

Digital Arts Inc. (2326)



FY03/19 Consolidated Financial Results
For the Second Quarter ended 30
September 2018
Reference Slides
30 September 2018

FY03/19 Second Quarter Financial Results

KEY FINANCIAL POINTS

- ① **Increased acknowledgement as a total security solution provider in the public sector market, leading to record sales**
 - Cultivated sales channels that were able to provide a more comprehensive security solutions, when the local governments were implementing security measures as part of the Ministry of Internal Affairs and Communications measures the year before last
 - As a result of partnering and selling “i-FILTER” ver.10 and “m-FILTER” Ver.5 with such sales channels, not only were we able to increase our sales but were also able to increase our presence in the market

- ② **There was an increase in new demand, and by actively pursuing sales promotion activities via strategic upfront investment, potential projects have been obtained**
 - In domestic business, we continue to aggressively promote sales activities in response to expanding demand
 - In overseas operations, despite our efforts to strengthen the organizational structure, etc., due to the revision of our mid- to long-term product strategy and sales strategy, we reorganized our group. Although costs were incurred ahead of schedule in the first half of the year, the cost is expected to shrink in the second half due to the group restructuring effect.

- ③ **Continual growth of Digital Arts Consulting**
 - Contributing to the growth of group sales, driven by the growing awareness of security human resources shortage and strengthening of information security measures

FY03/19 Second Quarter Financial Results

**CONSOLIDATED RESULTS
HIGHLIGHTS**

Consolidated
Net Sales

JPY 2,764 million (YoY +JPY 296million/+ 12.0%)

Significant growth due to the increased recognition in the public sector as a comprehensive security solution provider and a favorable consumer market

Operating
Income

JPY 1,036 million (YoY +JPY 113 million/+ 12.4%)

Despite the costs in association with overseas sales initiatives and group restructuring, the increase in sales outweighed the costs and resulted in a higher operating income compared to the previous year

Ordinary
Income

JPY 1,040 million (YoY +JPY 107 million/+ 11.5%)

With the increase in operating income, the ordinary income also increased

Net Income
Attributable to
Owners of Parent

JPY 992 million (YoY +JPY 373 million/+ 60.4%)

Due to the tax reducing effect of the US subsidiary closure, the quarter's results have increased significantly

Consolidated Results

(million JPY)

	FY03/18 Second Quarter	FY03/19 Second Quarter	YoY Growth	FY03/19 Forecast
Net Sales	2,468	2,764	+12.0%	5,800
Gross Profit	2,000	2,237	+11.8%	4,700
Selling, General and Administration Expense	1,078	1,201	+11.4%	2,200
Operating Income	922	1,036	+12.4%	2,500
Ordinary Income	932	1,040	+11.5%	2,500
Net Income Attributable to Owners of Parent	618	992	+60.4%	1,619
ROE	11.3%	15.0%	—	—

