

## Digital Arts (2326)

Consolidated FY (Million Yen)		Sales	Operating Profit	Recurring Profit	Profit Attributable to Owners of Parent	EPS (Yen)	DPS (Yen)	BPS (Yen)
FY03/2018		5,116	1,902	1,909	1,281	92.5	28.0	446.4
FY03/2019		5,841	2,629	2,630	1,961	141.1	48.0	558.3
FY03/2020CoE		6,800	3,300	3,300	2,277	163.8	50.0	-
FY03/2019	YoY	14.2%	38.2%	37.8%	53.0%	-	-	-
FY03/2020CoE	YoY	16.4%	25.5%	25.4%	16.1%	-	-	-

Consolidated Quarter (Million Yen)		Sales	Operating Profit	Recurring Profit	Profit Attributable to Owners of Parent	EPS (Yen)	DPS (Yen)	BPS (Yen)
Q1 FY03/2019		1,217	295	294	175	-	-	-
Q2 FY03/2019		1,546	740	745	816	-	-	-
Q3 FY03/2019		1,402	638	634	426	-	-	-
Q4 FY03/2019		1,674	954	956	542	-	-	-
Q1 FY03/2020		1,249	413	411	280	-	-	-
Q1 FY03/2020	YoY	2.6%	40.0%	39.8%	60.2%	-	-	-

Source: Company Data, WRJ Calculation

### 1.0 Results Update (7 August 2019)


#### White List Management

On 31 July 2019, Digital Arts to plan, develop and sell proprietary software as Internet security maker released its Q1 FY03/2020 results. It has been revealed that recent trading is rather adjusting. Sales increased by no more than 2.6% over the same period in the previous year. In the first place, sales in Q1 are smaller than other quarters every year as it is a slack period, but the Company saw sales associated with a few large-scale projects on the Public Sector Market side during the same period in the previous year, having resulted in a negative repercussion. Together with some other short-term factors, sales as a whole for the Company have suffered from decelerated growth rate. Meanwhile, more importantly, the Company has already launched software to provide advanced security measures against Targeted Attacks for specific organizations on top of existing capability of filtering to block access to harmful sites, which is expected to consistently drive sales with the Company as a whole going forward. The Company, accounting for more than half of the market for website filtering in Japan, has accumulated information on every URL of Japan and overseas to date, with which white list management of websites or “sterilization” of websites and e-mails is now available for users in Japan. As far as we could see, the Company has a good opportunity to gradually replace antivirus software in the future, where the market is far too larger than existing ones to which the Company is currently exposed.

