

SIR CORPORATE REPORT

August 4th, 2014

Enish, Inc. (TSE 1st section : 3667)



Business profile

- Designs, develops and operates social apps games.
- Has an edge in management simulation games, such as “My Restaurant (*Bokuno resutoran*)” series, which has a long life time value. These games also attract female users, which is also a strength of the company. Through platforms such as GREE and DeNA, the company has been able to sustain a high “continuance rate”.
- Moving towards making a smooth transition into the native apps game titles, the main challenge for this fiscal year is to establish a unique revenue generating model.
- Expanding its business in the high growth markets of Asia ; particularly in China and South Korea.



Keep a close eye on Q3

(Q2 review for FYE December 2014)

Summary

The company has revised downward its Q2 and year-end figures on July 18th. For Q2, sales was 3,254 million yen (12.0% lower than the previously announced forecast), and operating profit was 230 million yen (50.9% lower than the previously announced forecast) . In particular, the performance for Q2 (April to June) deteriorated as sales declined by 272 million yen to 1,491 million yen (which

was a 15.4% revenue decrease qoq) and operating profit declined by 210 million yen (qoq) to 10 million yen.

The main reasons for this performance were as follows: for the major current game titles, ① Sales for card battle games (targeting “mid-core users”) declined 28.9% qoq ②Sales for simulation games (targeting “light users”), which the company has an advantage, declined 8.1% qoq.

While sales declined, costs and SGA expenses remained broadly at the same level as Q1 (although there was a slight decrease in commission expenses); therefore, the decline in sales directly hit profit levels.

Also, delays in releasing the new game title “My Restaurant 3 (*Boku no resutoran 3*)” (targeting light users, native apps) was another reason why sales did not meet the initial target. The release was delayed until the end of Q2, but as there were issues on tuning, its full-fledged release had to be pushed back until the second half of the fiscal year.

For costs and SGA expenses, the actual figure for Q2 was 3,024 million yen (206 million yen lower than the company forecast of 3,230 million yen). The main reason was because the company did not make promotional expenses for the new title games.

PL for Q2

(Units: million yen)

	1Q (Jan.-Mar.) 2014 (actual)	2Q (Apr.-Jun.) 2014 (actual)	2Q(Jan.-Jun.) 2014 (accumulated)	2Q(Jan.-Jun.) 2014 (previous forecast)	% difference
Sales	1,763	1,491	3,254	3,700	(12.0%)
Cost of Sales	1,250	1,182	2,433	-	
Gross Margin	512	308	821	-	
SGA	292	298	590	-	
Operating Profit	220	10	230	470	(50.9%)
Operating Margin	12.5%	0.7%	7.1%	12.7%	
Ordinary Profit	219	3	223	470	(52.5%)
Pretax Profit	219	1	221	-	
Net Profit	131	(2)	129	290	(55.3%)

Revised forecast for FY 2014

The revised forecast for the full FY 2014 announced by the company is as follows: Sales:6,500 million yen (previous forecast : 8,700million yen, a 25.3% decrease) , Operating profit: 0 yen (previous forecast : 1,350million yen) . The assumptions

behind this are ①Sales for current titles will continue to gradually decline at the present pace ②Will concentrate on releasing 3 game titles for this fiscal year (instead of the initial 5 game titles; ie. 1 new game title for the second half of the year), ③Will continue to strengthen domestic development capacity and expansion to overseas markets as originally scheduled, in order to secure growth in the future.

Actual·Forecast·Previous forecast

(Units : million yen)

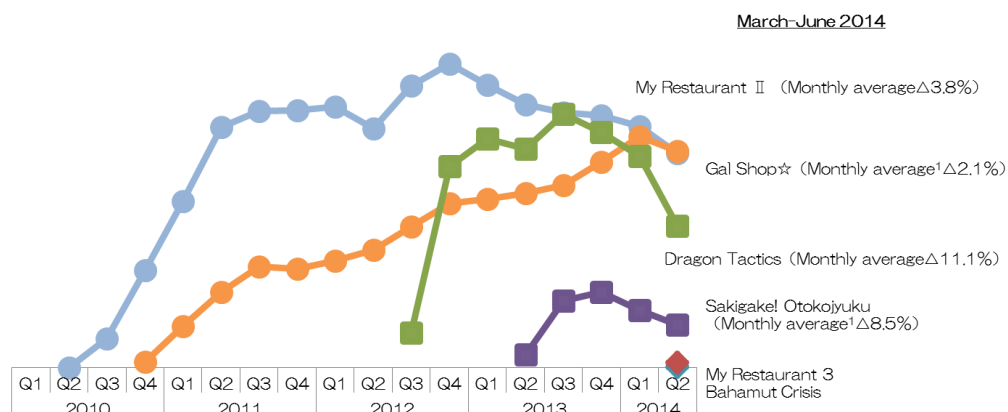
	2Q(Jan.-Jun.) 2014 (accumulated)	FY2014 (earning forecast)	FY2014 (previous forecast)	% difference
Sales	3,254	6,500	8,700	(25.3%)
Operating Profit	230	0	1,350	-
Operating Margin	7.1%	0.0%	15.5%	-
Ordinary Profit	223	0	1,350	-
Net Profit	129	0	830	-

Verification of the validity of the company's forecast

1. On current game titles

The feature of the company has been in its high life-time-value (low turnover of current users) , with sizable revenue flowing from browser games distributed through platforms such as GREE and DeNA. From Q2 however, sales (revenue) for the company as a whole have been declining (See diagram below).