※ "FY03/19 Forecast" is the forecast announced on 8 May 2018

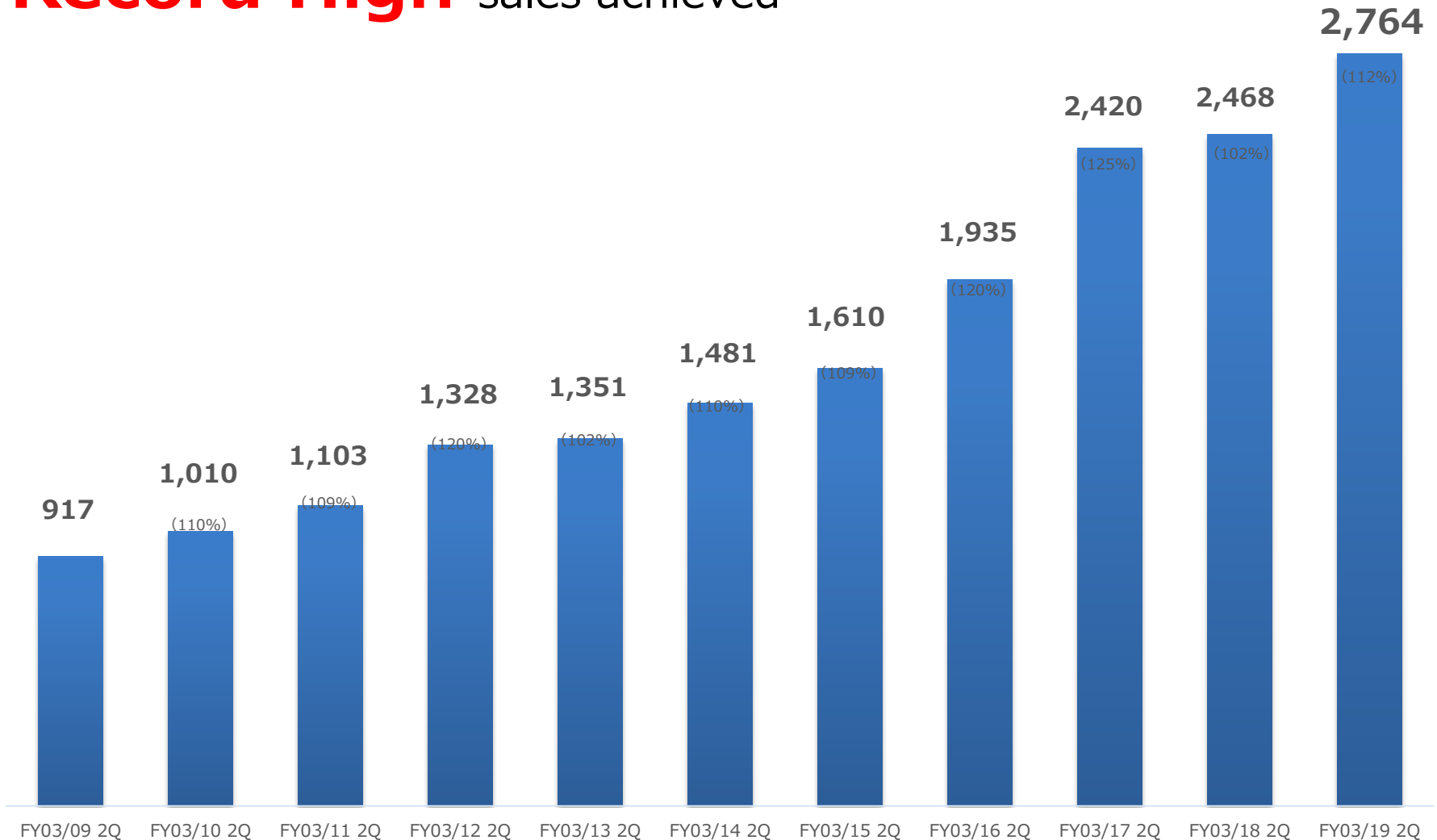
Non-Consolidated Results

(million JPY)

	FY03/18	FY03/19 Second Quarter	YoY Growth	FY03/19 Forecast
Net Sales	2,474	2,739	+10.7%	5,600
Gross Profit	1,978	2,233	+12.9%	4,250
Selling, General and Administration Expense	956	1,046	+9.4%	1,900
Operating Income	1,021	1,186	+16.2%	2,350
Ordinary Income	1,030	1,190	+15.5%	2,350
Net Income	734	818	+11.4%	1,598
ROE	12.0%	12.1%	—	—