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## 2.0 Company Profile

### Internet Security Maker

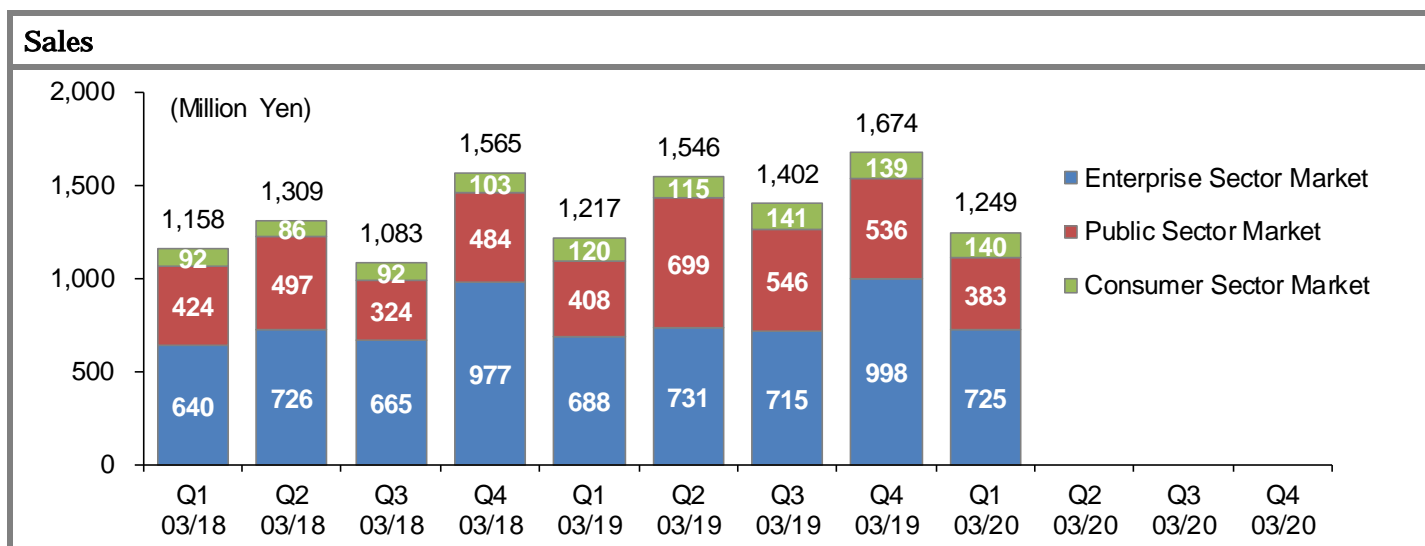
<b>Company Name</b>	Digital Arts Inc. <a href="#">Company Website</a> <a href="#">IR Information</a> <a href="#">Share Price (Japanese)</a> 
<b>Established</b>	21 June 1995
<b>Listing</b>	19 March 2013: Tokyo Stock Exchange 1st section (ticker: 2326) 28 February 2012: Tokyo Stock Exchange 2nd section 19 September 2002: Osaka Stock Exchange Nasdaq Japan (currently, JASDAQ)
<b>Capital</b>	¥713m (as of the end of June 2019)
<b>No. of Shares</b>	14,133,000 shares, including 224,220 treasury shares (as of the end of June 2019)
<b>Main Features</b>	<ul style="list-style-type: none"> <li>● Specializing in operations to plan, develop and sell proprietary software</li> <li>● “i-FILTER” and “m-FILTER” for filtering of websites and e-mails, respectively</li> <li>● Materializing “sterilization” with “i-FILTER” (Ver.10) and “m-FILTER” (Ver.5)</li> </ul>
<b>Business Segments</b>	. Security Business
<b>Top Management</b>	Representative Director, President and CEO: Toshio Dogu
<b>Shareholders</b>	Toshio Dogu 17.6%, Japan Trustee Services, T. 13.5%, DAM Co. 4.8% (as of the end of March 2019)
<b>Headquarters</b>	Chiyoda-ku, Tokyo, JAPAN
<b>No. of Employees</b>	Consolidated: 207, Parent: 201 (as of the end of March 2019)

Source: Company Data

## 3.0 Recent Trading and Prospects

### Q1 FY03/2020 Results

In Q1 FY03/2020, sales came in at ¥1,249m (up 2.6% YoY), operating profit ¥413m (up 40.0%), recurring profit ¥411m (up 39.8%) and profit attributable to owners of parent ¥280m (up 60.2%), while operating profit margin 33.1% (up 8.9% points).



