

Digital Arts Inc. (2326)



**FY03/17 Consolidated Financial Results
for Second Quarter Ended September 30, 2016**
(April 1, 2016 through September 30, 2016)

Supplemental Material
October 27, 2016

FY03/17 Second Quarter Financial Results

KEY FINANCIAL POINTS

- ① **Increase in acquisition of contracts due to dramatic increase in demands related to “cloud solutions for local government data security” and “local government data security enhancement measures”**
 - Mainstay i-FILTER (or D-SPA) and m-FILTER sales soared in the public sector: Government agencies at the prefectural and local levels performed measures to enhance cyber security in accordance to a guideline issued by the Ministry of Internal Affairs and Communications to fundamentally enhance information security in local municipalities.
- ② **FinalCode continues rapid growth**
 - Increase in sales of FinalCode Ver. 5, providing advanced files security for companies and organizations that handle large volumes of customer data.
 - Steady increase in deployment of FinalCode Limited Edition for Local Government, an edition that responds to needs specific to prefectural, city and local municipality governments.
- ③ **Sales results in the US and Asia Pacific**
 - US subsidiary FinalCode, Inc. and Asia-Pacific subsidiary FinalCode Asia Pacific Pte. Ltd. began to produce concrete sales results thanks to progress in partnerships with local sales partners.

FY03/17 Second Quarter Financial Results

CONSOLIDATED RESULTS HIGHLIGHTS

Consolidated Net Sales

¥ 2,420 million (YoY +¥484 million / +25.0%)

Significant growth in mainstay i-FILTER and m-FILTER by capturing the needs of clients adhering to guidelines issued by Ministry of Internal Affairs and Communications

Operating Income

¥ 789 million (YoY +¥292 million / +58.9%)

Surge in sales absorbed costs, such as increase in domestic personnel expenses, for a considerable increase in operating income

Ordinary Income

¥ 767 million (YoY +¥267 million / +53.6%)

Secured substantial earnings growth despite forex fluctuation with the rapid appreciation of the yen, while loss remained at the same level as Q1

Net Income Attributable to Owners of Parent

¥ 454 million (YoY +¥139 million / +44.5%)

Achieved extensive increase in revenue with domestic sales absorbing increase in tax expenses as a result of advance investment to overseas subsidiaries

Consolidated Results

(million yen)

