a simplified version of the BowNow MA tool
9	AppGoose Free	Can use a simplified version of the AppGoose app-creation software
10	BiziSUKE Concierge	Telephone support with personnel allocated to each customer to confirm usage conditions and consult on individual problems.
11	Business succession support	Provides matching support for business succession, together with professional consultants
12	Online seminars	Provide online seminars, including on the latest IT, law, and management issues
13	Free books from Gokigen Business Publications	Can receive 3 e-books free of charge every month from Gokigen Business Publications
14	Security tests	Provides free in-house tests of the security-level surveys as a measure against targeted attack emails
15	Startia Hikari BiziSUKE Plan	Provides the Startia Hikari as part of Hikari Collaboration setup at a special price
16	Web production special plan	Provides at 10% off the total website production cost, and maintenance and renewal is provided free of charge

Note: the above description is at the time of the launch of the BiziSUKE service and the number of items will increase in the future.
Source: Prepared by FISCO from the Company's materials

Centered on COCOAR and BowNow, it is actively progressing sales growth through utilizing their respective high levels of functionality.

3. Startia Lab

The same as up to the present time, Startia Lab will mainly aim for business growth for the Digital Marketing segment. In relation to the transition to the holding company structure, its web promotion business will be split off and allocated to the newly established subsidiary Mtame. But when considering the roles of Startia Lab and the Group, we think there will be no major changes.

In the Digital Marketing segment, sales were sluggish and the results hit their lowest period in FY3/16 during the process of changing the customer groups, from the early adopter group up to that time (the group with a strong desire to introduce new products) to the majority group (group with an average desire to introduce new products). In order to break-out of this situation, the Company significantly changed its sales strategy, switching from an approach of providing various types of software to a cloud-based approach. In conjunction with this, it grouped its various software, branded the software-product group as Cloud Circus, and introduced a framework to provide them as a package on the Cloud.

The main software provided by Startia Lab and the Group

Cloud Circus		
Name	Function	Distinguishing characteristics
ActiBook	e-book production tool	Security function that blocks forwarding to other users, log analysis into depth of content is possible
ActiBook AR COCOAR	A tool for creating AR (Augmented Reality) content	Increases the effective use of flyers, directing routes cannot be compared, measures the effect of flyer
ActiBook Docs	Document management tool	Shares materials among all sales people, allows materials to be improved based on data, enables viewing of on-site negotiations with customers
Content management system (CMS) Blue Monkey	Tool for the production and management of websites	Provides long-tail search engine optimization (SEO) function, offers work flow function with updating rights for page setting
Plusdb	Tool for producing and managing databases	Enables the generation of product databases, can be installed on existing websites, allows searches based on complex (detailed) conditions
AppGoose	Tool for producing application software programs	Simplifies online-to-offline marketing
Bow Now	Marketing automation (MA) tool	Enables the management of information on prospective customers and the nurturing of these customers, allows the configuration of one-to-one email contacts, produces content for limited parties

Source: Prepared by FISCO from the Company's materials

Moreover, from FY3/18 the Company decided to introduce the freemium model. Freemium can be described as a business model in which the basic functions are provided for free, and customers are billed for the portion that goes beyond a certain amount and for special functions in the form of pay-as-you-go fees or additional fees. It can be said to be a model similar to F2P (free to play) in online gaming. Up to the present time, the Company has sequentially added freemium to its product offerings, starting with "creca," which is software for creating landing page websites for smartphones, then the app-creation software App Goose, and then BowNow.

As previously described, the Digital Marketing segment's FY3/18 results were higher sales and a return to profitability. Compared to the peak in the past, profits are still at a low level, but in the context of the change to the customer group, at FISCO we think it is very significant that it was able to return to profitability. Also, in the same way it is extremely significant that freemium has been introduced as a new business model, and that the sequence for BowNow, of freemium members being converted into fee-paying members, has been demonstrated and that it is contributing to profit growth.

Up until presently, the Digital Marketing segment has handled COCOAR and BowNow, together with the e-book ActiBook, as the three core products. Going forward, expectations are particularly large for COCOAR and BowNow. For COCOAR, the plan is to grow profits by strengthening measures for AR, characters, and real games and increasing the number of COCOAR active users. For BowNow, the policy is on the one hand to continue the freemium strategy and to work to increase the number of fee-paying customers, and on the other hand to actively grow sales to small- and medium-sized enterprises (SMEs) by appealing to them for its excellent cost performance.