Source: Company Data, WRJ Calculation

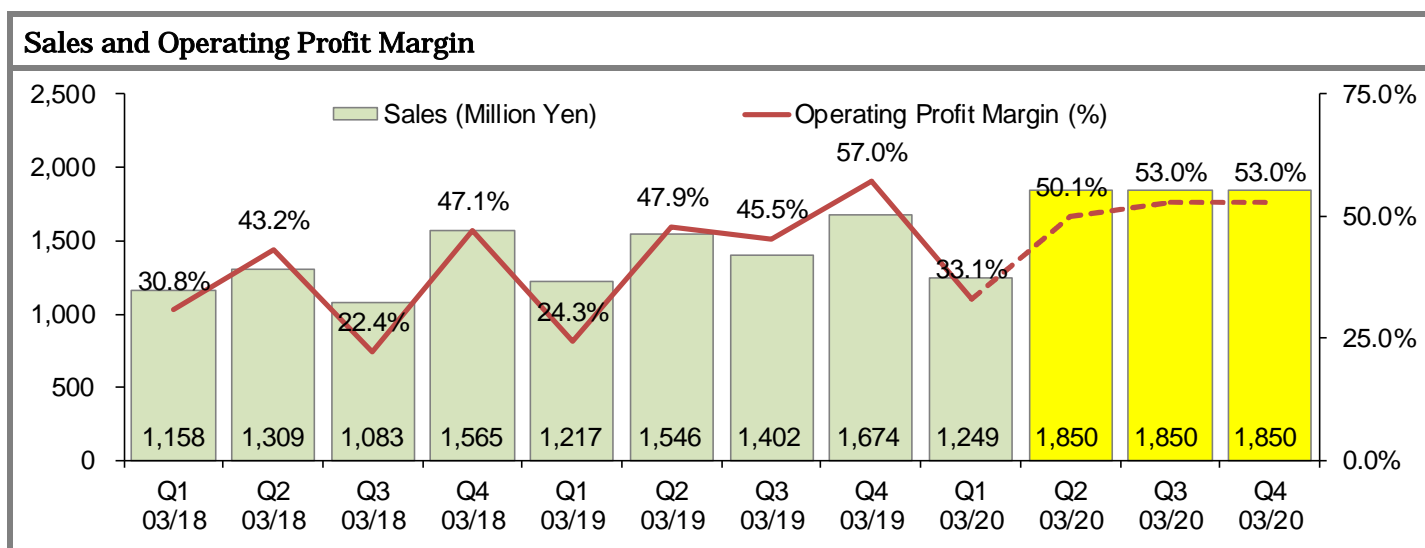
Gross profit came in at ¥962m (up 3.8%) and SG&A expenses ¥548m (down 13.2%), implying gross profit margin of 77.0% (up 0.9% points) and sales to SG&A expenses ratio of 43.9% (down 8.0% points). While gross profit margin is almost stable, SG&A expenses came down a lot over the same period in the previous year due to the Company's strategy to spend own resources on anything after selection and concentration. In FY03/2019, the Company took another look at measures to cultivate markets overseas, having decided to focus on the market of Japan for the time being. Then, from the beginning of FY03/2020, SG&A expenses have been on the decreases in line with this, according to the Company.

Sales on the Enterprise Sector Market side came in at ¥725m (up 5.4%), sales on the Public Sector Market side ¥383m (down 6.3%) and sales on the Consumer Sector Market ¥140m (up 16.4%). With respect to the mainstay Enterprise Sector Market and Public Sector Market, collectively accounting for 88.8% of sales as a whole for the Company, it appears that the Company suffers from negative impacts stemming from short-term measures with distributors in charge of selling the Company's software products. It could be the case that this situation may persist in Q2, but the Company is rather convinced that it will not be the case in H2.

Given that support services on Windows 7 are to be suspended on 14 January 2020, there is increased needs to make a shift to new hardware with the latest Windows 10 being installed amongst final users on the Enterprise Sector Market side and on the Public Sector Market side, i.e., companies, schools, municipalities, etc. Thus, distributors in charge of selling the Company's "i-FILTER", "m-FILTER" and other software products allocate the bulk of resources on selling hardware at the moment, as far as we could see. The Company directly sells own software products to a Softbank group company, Daiwabo Information System, Net One Systems etc., i.e., all those companies working as distributors for the Company and this is almost everything, according to the Company.

### FY03/2020 Company Forecasts

FY03/2020 initial Company forecasts have remained unchanged, going for prospective sales of ¥6,800m (up 16.4% YoY), operating profit of ¥3,300m (up 25.5%), recurring profit of ¥3,300m (up 25.4%) and profit attributable to owners of parent of ¥2,277m (up 16.1%), while operating profit margin of 48.5% (up 3.5% points). At the same time, Company forecasts have also remained unchanged for prospective annual dividend, going for ¥50.0 per share, implying payout ratio of 30.5%.