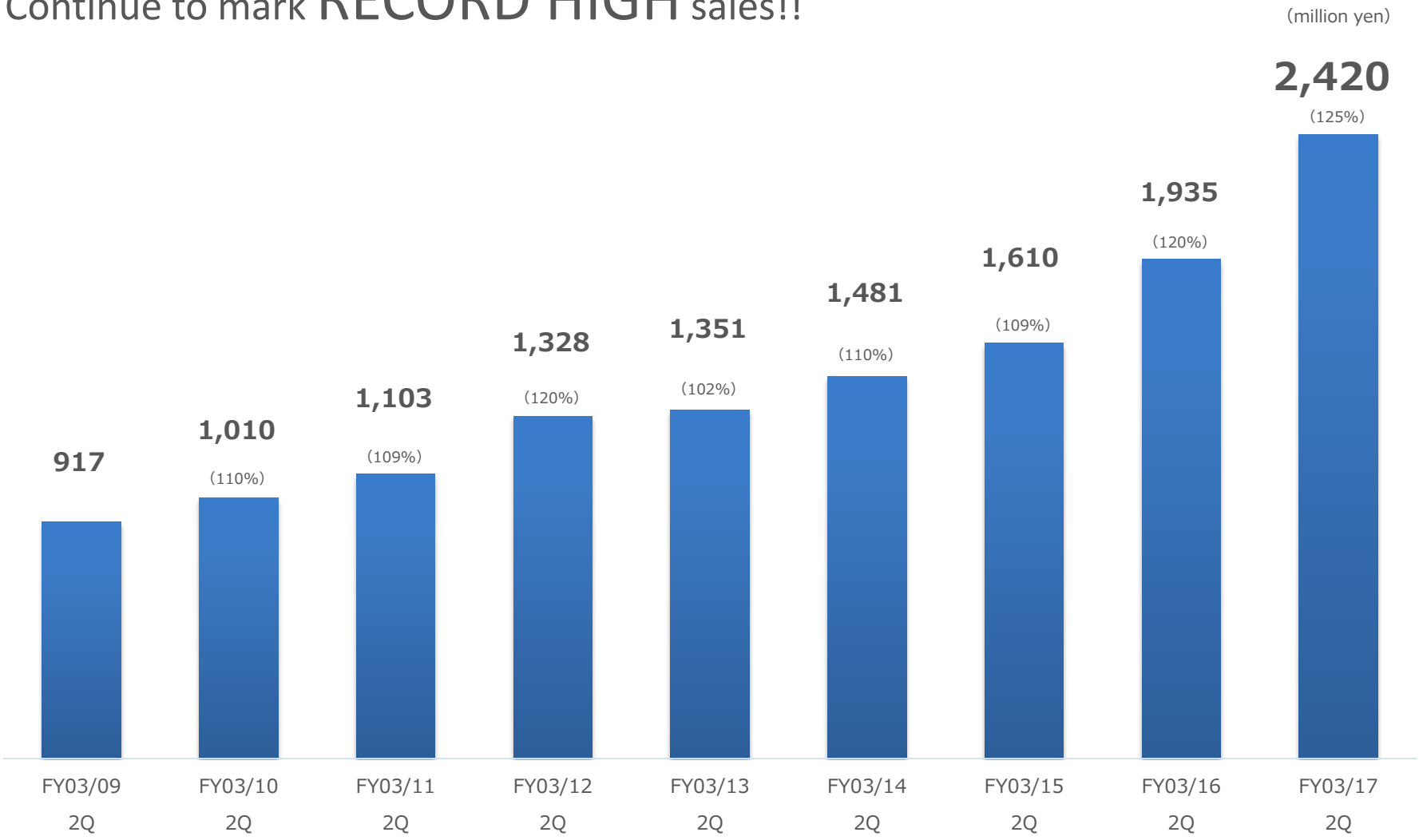
	FY03/16 Second Quarter	FY03/17 Second Quarter	YoY Growth	FY03/17 Forecast
Net Sales	1,935	2,420	+25.0%	4,600
Gross Profit	1,496	1,922	+28.5%	3,652
Selling, General and Administration Expense	999	1,132	+13.4%	2,252
Operating Income	497	789	+58.9%	1,400
Ordinary Income	499	767	+53.6%	1,400
Net Income Attributable to Owners of Parent	314	454	+44.5%	870
ROE	7.3%	9.6%	—	—

Non-Consolidated Results

(million yen)

	FY03/16 Second Quarter	FY03/17 Second Quarter	YoY Growth	FY03/17 Forecast
Net Sales	1,933	2,465	+27.5%	4,598
Gross Profit	1,532	1,938	+26.5%	3,555
Selling, General and Administration Expense	875	1,001	+14.4%	1,843
Operating Income	656	936	+42.7%	1,712
Ordinary Income	659	918	+39.4%	1,712
Net Income	437	619	+41.5%	1,182
ROE	9.7%	11.8%	—	—

