

# Presentation Material

for the Nine Months Ended December 31, 2019

February 7, 2019

Tokyo Stock Exchange First Section : Code 3676  
<https://www.digitalhearts-hd.com/>

# Q3 FY2019 Financial Results

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(The nine months ended December 31, 2019)

Net Sales

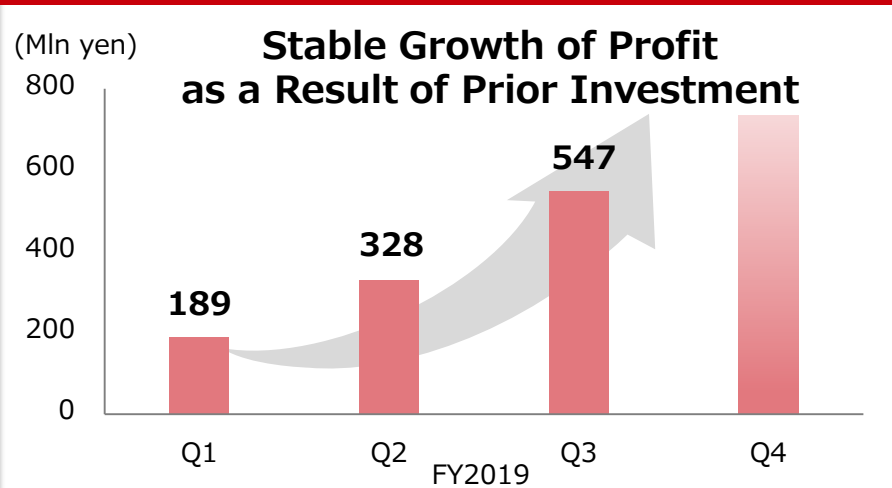
**15,677** Mln yen  
(YoY 108.9%)

Operating Income

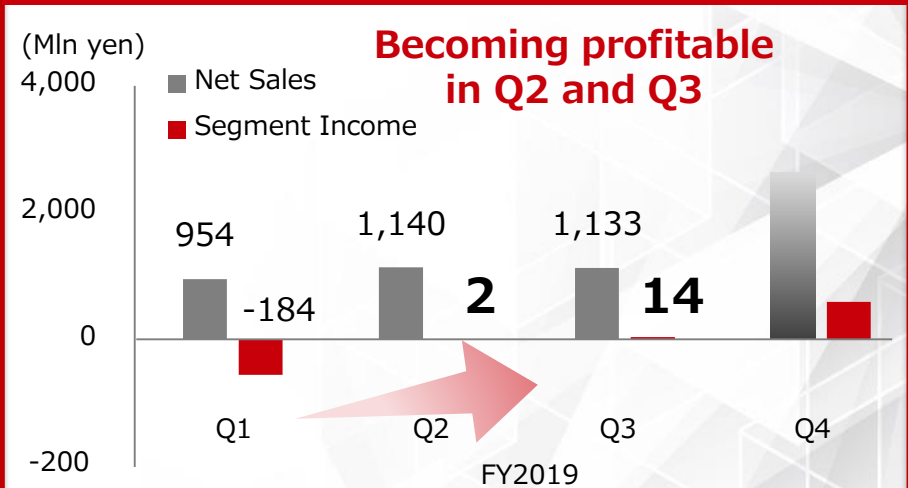
**1,066** Mln yen  
(YoY 85.9%)

- New **record-high sales** as nine months of Q3.
- The highest quarterly operating income of **547 Mln yen** in the latest two years.
- **Improvement of the profit** in both Entertainment and Enterprise Business.
- Made **Enterprise business profitable** in Q3 three months as well as Q2.

## Quarterly Consolidated Operating Income



## Quarterly Trend of Enterprise Business



# Summary of Financial Results for the Nine Months Ended December 31, 2019



New record-high sales in the nine months Q3 of the fiscal year.  
Operating income declined due to higher M&A-related expenses and others.

(Mln Yen)	Q3 FY2018	Q3 FY2019	YoY Change	
<b>Net sales</b>	<b>14,393</b>	<b>15,677</b>	<b>1,284</b>	<b>108.9%</b>
<b>Cost of sales</b>	<b>10,284</b>	<b>11,552</b>	<b>1,268</b>	<b>112.3%</b>
<b>Cost of sales (%)</b>	<b>71.5%</b>	<b>73.7%</b>		<b>+2.2 points</b>
<b>Gross profit</b>	<b>4,109</b>	<b>4,125</b>	<b>16</b>	<b>100.4%</b>
<b>SG&amp;A</b>	<b>2,867</b>	<b>3,059</b>	<b>191</b>	<b>106.7%</b>
<b>Operating income</b>	<b>1,241</b>	<b>1,066</b>	<b>-175</b>	<b>85.9%</b>
<b>Operating income margin</b>	<b>8.6%</b>	<b>6.8%</b>		<b>-1.8 points</b>
<b>Ordinary income</b>	<b>1,233</b>	<b>1,055</b>	<b>-177</b>	<b>85.6%</b>
<b>Profit attributable to owners of parent</b>	<b>847</b>	<b>652</b>	<b>-194</b>	<b>77.0%</b>