Sales per different game titles



This stark decline in sales can be broken down into two factors:

- ① Sales decline for current game titles targeting light users (“My Restaurant II (*Boku no resutoran II*)” “Gal Shop☆ (*Garu sho*☆) ”

This has occurred as operation staff for the current game titles have been transferred to work on the development of “My Restaurant 3 (*Boku no resutoran 3*)”. The game itself has a relatively low turnover (users usually do not leave easily), so the major reason for the decline in revenue is most probably because of temporary drop in PAY RATIO from lower operational proficiency.

- ② Sales decline in current game titles targeting mid-core users (“Dragon Tactics” “*Sakigake! Otoko-juku*”)

As competition is fierce with numerous choices for mid-core users, there is a possibility that users may have chosen other game titles over the company’s games. Therefore the company needs to reconstitute its operating system and endeavor to accumulate know-how within the company. In this area, the potential for a rapid recovery is unclear.

Considering the above, for ①, by reorganizing the system and conducting proper operations, it should be relatively easy to improve the revenue structure. On the other hand, ② is a fundamental structural issue; since July, the company has been taking measures such as making changes to the system (upgrading the battle system) for “Dragon Tactics” and distributing to COLOPL. It seems that the company has been endeavoring to put a halt to the decline in revenue by implementing various measures through trial and error.

Therefore, SIR sees that the company’s forecast that the rate of decline in sales will continue into the second half, is a conservative estimate.

2. New game titles

“My Restaurant 3 (*Boku no resutoran 3*)” (Released : Native application for light users)

For this new game title, the company had a certain track record (know-how) on the game’s operation as this new title was a continuation of a previously released game.

However, since it was the first full-fledged/ major native application game, technical issues arose. As such, it is currently being tuned-up, and its full-fledged release will be made in the second half of this fiscal year. For the iOS version that has already been released, the KPI is following that of the previous game. Therefore, through enhanced promotional efforts after its major release, it can be expected that the game will contribute to revenue in a relatively short period of time.

「Bahamut Crisis」 (Released : Browser application for mid-core users)

Targeting mid-core users, this game is provided through a browser application. The company can therefore launch this game in collaboration with the distributor, thus limiting promotional expenses. Also, as the distributors have been major social network companies such as dgame and GREE, it is expected that revenue from this game title could fill in for the weaker performances of the current mid-core games (“Dragon Tactics” “Sakigake! Otoko-juku”).

「Grand Gods of the Millennium (Sennen no Kyoshin)」 (To be released: Native application for light users)

This is a game for light users, an area in which the company has an advantage. While its contribution to revenue is still unknown, this new game title should become the core in realizing the company’s smooth transition into native apps.

The company has, in effect, decided to defer the costly (development and promotional expense-wise) native apps for the mid-core game title (where the company still lacks operational know-how) until the next fiscal year and concentrate on game titles for light users (where the company’s strengths lie); such strategy of aiming for success by focusing on a single title can be commended as most reasonable. Also, this does not mean that the company has given up on mid-core users, but rather, sequencing the release of new game titles by starting out with “Bahamut Crisis” on a browser base, waiting until it matures before moving on to the native apps version, and then introducing the mid-core native apps new game title at that same timing, shows that the company still has growth potential.

3. The validity of the company’s full year forecast

Taking into consideration the above, the company’s forecast of 6,500 million yen for sales is under the assumption that sales for the latter half of the year will be the

same as the first half (cumulative Q2). However,

- ① The declining trend for current game titles should not continue at the same pace, because revenue for games such as “My Restaurant II” and “Gal Shop☆” should be able to recover relatively quickly;
- ② Revenue contribution of the two new game titles released in the first half of the year should more than make up for the drop in revenue from current game titles;
- ③ On top of the revenue for①,② above, which should be at least as much as what it was in the first half, revenue for “Grand Gods of the Millennium (*Sennen no Kyoshin*)” would be added;

Therefore, the company’s forecast could be regarded as quite conservative.

Regarding performance for future quarters

The company sees the latest downward revision as “a plateau, to be followed by the next growth phase”. While both sales and profits may have declined temporarily, the company claims that it will continue to make investments consistent with its growth strategy.



SIR regards the temporary stagnation in sales and profit has proven to be a blessing for the company to re-think its growth strategy. SIR intends to continue to keep a close eye on the company’s actions to induce growth and

the results of those actions in Q3.

Strategic IR Insight Inc. CEO Yuichi Sekiguchi

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