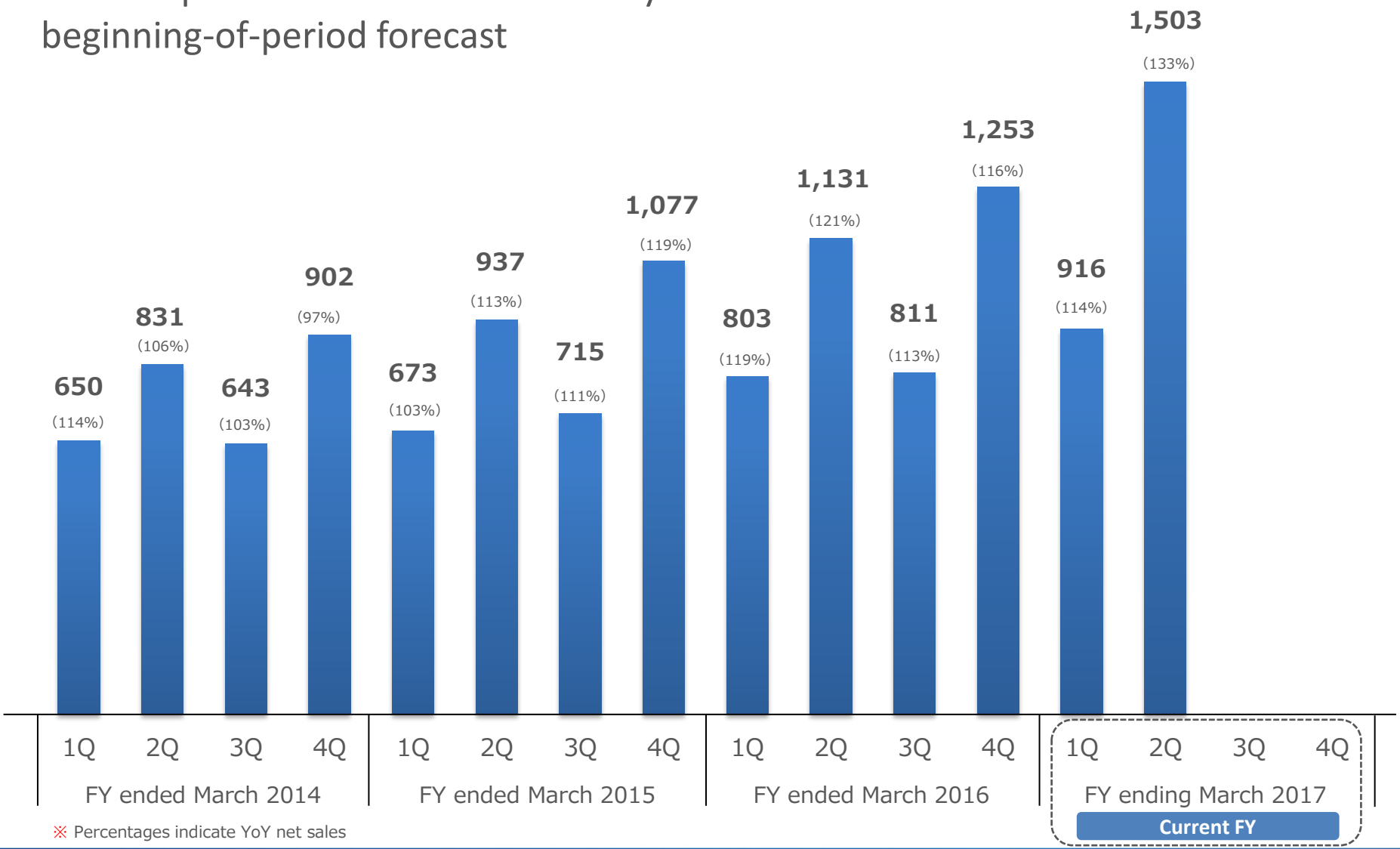
Continue to mark **RECORD HIGH** sales!!



※ Percentages indicate YoY net sales

(million yen)