Source: Company Data, WRJ Calculation (Q3 and Q4 FY03/2020: H2 Company forecasts, pro rata)

With some variety, antivirus software products (with which the Company is not involved) are penetrated in Japan across the board, but eradication of viral infection has not materialized. One of the key factors is that new sources are always being created for the sake of bringing in viral infection. Meanwhile, adoption of aforementioned white list management makes it impossible to access URLs not listed here, which is expected to contribute a lot to eradication of viral infection. The Company is looking to improved recognition on this fact going forward and thus to consistently increased sales as a whole for the Company.

## 4.0 Financial Statements

### Income Statement (Cumulative, Quarterly)

Income Statement	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	YoY
(Million Yen)	Q1	Q1 to Q2	Q1 to Q3	Q1 to Q4	Q1	Q1 to Q2	Q1 to Q3	Q1 to Q4		Net Chg.
	03/2019	03/2019	03/2019	03/2019	03/2020	03/2020	03/2020	03/2020	03/2020	
<b>Sales</b>	<b>1,217</b>	<b>2,764</b>	<b>4,166</b>	<b>5,841</b>	<b>1,249</b>	-	-	-	-	<b>+31</b>
Cost of Sales	289	526	809	1,059	286	-	-	-	-	(3)
Gross Profit	927	2,237	3,357	4,781	962	-	-	-	-	+34
SG&A Expenses	632	1,201	1,683	2,152	548	-	-	-	-	(83)
<b>Operating Profit</b>	<b>295</b>	<b>1,036</b>	<b>1,674</b>	<b>2,629</b>	<b>413</b>	-	-	-	-	<b>+118</b>
Non Operating Balance	0	3	0	1	(1)	-	-	-	-	(1)
<b>Recurring Profit</b>	<b>294</b>	<b>1,040</b>	<b>1,674</b>	<b>2,630</b>	<b>411</b>	-	-	-	-	<b>+117</b>
Extraordinary Balance	(1)	0	0	(67)	-	-	-	-	-	+1
Profit before Income Taxes	293	1,039	1,674	2,563	412	-	-	-	-	+118
Total Income Taxes	117	45	253	598	132	-	-	-	-	+14
NP Belonging to Non-Controlling SHs	-	1	2	3	-	-	-	-	-	(1)
<b>Profit Attributable to Owners of Parent</b>	<b>175</b>	<b>992</b>	<b>1,418</b>	<b>1,961</b>	<b>280</b>	-	-	-	-	<b>+105</b>
Sales YoY	+5.2%	+12.0%	+17.3%	+14.2%	+2.6%	-	-	-	-	-
Operating Profit YoY	(17.1%)	+12.4%	+43.7%	+38.2%	+40.0%	-	-	-	-	-
Recurring Profit YoY	(18.2%)	+11.5%	+42.2%	+37.8%	+39.8%	-	-	-	-	-
Profit Attributable to Owners of Parent YoY	(32.1%)	+60.4%	+82.4%	+53.0%	+60.2%	-	-	-	-	-
Gross Profit Margin	76.2%	80.9%	80.6%	81.9%	77.0%	-	-	-	-	+0.9%