Record High sales achieved

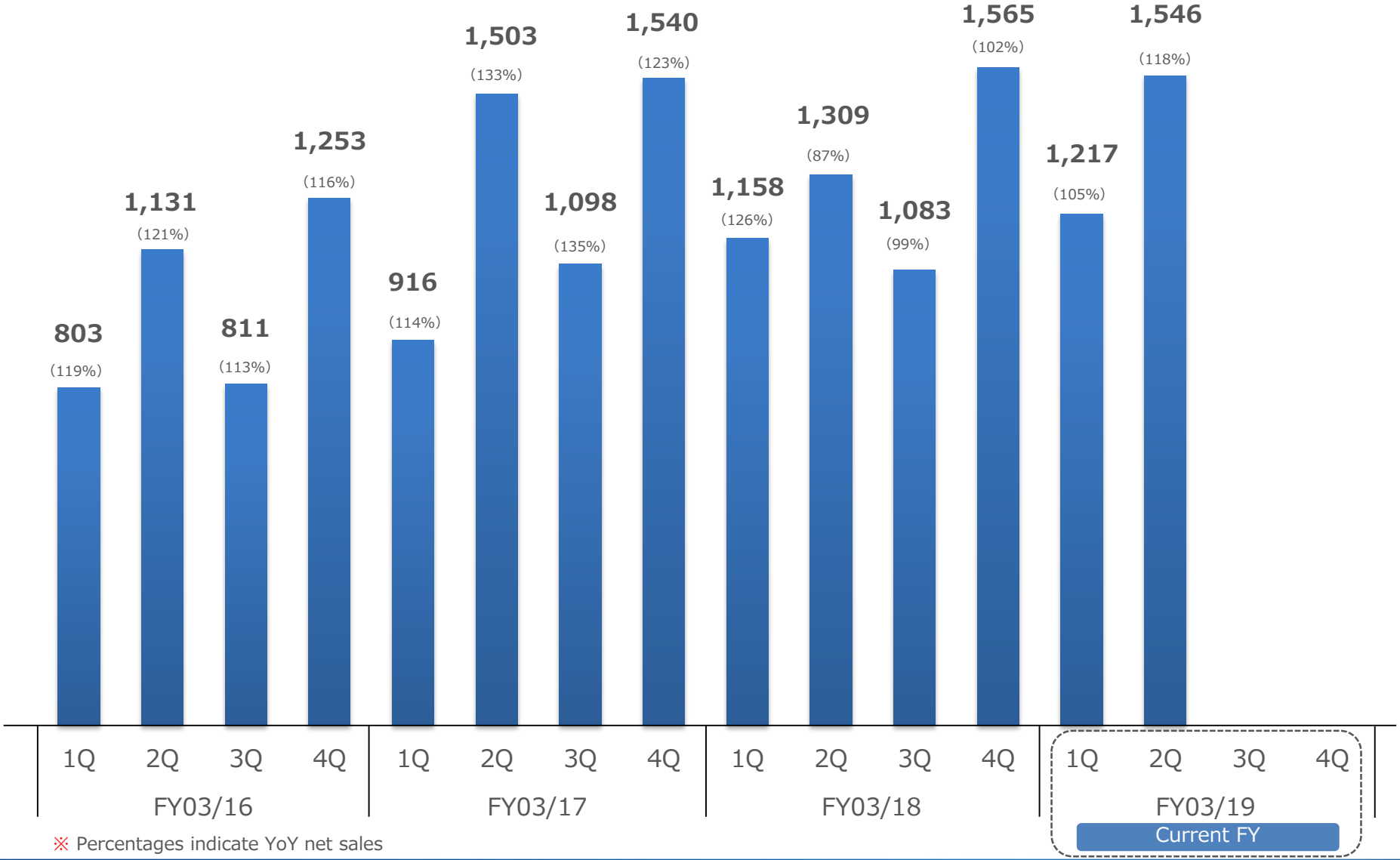
(million JPY)



※ Percentages indicate YoY net sales

Increased acknowledgement as a total security solution provider in the public sector market, leading to growth in sales

(million JPY)



※ Percentages indicate YoY net sales

- In Japan, we actively promoted sales promotion targeting new demand. In the overseas market, SG&A expenses temporarily increased due to organizational expansion centered on US subsidiaries and group restructuring due to revisions to medium- to long-term product and sales strategies.