Second quarter net sales substantially exceeded beginning-of-period forecast



※ Percentages indicate YoY net sales

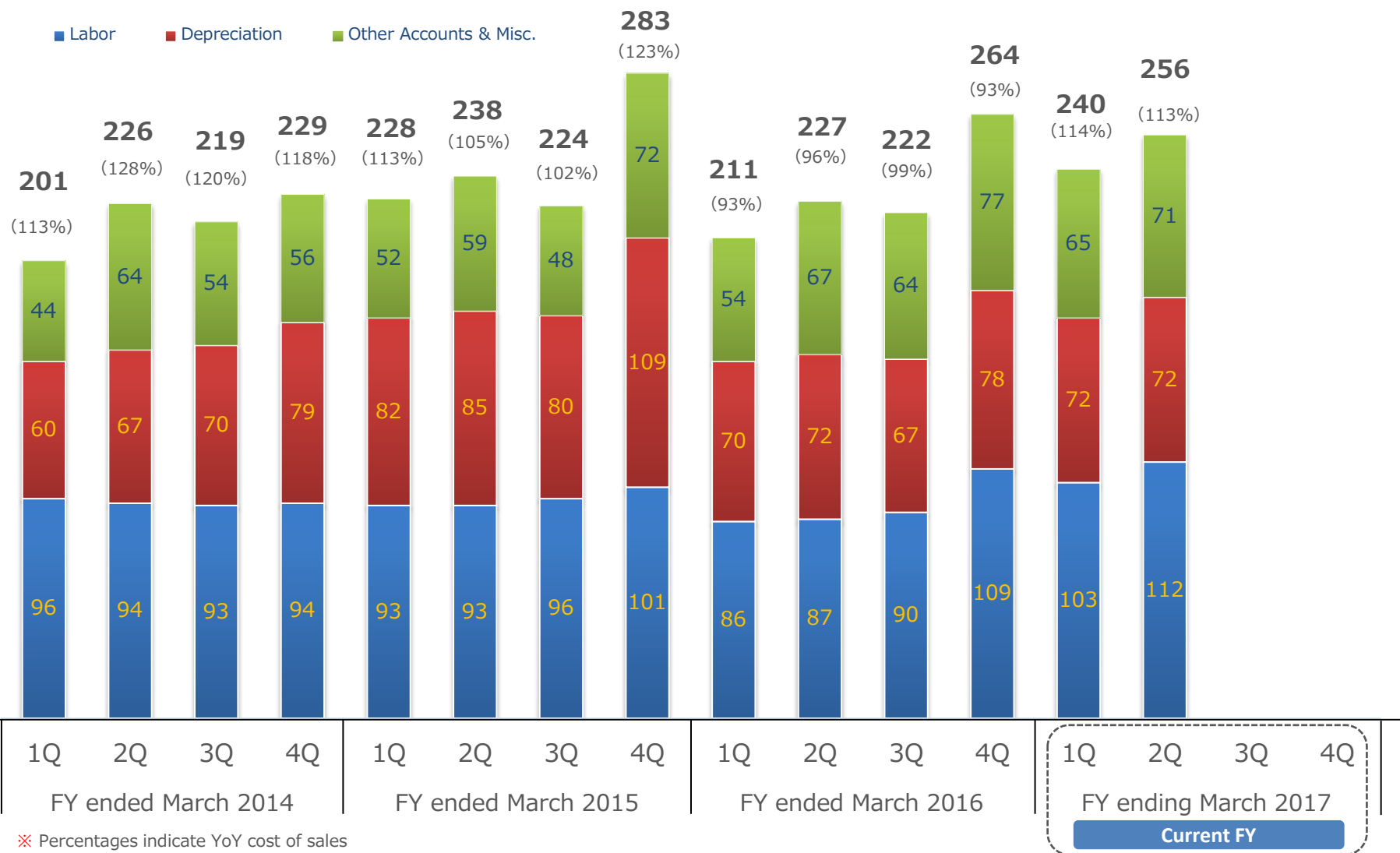
- COS and SG&A increased slightly due to increased personnel expenses in Japan
However, COS and SG&A trends remain largely according to period start forecast

(million yen)

	FY03/16 Second Quarter	FY03/17 Second Quarter	YoY Growth	Key Factors
Cost of Sales	439	497	+58	
Labor	174	215	+41	
Depreciation	142	144	+2	
Transfer to other accounts Misc production cost	122	137	+14	
Selling, General and Administrative Expenses	999	1,132	+133	
Labor	517	585	+68	Incl. domestic personnel expenses (+70 M)
Publicity	139	174	+35	
Others	342	372	+29	Server replacement, hiring employees in Japan, etc.

(million yen)