Sales to SG&A Expenses Ratio	51.9%	43.5%	40.4%	36.9%	43.9%	-	-	-	-	(8.0%)
Operating Profit Margin	24.3%	37.5%	40.2%	45.0%	33.1%	-	-	-	-	+8.9%
Recurring Profit Margin	24.2%	37.6%	40.2%	45.0%	33.0%	-	-	-	-	+8.8%
Profit Attributable to Owners of Parent Margin	14.4%	35.9%	34.0%	33.6%	22.5%	-	-	-	-	+8.1%
Total Income Taxes / Profit before Income Taxes	40.1%	4.4%	15.1%	23.4%	32.0%	-	-	-	-	(8.0%)
Income Statement	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	YoY
(Million Yen)	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4		Net Chg.
	03/2019	03/2019	03/2019	03/2019	03/2020	03/2020	03/2020	03/2020	03/2020	
<b>Sales</b>	<b>1,217</b>	<b>1,546</b>	<b>1,402</b>	<b>1,674</b>	<b>1,249</b>	-	-	-	-	<b>+31</b>
Cost of Sales	289	236	282	250	286	-	-	-	-	(3)
Gross Profit	927	1,309	1,120	1,424	962	-	-	-	-	+34
SG&A Expenses	632	568	482	469	548	-	-	-	-	(83)
<b>Operating Profit</b>	<b>295</b>	<b>740</b>	<b>638</b>	<b>954</b>	<b>413</b>	-	-	-	-	<b>+118</b>
Non Operating Balance	0	4	(3)	1	(1)	-	-	-	-	(1)
<b>Recurring Profit</b>	<b>294</b>	<b>745</b>	<b>634</b>	<b>956</b>	<b>411</b>	-	-	-	-	<b>+117</b>
Extraordinary Balance	(1)	0	0	(67)	-	-	-	-	-	+1
Profit before Income Taxes	293	745	634	888	412	-	-	-	-	+118
Total Income Taxes	117	(71)	207	345	132	-	-	-	-	+14
NP Belonging to Non-Controlling SHs	-	-	-	-	-	-	-	-	-	(1)
<b>Profit Attributable to Owners of Parent</b>	<b>175</b>	<b>816</b>	<b>426</b>	<b>542</b>	<b>280</b>	-	-	-	-	<b>+105</b>
Sales YoY	+5.2%	+18.0%	+29.5%	+6.9%	+2.6%	-	-	-	-	-
Operating Profit YoY	(17.1%)	+30.9%	+163.0%	+29.4%	+40.0%	-	-	-	-	-
Recurring Profit YoY	(18.2%)	+30.3%	+158.6%	+30.7%	+39.8%	-	-	-	-	-
Profit Attributable to Owners of Parent YoY	(32.1%)	+126.5%	+168.0%	+7.7%	+60.2%	-	-	-	-	-
Gross Profit Margin	76.2%	84.7%	79.8%	85.1%	77.0%	-	-	-	-	+0.9%
Sales to SG&A Expenses Ratio	51.9%	36.8%	34.4%	28.0%	43.9%	-	-	-	-	(8.0%)
Operating Profit Margin	24.3%	47.9%	45.5%	57.0%	33.1%	-	-	-	-	+8.9%
Recurring Profit Margin	24.2%	48.2%	45.2%	57.1%	33.0%	-	-	-	-	+8.8%
Profit Attributable to Owners of Parent Margin	14.4%	52.8%	30.4%	32.4%	22.5%	-	-	-	-	+8.1%
Total Income Taxes / Profit before Income Taxes	40.1%	-	32.7%	38.8%	32.0%	-	-	-	-	(8.0%)