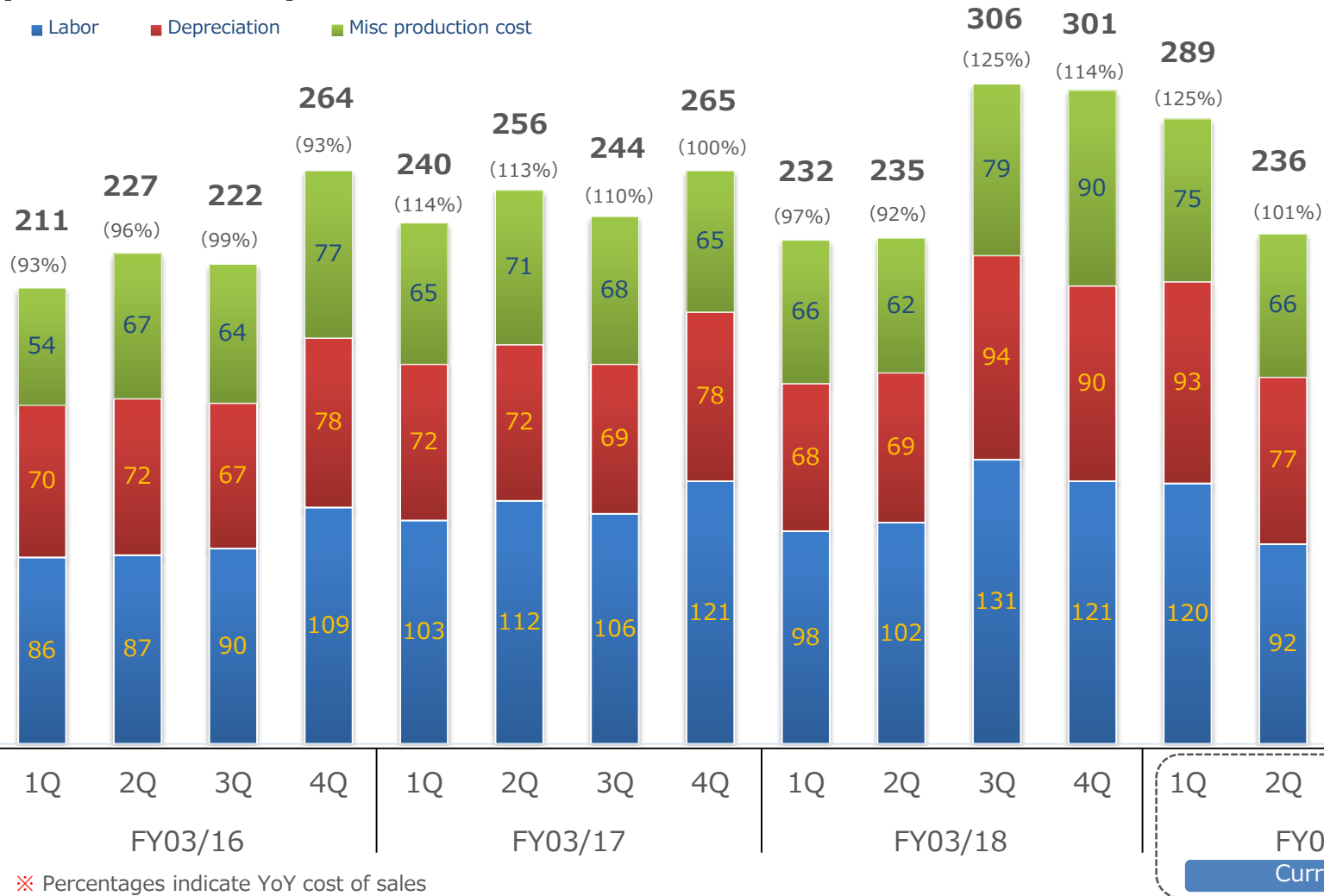
(million JPY)

	FY03/18 Second Quarter	FY03/19 Second Quarter	YoY	Key Factors
Cost of Sales	467	526	+59	
Labor	200	213	+12	Due to the growth of consulting subsidiary
Depreciation	137	170	+32	Depreciation attributable to release of new products
Transfer to other accounts Misc production cost	128	142	+13	
Selling, General and Administrative Expenses	1,078	1,201	+122	
Personnel Expenses	540	540	△0	
Publicity	163	183	+19	Caused mainly by the aggressive sales promotion targeting domestic market
Others	373	477	+103	Costs due to the organizational growth centered on US subsidiary and group restructuring costs

Despite the temporary increase in depreciation due to the release of a new product, the second quarter costs were on par with the previous FY

(million JPY)