No significant changes in the breakdown of cost of sales



※ Percentages indicate YoY cost of sales

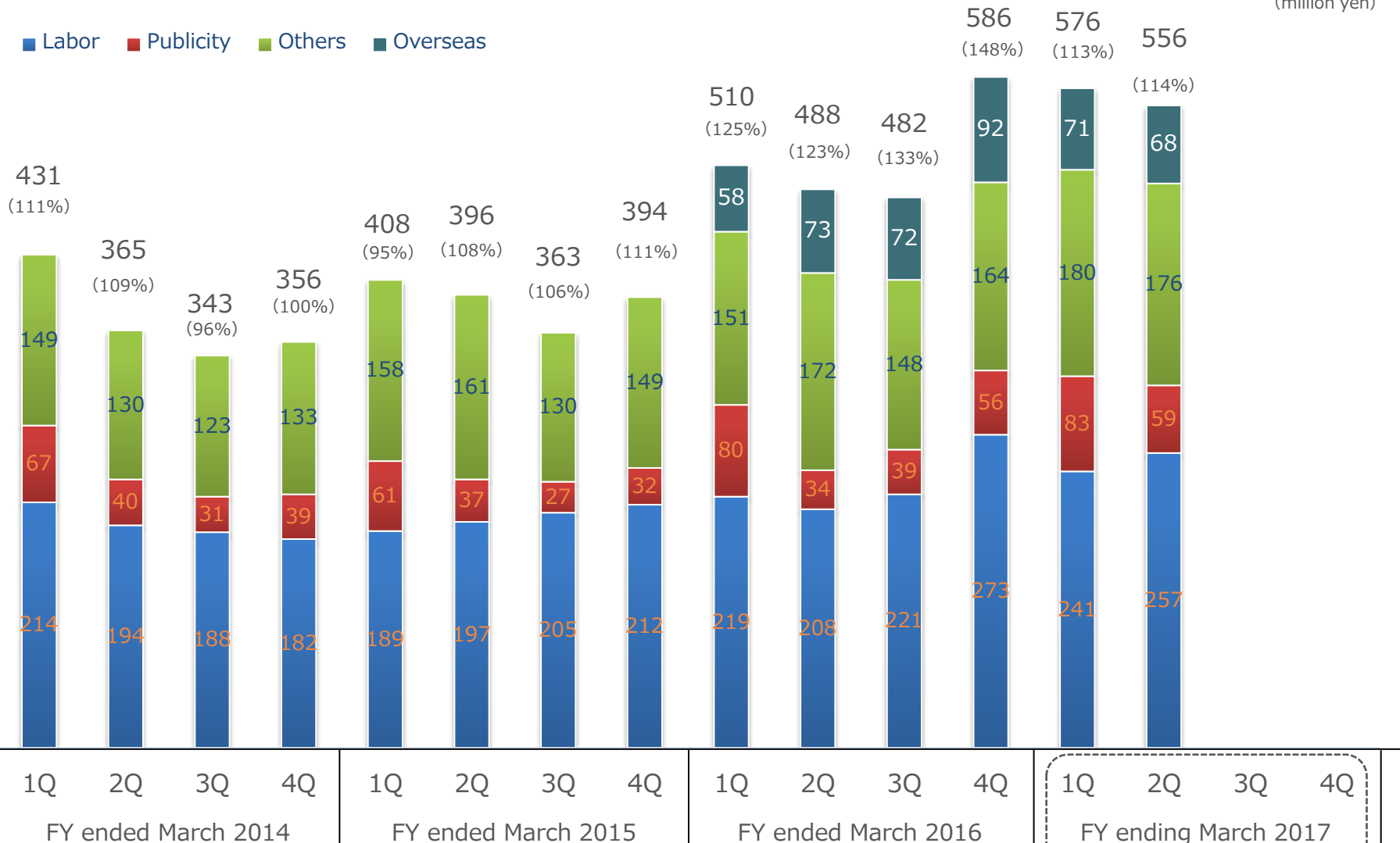
Selling, General and Administrative Expenses (by Quarter)



SG&A increased due to increase in domestic personnel

(million yen)

■ Labor ■ Publicity ■ Others ■ Overseas



※ Percentages indicate YoY cost of sales

FY ending March 2017
Current FY

FY03/17 Second Quarter Financial Results

BY MARKET

- +25.0% growth in consolidated sales
- Enterprise: continue steady sales trends at +13.8%
- Public: dramatic increase of +45.2% in providing cloud solutions for data security in local municipalities
- Consumer: held firm despite steep decline in domestic consumer PC shipments

Consolidated Net Sales

Net sales: ¥ 2,420 million (+484 million / +25.0% YoY)

Enterprise

Net sales: ¥ 1,149 million (+139 million / +13.8% YoY)