Source: Company Data, WRJ Calculation

### Sales by Market (Cumulative, Quarterly)

Sales by Market	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	YoY
(Million Yen)	Q1	Q1 to Q2	Q1 to Q3	Q1 to Q4	Q1	Q1 to Q2	Q1 to Q3	Q1 to Q4		Net Chg.
	03/2019	03/2019	03/2019	03/2019	03/2020	03/2020	03/2020	03/2020		
Enterprise Sector Market	688	1,419	2,134	3,133	725	-	-	-		+37
Public Sector Market	408	1,108	1,655	2,191	383	-	-	-		(25)
Consumer Sector Market	120	235	377	516	140	-	-	-		+19
<b>Sales</b>	<b>1,217</b>	<b>2,764</b>	<b>4,166</b>	<b>5,841</b>	<b>1,249</b>	-	-	-		<b>+31</b>
Enterprise Sector Market	+7.5%	+3.9%	+5.1%	+4.1%	+5.4%	-	-	-		-
Public Sector Market	(3.8%)	+20.2%	+32.7%	+26.5%	(6.3%)	-	-	-		-
Consumer Sector Market	+30.0%	+31.7%	+38.7%	+37.4%	+16.4%	-	-	-		-
<b>Sales (YoY)</b>	<b>+5.2%</b>	<b>+12.0%</b>	<b>+17.3%</b>	<b>+14.2%</b>	<b>+2.6%</b>	-	-	-		-
Enterprise Sector Market	56.5%	51.3%	51.2%	53.6%	58.1%	-	-	-		-
Public Sector Market	33.6%	40.1%	39.7%	37.5%	30.7%	-	-	-		-
Consumer Sector Market	9.9%	8.5%	9.0%	8.8%	11.2%	-	-	-		-
<b>Sales (Composition Ratio)</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	-	-	-		-
Sales by Market	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	YoY
(Million Yen)	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4		Net Chg.
	03/2019	03/2019	03/2019	03/2019	03/2020	03/2020	03/2020	03/2020		
Enterprise Sector Market	688	731	715	998	725	-	-	-		+37
Public Sector Market	408	699	546	536	383	-	-	-		(25)
Consumer Sector Market	120	115	141	139	140	-	-	-		+19
<b>Sales</b>	<b>1,217</b>	<b>1,546</b>	<b>1,402</b>	<b>1,674</b>	<b>1,249</b>	-	-	-		<b>+31</b>
Enterprise Sector Market	+7.5%	+0.7%	+7.5%	+2.2%	+5.4%	-	-	-		-
Public Sector Market	(3.8%)	+40.7%	+68.2%	+10.7%	(6.3%)	-	-	-		-
Consumer Sector Market	+30.0%	+33.5%	+52.0%	+34.2%	+16.4%	-	-	-		-
<b>Sales (YoY)</b>	<b>+5.2%</b>	<b>+18.0%</b>	<b>+29.5%</b>	<b>+6.9%</b>	<b>+2.6%</b>	-	-	-		-
Enterprise Sector Market	56.5%	47.3%	51.0%	59.7%	58.1%	-	-	-		-
Public Sector Market	33.6%	45.3%	38.9%	32.0%	30.7%	-	-	-		-
Consumer Sector Market	9.9%	7.5%	10.1%	8.3%	11.2%	-	-	-		-
<b>Sales (Composition Ratio)</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	-	-	-		-