■ Labor ■ Depreciation ■ Misc production cost

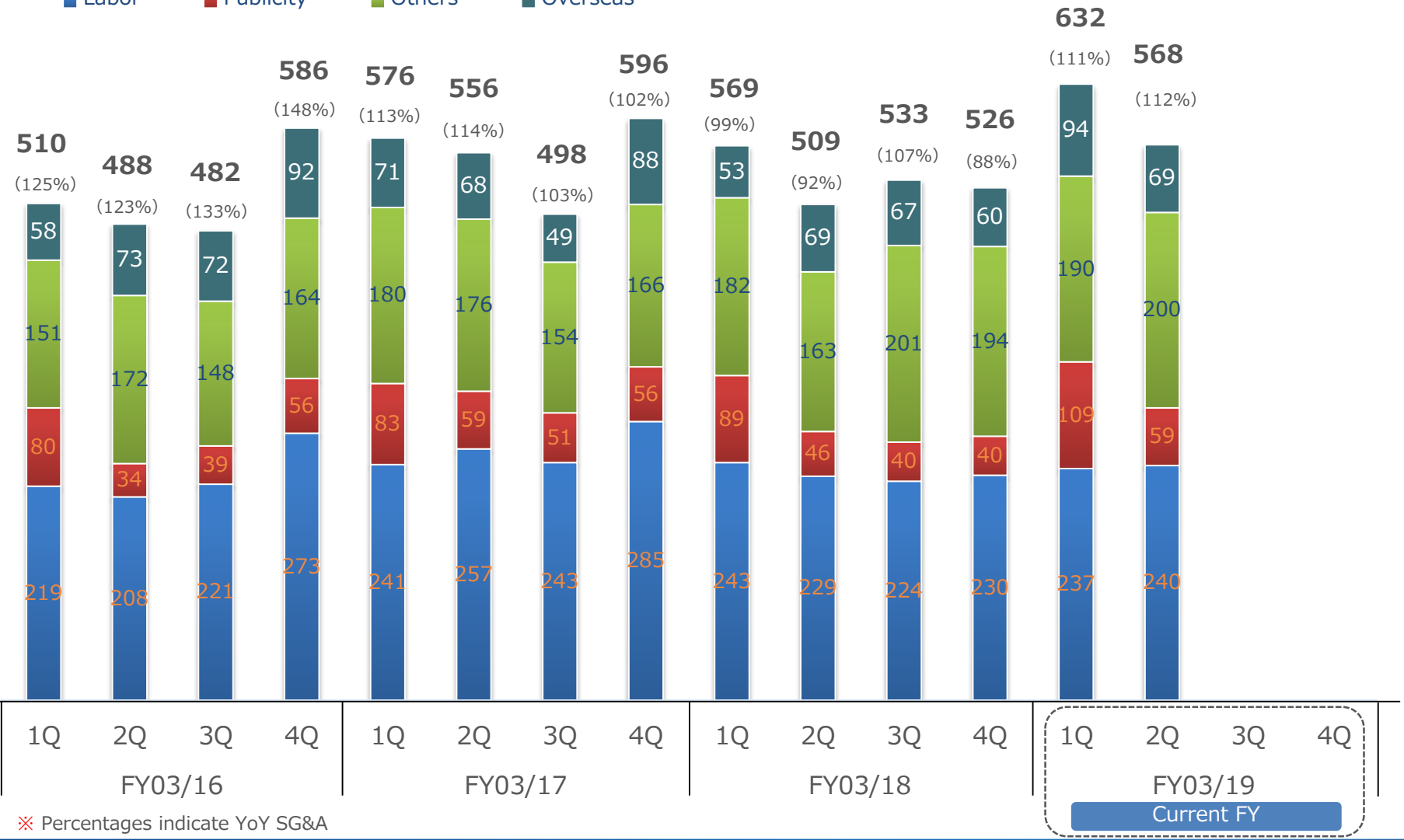


※ Percentages indicate YoY cost of sales

SG&A expenses temporarily increased due to strategic upfront investment and group restructuring

(million JPY)

■ Labor ■ Publicity ■ Others ■ Overseas



※ Percentages indicate YoY SG&A

FY03/19 Second Quarter Financial Results

BY MARKET

- +12.0% YoY growth in consolidated net sales
- Enterprise : +3.9% growth due to the concentration of large projects due in the second half of the FY
- Public : +20.2% growth due to strong demand for new products
- Consumer : +31.7% growth due to favorable market in the MNVO sphere, etc.

Consolidated Net Sales

Net Sales : JPY **2,764** million (JPY+296 million/ +12.0% YoY)

Enterprise

Net Sales : JPY **1,419** million (JPY +52 million/+3.9% YoY)

Public

Net Sales : JPY **1,108** million (JPY +186 million/+20.2% YoY)