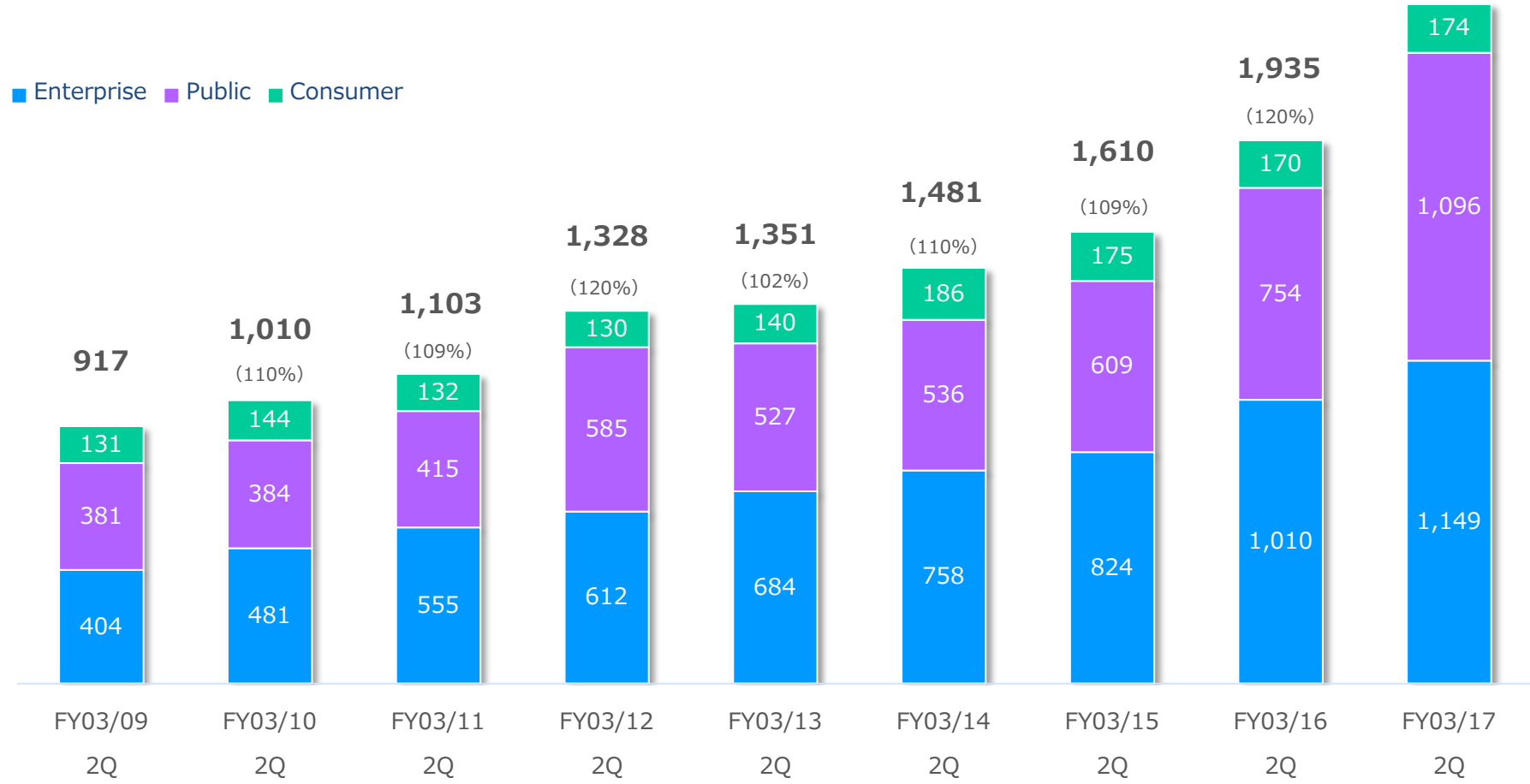
Public

Net sales: ¥ 1,096 million (+341 million / +45.2% YoY)

Consumer

Net sales: ¥ 174 million (+4 million / +2.4% YoY)

Public sector dramatically grew with solutions that satisfy the level of security demanded in the Ministry of internal Affairs and Communications' guidelines on strengthening local government security