Constituted of Secure SAMBA and the RPA business. Has realized the launch of the RPA business at an early stage and is aiming for it to become profitable as a business company.

4. Startia Raise

Startia Raise was established alongside the recent transition to the holding company. Its business domain is constituted of two businesses, the cloud storage business and the RPA business. These two are sometimes collectively referred to as the IT solutions business.

The cloud storage business consists of the Secure Samba service, which up until FY3/18 was included in the IT Infrastructure segment. Alongside the transition to the holding company, it was separated from the IT Infrastructure segment and transferred to Startia Raise. Secure SAMBA is a SaaS-type online storage service, and its features include that customers can share files between sites with the same sense as sharing them on a file server within a company (in other words, they can operate in the same environment outside of the office as inside the office). From the viewpoint of BCP (business continuity plans), contracts for it grew significantly after the earthquake. It has also been attracting attention in recent years from the viewpoint of reforms to ways of working.

Secure SAMBA has already expanded its customer base and is contributing to profits. But in the other hand, it is also a fact that, based on the rising needs described above, the number of companies entering this market is increasing and the competitive environment is intensifying. The Company's policy is to use the further strengthening of information security as the point of entry to actively propose to the SMEs that are considering introducing teleworking the creation of an environment in which their employees can work "anywhere and at any time."

The RPA business consists of using RPA (Robotic Process Automation) technologies to provide tools and services that contribute to improved operational efficiency, mainly in administrative departments (such as general affairs, personnel, and accounting). While using the term Robotic, it involves not only work by robots as machines, but carrying out other tasks, like software that inputs data.

The policy for the RPA business is to develop a RPA market for SMEs in Japan by providing support for their selection and introduction of the most appropriate tools and realizing coordination with various business application tools. It is currently at the stage of upfront investment, including software development, product launches, and systems development.

In terms of the profitability of Startia Raise, it seems that the Secure SAMBA business is already profitable. However, the RPA business is in the upfront investment period, so the present time Startia Raise is unprofitable as the total from both businesses. For RPA itself, the technology has been growing rapidly since around 2016, and it is considered that the extent of the spread of its use among the Company's main target group of SMEs is extremely low. Or in other words, if the Company can create products and services that match the needs of SMEs, then this business has the potential to grow quickly. It intends to rapidly start the RPA business with the aim of it contributing to profits at an early stage.

The Startia Shanghai high-speed communication line service has become profitable. Going forward, the focus will be on the deployment of COCOAR in China through Shanghai Find IT Intelligence Technology.

5. Startia Asia

Startia Asia is the operating company that supervises development of the Company's overseas businesses in Asia. There are three companies under its umbrella: Startia Shanghai, XI'AN STARTIASOFT, and Shanghai Find IT Intelligence Technology.

Startia Shanghai is the Company's wholly-owned subsidiary and it operates the Global Gateway (GG) service, which is a high-speed communication line service between Japan and China. Its customers are Japanese companies with bases in China and individuals. Startia Shanghai has secured the lines through a collaboration with a major Chinese carrier and it provides its customers with high-speed Internet services up to 10 times faster than normal (note: improvements from 0.4Mbps to 5.0Mbps have been confirmed in customer offices).

XI'AN STARTIASOFT is an equity method affiliate in which the Company's investment ratio is 30%, and it conducts a software planning and development business. In terms of its relation with the Company, it is contracted by Startia Lab to develop software. Its results seem to fluctuate greatly over time, and at FISCO we think its impact on the Company's results is limited.

Shanghai Find IT Intelligence Technology was established in June 2017 through investments of 40% by Startia Lab, 20% by XI'AN STARTIASOFT, and 10% each by four Shanghai printing companies. Its business objective are sales in the Chinese market, mainly of the AR creation software COCOAR

At FISCO, we think Startia Asia's growth strategy has two core elements; grow profits at Startia Shanghai and achieve profitability at Shanghai Find IT Intelligence Technology. Within these, it seems that Startia Shanghai already became profitable in FY3/18 as a result of the steady increase in the number of GG customers. It would appear that for Startia Shanghai, this profitability includes from the contribution of the launch in October 2017 of Global Gateway for AWS (please refer to the previous report of 26 February, 2018, for details on Global Gateway for AWS). Profits are expected to grow even further in FY3/19.