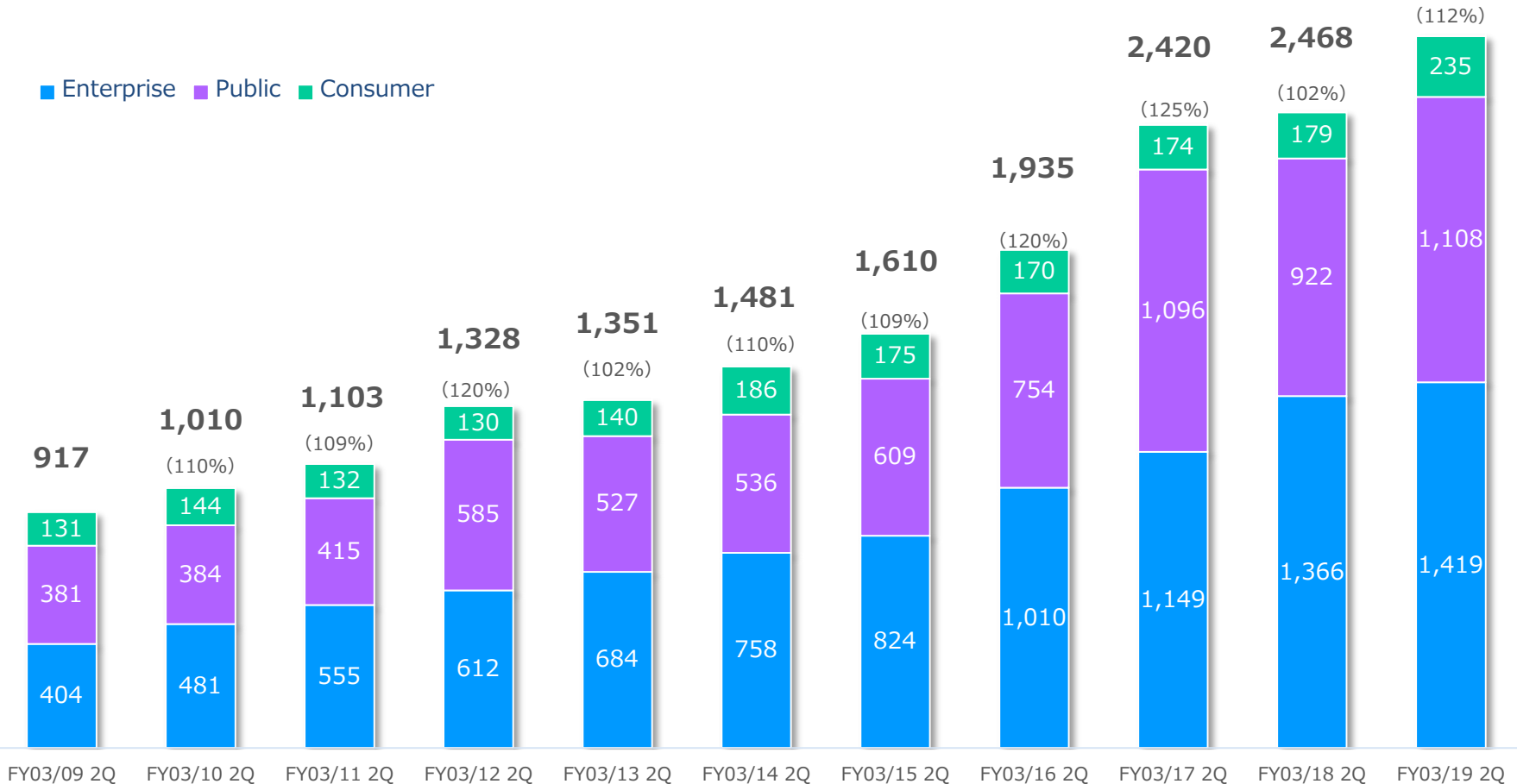
Consumer

Net Sales : JPY **235** million (JPY +56 million/ +31.7%YoY)

Increased acknowledgement as a total security solution provider in the public sector market, driving growth in overall sales

(million JPY)