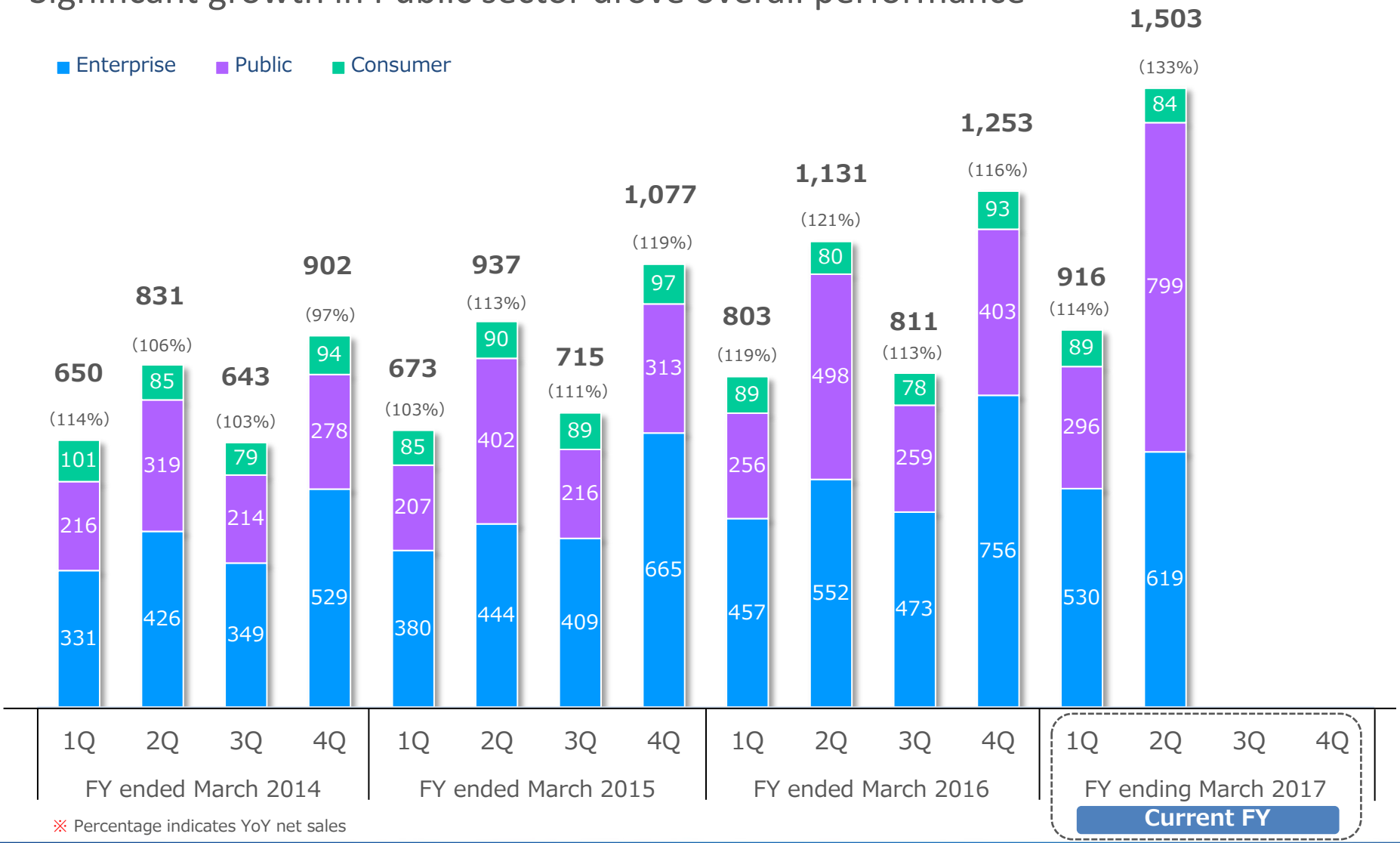


※ Percentage indicates YoY net sales

Significant growth in Public sector drove overall performance

(million yen)

■ Enterprise ■ Public ■ Consumer



※ Percentage indicates YoY net sales

FY03/17 Second Quarter Financial Results

ENTERPRISE SECTOR

- Robust sales in mainstay i-FILTER and FinalCode.
- m-FILTER sales fell YoY due to a special procurement demand in the previous Q2, however with steady accumulation of orders, secured a foundation of growth for Q3 and on.
- Amid a series of incidents with leaks of important information, FinalCode Ver. 5 sales firmly increased by providing company-wide advanced file security, meeting the needs of corporations that handle large volume of customer data.