Source: Company Data, WRJ Calculation

## Balance Sheet (Quarterly)

Balance Sheet	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	YoY
(Million Yen)	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4		Net Chg.
	03/2019	03/2019	03/2019	03/2019	03/2020	03/2020	03/2020	03/2020		
Cash & Deposit	4,616	5,224	5,356	6,169	6,430	-	-	-	-	+1,813
Accounts Receivables	1,038	1,144	1,100	1,172	998	-	-	-	-	(39)
Inventory	-	1	-	-	-	-	-	-	-	-
Other	149	129	76	387	153	-	-	-	-	+3
<b>Current Assets</b>	<b>5,805</b>	<b>6,499</b>	<b>6,535</b>	<b>7,729</b>	<b>7,582</b>	-	-	-	-	<b>+1,776</b>
Tangible Assets	168	166	164	261	257	-	-	-	-	+89
Intangible Assets	1,296	1,363	1,380	1,411	1,436	-	-	-	-	+139
Investments & Other Assets	782	1,113	1,088	456	453	-	-	-	-	(328)
<b>Fixed Assets</b>	<b>2,247</b>	<b>2,643</b>	<b>2,633</b>	<b>2,129</b>	<b>2,148</b>	-	-	-	-	<b>(99)</b>
<b>Total Assets</b>	<b>8,052</b>	<b>9,142</b>	<b>9,168</b>	<b>9,859</b>	<b>9,730</b>	-	-	-	-	<b>+1,677</b>
Accounts Payables	14	15	22	22	10	-	-	-	-	(4)
Advances Received	1,095	1,138	1,157	1,225	1,312	-	-	-	-	+217
Short Term Debt	-	-	-	-	-	-	-	-	-	-
Other	655	886	692	762	693	-	-	-	-	+37
<b>Current Liabilities</b>	<b>1,765</b>	<b>2,040</b>	<b>1,872</b>	<b>2,010</b>	<b>2,016</b>	-	-	-	-	<b>+250</b>
Long Term Debt	-	-	-	-	-	-	-	-	-	-
Other	45	45	45	46	46	-	-	-	-	-
<b>Fixed Liabilities</b>	<b>45</b>	<b>45</b>	<b>45</b>	<b>46</b>	<b>46</b>	-	-	-	-	-
<b>Total Liabilities</b>	<b>1,811</b>	<b>2,086</b>	<b>1,918</b>	<b>2,056</b>	<b>2,062</b>	-	-	-	-	<b>+251</b>
<b>Shareholders' Equity</b>	<b>6,201</b>	<b>7,020</b>	<b>7,211</b>	<b>7,752</b>	<b>7,624</b>	-	-	-	-	<b>+1,422</b>
Adjustments	40	35	38	50	43	-	-	-	-	+3
<b>Total Assets</b>	<b>6,241</b>	<b>7,056</b>	<b>7,250</b>	<b>7,802</b>	<b>7,667</b>	-	-	-	-	<b>+1,426</b>
<b>Total Liabilities &amp; Net Assets</b>	<b>8,052</b>	<b>9,142</b>	<b>9,168</b>	<b>9,859</b>	<b>9,730</b>	-	-	-	-	<b>+1,677</b>
Equity Capital	6,201	7,015	7,209	7,761	7,630	-	-	-	-	+1,429
Interest Bearing Debt	-	-	-	-	-	-	-	-	-	-
Net Debt	(4,616)	(5,224)	(5,356)	(6,169)	(6,430)	-	-	-	-	(1,813)
Equity Capital Ratio	77.0%	76.7%	78.6%	78.7%	78.4%	-	-	-	-	-
Net-Debt-Equity Ratio	(74.5%)	(74.5%)	(74.3%)	(79.5%)	(84.3%)	-	-	-	-	-
ROE (12 months)	20.8%	26.0%	29.8%	28.1%	29.9%	-	-	-	-	-
ROA (12 months)	23.9%	23.7%	29.4%	29.6%	30.9%	-	-	-	-	-
Total Assets Turnover	60%	68%	61%	68%	51%	-	-	-	-	-
Quick Ratio	320%	312%	345%	365%	368%	-	-	-	-	-
Current Ratio	329%	319%	349%	384%	376%	-	-	-	-	-

Source: Company Data, WRJ Calculation

## Cash Flow Statement (Cumulative)

Cash Flow Statement	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	Cons.Act	YoY
(Million Yen)	Q1	Q1 to Q2	Q1 to Q3	Q1 to Q4	Q1	Q1 to Q2	Q1 to Q3	Q1 to Q4		Net Chg.
	03/2019	03/2019	03/2019	03/2019	03/2020	03/2020	03/2020	03/2020		
Operating Cash Flow	-	1,377	-	3,091	-	-	-	-	-	-
Investment Cash Flow	-	(405)	-	(908)	-	-	-	-	-	-
<b>Operating CF &amp; Investment CF</b>	<b>-</b>	<b>972</b>	<b>-</b>	<b>2,183</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
Financing Cash Flow	-	(180)	-	(429)	-	-	-	-	-	-

Source: Company Data, WRJ Calculation

**Disclaimer**

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Information here is a summary of “IR Information” of the Company, compiled by Walden Research Japan, from a neutral and professional standing point, in the form of a report. “IR Information” of the Company comprises a) contents of our interview with the Company, b) contents of presentations for institutional investors, c) contents of timely disclosed information and d) contents of the homepage etc.

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