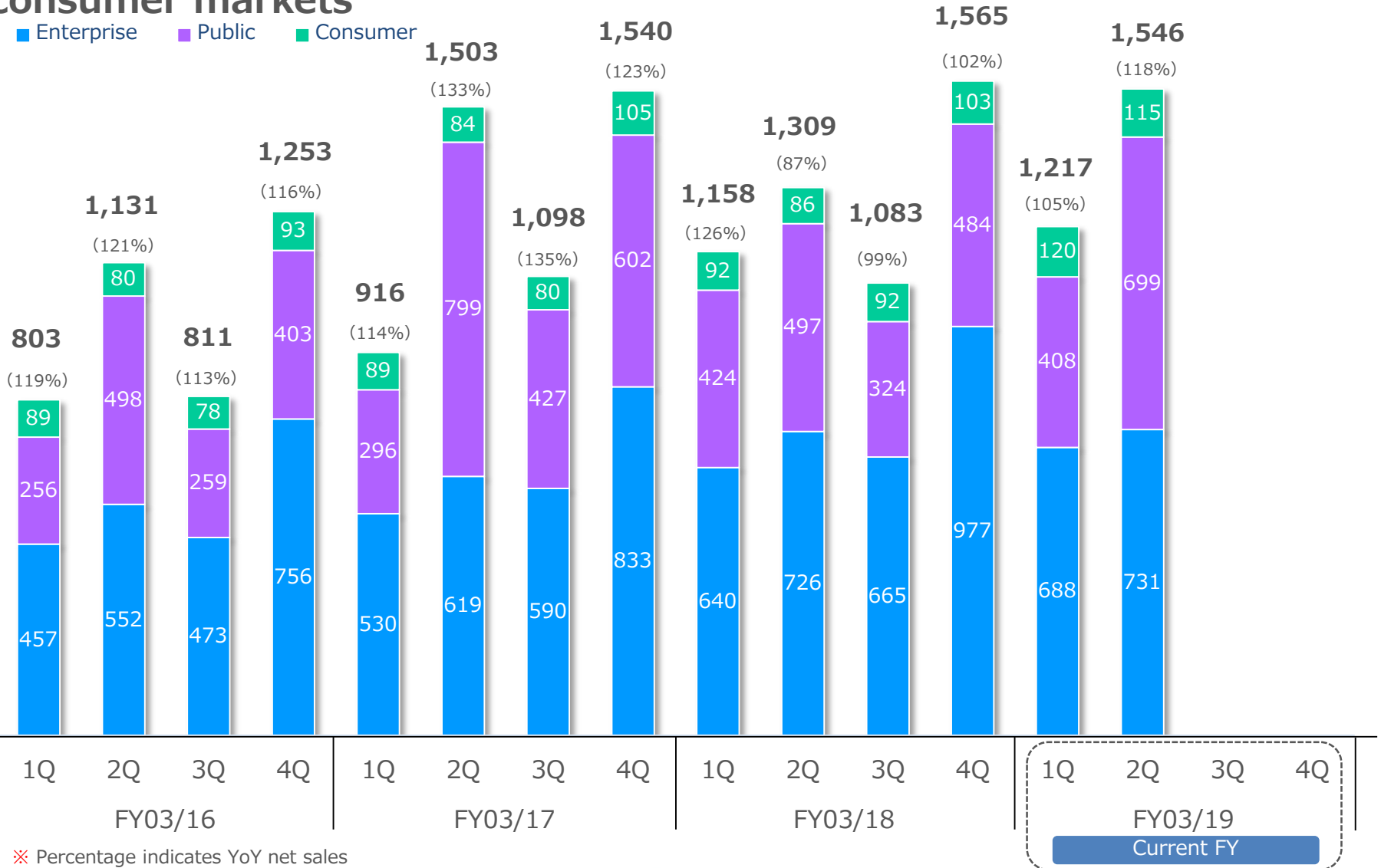
2,764



※ Percentage indicates YoY net sales

Record sales achieved due to the growth in sales in both public and consumer markets (million JPY)

■ Enterprise ■ Public ■ Consumer



※ Percentage indicates YoY net sales

FY03/19 Second Quarter Financial Results

ENTERPRISE SECTOR

- Due to the abundance of large projects, much of the sales have been deferred to the second half of the FY, however centered on ongoing projects from the previous FY, sales for popular products i-FILTER and m-FILTER were solid
- For FinalCode, the large project gained in the previous FY contributed to a growth in sales

i-FILTER
Series YoY **97.9 %**



m-FILTER
Series YoY **104.3 %**



FINALCODE YoY **134.2 %**



FY03/17 Second Quarter Financial Results

PUBLIC SECTOR

- When developing municipal information security measures led by the Ministry of Internal Affairs and Communications two years ago, development of sales channels that can make more advanced and comprehensive security proposals progressed
- As a result of promoting the sales of i-FILTER Ver. 10 and m-FILTER Ver. 5 under the leadership of the powerful dealership, recognition of both products' capabilities has increased and the acquisition of projects is progressing
- Due to large FinalCode projects in the previous fiscal year, FinalCode was negative YoY, but demand continues to be strong

i-FILTER
Series

YoY **109.4 %**



m-FILTER
Series

YoY **195.2 %**



FINALCODE

YoY **61.5 %**



FY03/19 Second Quarter Financial Results

CONSUMER SECTOR

- Promoted partnerships with mobile phone companies and MNVOs, as well as sales of i-FILTER for Multi Device, which allows the usage on multiple devices with one serial number
- Despite the decrease in personal computer shipments, steady growth in multiple-year packages as well as i-FILTER for Multi Device contributed to net sales

PC

YoY **117.9** %

Game Console/TV

YoY **104.1** %

Mobile Device

YoY **161.8** %

FY03/19 Second Quarter Financial Results

FY 03/19 FORECAST

On the revision of the FY03/19 Forecast

- Revision of the mid-to long-term product and sales strategies, group restructuring were carried out
- Highly-likely cost-curbing effect of group restructuring factored into forecast
- Despite the turn to favorable market conditions, the sales and dividend amounts have been conservatively left unchanged