i-FILTER + 12.6 %

m-FILTER - 5.6 %

ID-SPA + 34.2 %

FINALCODE + 151.9 %



FY03/17 Second Quarter Financial Results

PUBLIC SECTOR

- i-FILTER (or D-SPA) and m-FILTER, main offerings for the public sector, soared as government in prefectural and local levels improving cyber security under the Ministry of Internal Affairs and Communications' guidelines on fundamental strengthening of local government security.
- Robust implementation of FinalCode's limited edition for local government, providing simple functions that public organizations want.

i-FILTER + 36.0 %

m-FILTER + 111.7 %

ID-SPA + 79.6 %

FINALCODE + 609.3 %



FY03/17 Second Quarter Financial Results

CONSUMER SECTOR

- Continued to enter tie-ups with mobile operators and MVNO operators to expand sales and increase collaboration for the mobile device version of i-FILTER (Consumer) for Smartphones.
- Firm sales for the PC version of i-FILTER (Consumer) due to OEM-driven sales and robust shipments of multi-year packaged products, despite a decline in the number of domestic consumer PC shipments.
- Sales expanded for i-FILTER (Consumer) for Multi-Device, which can be used on multiple OS with a single serial ID.

PC

-0.8 %

Game Console/TV

-0.6 %

Mobile Device

+11.8 %

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FY03/17 Second Quarter Financial Results

FY03/17 FORECAST

FY03/17 Consolidated Forecast

During the cumulative second quarter ended September 30, 2016 (consolidated and non-consolidated), demand for the Company's main offerings in the public-sector market, i-FILTER (and/or D-SPA) and m-FILTER, increased dramatically as a result of government agencies in the prefectural and local levels performing measures to enhance cyber security in accordance to a guideline issued by the Ministry of Internal Affairs and Communications to fundamentally enhance information security in local municipalities. Therefore, net sales and incomes have exceeded beginning-of-the-year forecasts.

Favorable environment is anticipated to continue mainly in the public-sector market. Consolidated forecast for FY03/17 (April 1, 2016 through March 31, 2017) is currently under review and will be released and announced accordingly.

FY03/17 Consolidated Forecast

- FY03/16 favorable domestic market conditions are expected to continue
- Conservative guidance for overseas operations although has started to produce concrete sales results
- Expects increase in margins as overseas investment will be limited to a slight increase

(million yen)

	FY03/16 Actual	FY03/17 Forecast	Growth Rate
Net sales	4,000	4,600	15.0 %
Gross Profit	3,074	3,652	18.8 %
Selling, General and Administration Expense	2,067	2,252	9.0 %
Operating Income	1,006	1,400	39.1 %
Ordinary Income	994	1,400	40.8 %
Net Income Attributable to Owners of Parent	545	870	59.5 %
Dividends per Share	15 yen	20 yen	—

FY03/17 Non-Consolidated Earnings Forecast

- Favorable domestic market environment in FY03/16 is expected to continue

(million yen)

	FY03/16 Actual	FY03/17 Forecast	Growth Rate
Net Sales	4,018	4,598	14.4 %
Gross Profit	3,123	3,555	13.8 %
Selling, General and Administration Expense	1,788	1,843	3.0 %
Operating Income	1,335	1,712	28.3 %
Ordinary Income	1,328	1,712	28.9 %
Net Income	840	1,182	40.7 %

■ Dividend Distribution

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

Projected dividend payout ratio for FY03/17:

32.0% of consolidated net income of the current period

The amount of annual dividends for the period ending March 2017:

Estimated at 20.00 yen per share.

	Dividends per share (in yen)			Consolidated Payout Ratio
	Interim	Fiscal year-end	Annual	
FY03/16	7.00	8.00	15.00	38.2%
FY03/17	10.00			
FY03/17 (forecast)		10.00	20.00	32.0%

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 management's current assumptions and beliefs in light of the information currently available to it, however environmental changes and other important factors could cause actual results to differ materially from those expressed in our forward-looking statements. All statements herein are not intended to express DA's commitment to fulfill any forward-looking statements. Updated information, if applicable, will be disclosed in a timely manner.

All numerical indications in this statement, unless noted, are rounded to the nearest million yen.

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