On the other hand, at FISCO we think Shanghai Find IT Intelligence Technology will continue to make a loss in FY3/19 from sales of COCOAR. Although it is considered that the excellent product qualities of COCOAR are highly evaluated in China, it is struggling to increase sales due to various problems, such as local business practices and local employee management. Currently, the anticipated scenario is that it will acquire 300 contracts by FY3/20 and become profitable, but we shall be paying attention to developments going forward.

One more point with regards to Startia Asia is the CVC business. It is now clear that in the future, Startia Asia will be mainly responsible for conducting the CVC business. In the background to this is the fact that Startia Asia President Hiraoka is also presently the head of the CVC business and that it is easier to collect information relating to venture investment in Singapore, which is the base for his activities. The Company's CVC business is not limited to Japan, and it intends to capture business seeds by establishing footholds in the Southeast Asia region, where the speed of economic growth is fast.

Outlook

Profits at the two existing business companies will cover for the upfront investment in Startia Raise and Startia Asia to secure operating profit on an all-company basis

For FY3/19, the Company forecasts higher sales but a decline in profits, with net sales of ¥12,160mn (up 10.0% YoY) operating income of ¥325mn (down 9.3% YoY), ordinary income of ¥325mn (down 13.7% YoY), and profit attributable to owners of parent of ¥178mn (down 71.0% YoY).

Continuing on from the previous fiscal period, net sales are again forecast to achieve a new record high. The main reason for the decreases in operating income and ordinary income will be the previous described upfront investment to grow the new businesses. Profit attributable to owners of parent will greatly decrease, but this will be as a reaction to the temporary factors in the previous fiscal period (a gain on the sale of shares and a decrease in the tax burden from the recording of deferred tax assets).

Overview of FY3/19 forecast

(¥mn)

	FY3/18			FY3/19					
	1H	2H	Full year	1H	YoY	1H (E)	YoY	Full year (E)	YoY
Net sales	5,372	5,686	11,058	5,814	8.2%	6,346	11.6%	12,160	10.0%
Operating income	221	137	358	46	-79.1%	279	103.7%	325	-9.3%
Operating income margin	4.1%	2.4%	3.2%	0.8%	-	4.4%	-	2.7%	-
Ordinary income	235	142	376	46	-80.4%	279	97.0%	325	-13.7%
Profit attributable to owners of parent	210	403	613	25	-88.1%	153	-62.1%	178	-71.0%

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

In April 2018, the Company transitioned to a holding-company structure and changed to a developmental structure for its four main businesses. Based on this, at FISCO we think it is possible that it will also change the business segments for which it discloses information.

As the breakdown of Company's results forecasts for FY3/19, it has announced forecasts for each Group company (please refer to the table below). Startia Raise and Startia Asia will record operating losses due to the upfront investment. But these losses will be absorbed by the profits from Startia's IT Infrastructure segment and Startia Lab's Digital Marketing segment, and so profits will be secured on an all-company basis. The reason why the consolidated operating income forecast does not match the total operating income forecasts of the four companies is that the results of the holding company (Startia Holdings) are not listed and there is a separate adjustment amount.

FY3/19 results forecasts by Group company

(¥mn)

	Consolidated	Startia		Startia Lab		Startia Raise	Startia Asia
		FY3/19	FY3/18	FY3/19	FY3/18		
Net sales	12,160	9,446	8,824	2,128	1,858	411	166
Gross profit	5,466	3,828	3,629	1,351	1,110	165	122
Operating income	325	171	-	108	-	-98	-20

Note: figures for Startia and Startia Lab include the profits of their respective subsidiaries and affiliates. The results forecasts of each business company include internal transactions within the Group.
Source: Prepared by FISCO from the Company's results briefing materials

At FISCO, we do not feel there is anything particularly wrong with these profits-composition forecasts by Group company. Recurring income is growing in the IT Infrastructure segment and the Digital Marketing segment, and we think that a profit structure has been completely established. On the other hand, as the target is clearly to conduct upfront investment for Startia Raise and Startia Asia, if steady progress is made, we consider that it is fully possible that they will become profitable within three years, which is the Company's aim.