(million JPY, except Dividend per share)

	FY03/19 Original Forecast	FY03/19 Revised Forecast	Difference
Net Sales	5,800	5,800	—
Gross Profit	4,700	4,700	—
Selling, General and Administration Expense	2,200	2,100	- 100
Operating Income	2,500	2,600	+100
Ordinary Income	2,500	2,600	+100
Net Income Attributable to Owners of Parent	1,619	2,000	+381
Dividend per Share	JPY 36	JPY 36	—

Reasons for the revision of the forecast

The Group aims to become a comprehensive security countermeasure manufacturer, and has first been promoting higher-quality product development by integrating new functions and the existing product lineup in the domestic market.

We have acquired strong recognition and market share in the area of internal information leakage prevention measures, but as a result of sales promotion activities with which the Group and dealerships were united, the new global view and solutions provided by the Group have been increasingly appreciated by the market, leading to an acceleration of sales, and our presence as a comprehensive security countermeasure manufacturer in Japan has grown.

In the overseas market, we had only deployed FinalCode, but going forward we plan to roll out the "DigitalArts" brand worldwide as a comprehensive security countermeasure manufacturer, similar to our approach in the domestic market.

Accordingly, FinalCode, Inc., a North American subsidiary, will be liquidated and business in North America will continue as Digital Arts America, Inc. For the Asia-Pacific region, business will continue as Digital Arts Asia Pacific Pte. Ltd. (name change planned from FinalCode Asia Pacific Pte. Ltd.) and Digital Arts Europe Ltd. (name change planned from FinalCode Europe Limited).

In terms of consolidated earnings, selling, general and administrative expenses are expected to shrink due to the selection and concentration effect of management resources resulting from the group restructuring as described above, and the almost certain cost reduction effect accompanying the group restructuring has been accounted for in our budgets and included in our revised forecasts.

Although the market environment is improving, sales and dividend forecasts have been conservatively left unchanged.

FY03/19 Consolidated Earnings Forecast

- Due to the cost-curbing impact of the group restructuring, costs are forecast to remain at the same level as the previous FY

(million JPY, except Dividend per share)

	FY03/18 Actual	FY03/19 Revised Forecast	Growth Rate
Net Sales	5,116	5,800	13.3 %
Gross Profit	4,041	4,700	16.3 %
Selling, General and Administration Expense	2,138	2,100	-1.8 %
Operating Income	1,902	2,600	36.6 %
Ordinary Income	1,909	2,600	36.2 %
Net Income Attributable to Owners of Parent	1,281	2,000	56.0 %
Dividends per Share	JPY 28	JPY 36	—

FY03/19 Non-Consolidated Earnings Forecast

- In the domestic market, bolster sales of new products released in September 2017
- In addition, we released a cloud-based service in May, which is accelerating growth in this area

(million JPY)

	FY03/18 Actual	FY03/19 Forecast	Growth Rate
Net Sales	5,046	5,600	11.0 %
Gross Profit	3,986	4,250	6.6 %
Selling, General and Administration Expense	1,898	1,900	0.1 %
Operating Income	2,087	2,350	12.6 %
Ordinary Income	2,097	2,350	12.0 %
Net Income	860	1,598	85.7 %

■ Dividend Distribution

Digital Arts plans to return profit to its shareholders as follows:

Projected dividend payout ratio for FY03/19:
25.0% of consolidated net income for current period

The annual dividend amount for the period ending March 2019:
Estimated at JPY 36.00 per share

	Dividend per share (JPY)			Consolidated Payout Ratio
	Interim	Fiscal year end	Annual	
FY03/18	14.00	14.00	28.00	30.3%
FY03/19	18.00			
FY03/19 (Forecast)		18.00	36.00	25.0%

※ As stated in the “Notice on the Revision of the FY03/19 Forecast” released today, although the (consolidated) earnings forecast has been revised, the dividend payment forecast has been conservatively left unchanged

All statements herein, other than historical facts, contain forward-looking statements and are based on DA's current plans, strategies and financial forecasts. These forward-looking statements are based upon the management's current assumptions and beliefs in light of the information currently available to it. However, environmental changes and other important factors may cause actual results to differ materially from those expressed herein. All statements herein are not intended to express DA's commitment to fulfil any forward-looking statements. Updated information, if applicable, will be disclosed in a timely manner.

All numerical indications in this statement, unless stated otherwise, are rounded to the nearest million JPY.

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