With regards to FY3/19, at FISCO we think that the Company has no choice but to accept the decline in profits due to the upfront investment, but that by FY3/20, the further growth in the profitable businesses will combine with the shrinking of the losses in the unprofitable businesses to achieve higher sales and profits YoY. Looking to the future, we consider that at the stage that all four business companies become profitable, the Company will have in sight new record high profits. In this sense, we think the biggest point to focus on for FY3/18 is not short-term results, but the progress made in the upfront investment.

Condensed income statements and key performance indicators

(¥mn)

	FY3/15	FY3/16	FY3/17	FY3/18	FY3/19	
					1H (E)	Full year (E)
Net sales	8,682	10,171	10,282	11,058	5,814	12,160
YoY	6.3%	17.1%	1.1%	7.5%	8.2%	10.0%
Gross profit	4,356	4,609	4,536	4,914	-	-
YoY	2.6%	5.8%	-1.6%	8.3%	-	-
Gross profit margin	50.2%	45.3%	44.1%	44.4%	-	-
SG&A expenses	3,609	4,106	4,271	4,555	-	-
YoY	5.7%	13.8%	4.0%	6.7%	-	-
Ratio of SG&A expenses to sales	41.6%	40.4%	41.5%	41.2%	-	-
Operating income	747	503	265	358	46	325
YoY	-10.0%	-32.6%	-47.3%	35.1%	-79.2%	-9.3%
Operating income margin	8.6%	5.0%	2.6%	3.2%	0.8%	2.7%
Ordinary income	878	544	285	376	46	325
YoY	2.6%	-38.0%	-47.6%	31.9%	-80.4%	-13.7%
Profit attributable to owners of parent	592	253	5	613	25	178
YoY	37.2%	-57.3%	-97.7%	-	-88.1%	-71.0%
Adjusted EPS (¥)	58.09	24.82	0.58	60.74	2.51	17.70
Adjusted DPS (¥)	10	9	9	12	3	9
Adjusted BPS (¥)	389.90	400.57	393.04	478.21	-	-

Note: Conducted a 2-for-1 stock split on October 1, 2015
Source: Prepared by FISCO from the Company's financial results

Condensed balance sheet

(¥mn)

	FY3/14	FY3/15	FY3/16	FY3/17	FY3/18
Current assets	4,051	4,057	4,700	4,498	6,064
Cash and deposits	2,247	2,335	2,638	2,221	3,718
Notes and accounts receivable	1,438	1,319	1,597	1,772	1,684
Other	366	403	465	505	662
Non-current assets	1,115	1,604	1,828	1,396	1,789
Tangible non-current assets	105	150	172	108	99
Intangible non-current assets	502	811	927	531	398
Investments and other long-term assets	507	642	728	756	1,291
Total assets	5,167	5,662	6,529	5,894	7,853
Current liabilities	1,661	1,684	1,878	1,712	2,388
Trade accounts payable	618	565	640	681	766
Short-term borrowings, etc.	-	-	333	346	400
Other	1,043	1,119	905	685	1,222
Non-current liabilities	12	-	561	211	600
Long-term borrowings	-	-	559	200	466
Other	12	-	1	11	133
Shareholders' equity	3,450	3,960	4,095	3,932	4,455
Capital stock	795	824	824	824	824
Additional paid-in capital	937	965	965	926	926
Retained earnings	1,717	2,208	2,344	2,268	2,791
Treasury stock	-0	-38	-38	-87	-87
Accumulated other comprehensive income	42	15	-11	37	375
Subscription rights to new shares	1	2	2	-	-
Net assets	3,493	3,977	4,088	3,970	4,865
Total liabilities and net assets	5,167	5,662	6,529	5,894	7,853

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

Consolidated statement of cash flows

(¥mn)

	FY3/14	FY3/15	FY3/16	FY3/17	FY3/18
Cash flow from operating activities	638	768	366	155	869
Cash flow from investing activities	-286	-595	-762	-165	378
Cash flow from financing activities	-24	-82	705	-403	276
Changes in cash and cash equivalents due to currency exchange fluctuations	-0	48	-24	-6	-5
Absolute change YoY in cash and cash equivalents	326	139	284	-420	1,518
Balance of cash and cash equivalents at start of fiscal year	1,868	2,195	2,335	2,620	2,199
Balance of cash and cash equivalents at end of fiscal year	2,195	2,335	2,620	2,199	3,718

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

Shareholder returns

In FY3/18, increased the dividend ¥3 YoY to ¥12 to commemorate the transition to the holding company

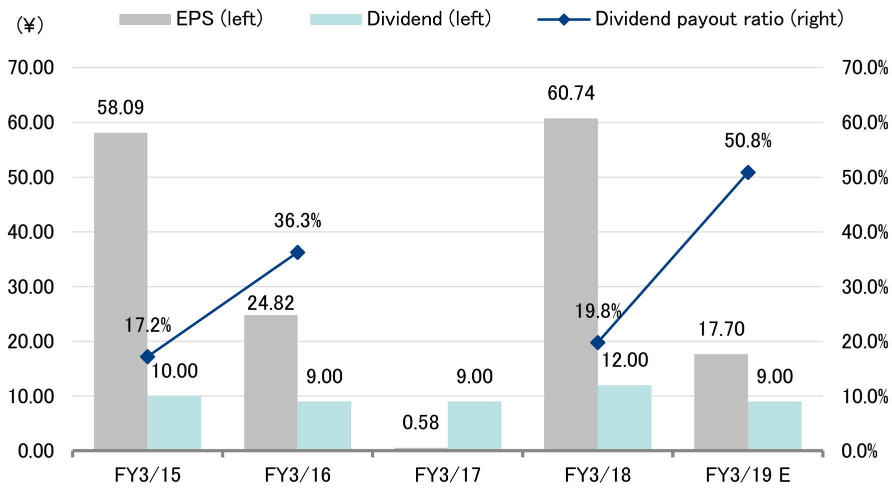
The Company values its individual shareholders and actively returns profits to them. Dividends are fundamental to that approach, and its basic policy is to determine the dividend while maintaining a balance with supplementing internal reserves to invest in growth for the future. In the past, the Company adopted a rule of a dividend payout ratio of 10% as a guideline, but from FY3/15, it raised the dividend payout ratio target for the ordinary dividend from 10% to 15%.

For FY3/18, the Company announced a dividend forecast that was unchanged YoY of an annual dividend of ¥9 (interim dividend ¥3, period-end dividend of ¥6). But in order to commemorate the transition to a holding company, in April 2018 it decided to increase the dividend ¥3 YoY for an annual dividend of ¥12 (interim dividend ¥3, period-end dividend ¥9) and a dividend payout ratio of 19.8%.

It has announced the FY3/19 dividend forecast, of an annual dividend of ¥9 (interim dividend ¥3, period-end dividend ¥6), as it will not pay the commemorative dividend of ¥3. Based on the earnings per share (EPS) of ¥17.70, the dividend payout ratio will be 50.8%.

At FISCO, we think that the payment of a commemorative dividend in March 2018 reflects the Company's approach of prioritizing returns to shareholders and its confidence that results will grow in the future. On the other hand, we consider that the FY3/19 dividend forecast indicates that in order to return profits to shareholders in accordance with results, it has for the time being reviewed the payment and decided on an ordinary distribution.

Trends in EPS, dividend, and dividend payout ratio



Source: Prepared by FISCO from the Company's materials

Information security

Has acquired several third-party certifications that it utilizes as the guidelines for establishing and strengthening the in-house structure

The Company provides its SME customers with advisory and consulting services, as well as products, on information security. Therefore, the Company itself is naturally strongly aware of the importance of information security and conducts measures for it. Specifically, it has acquired ISMS certification, which is an information security management system (ISO/IEC 27001), and PMS certification, which is a personal information protection and management system (JIS Q 15001). By acquiring these third-party certifications, the Company is supporting compliance with laws and regulations, the mitigation of risks, continuous improvements, and the strengthening of brands within the Startia Group. In addition, it is working to improve the trust in which it is held by stakeholders inside and outside of the Company.

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