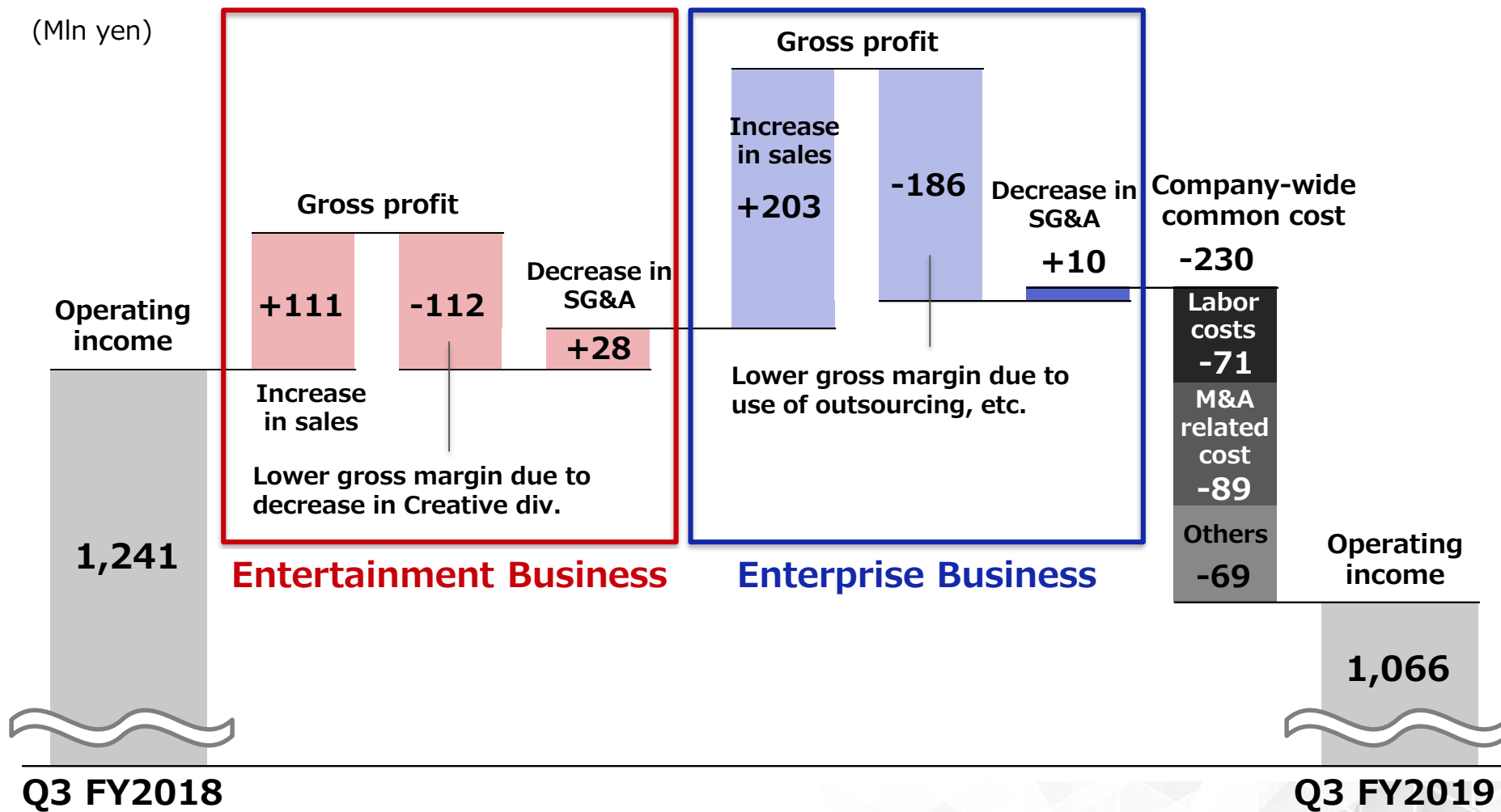
# Analysis of YoY Changes in Operating Income

- Compared with the Q3 FY2018 -



Improvement of profit in both Entertainment and Enterprise Business.  
Total profit declined due to increases in expenses for M&A, recruitment, education, etc.

(Mln yen)



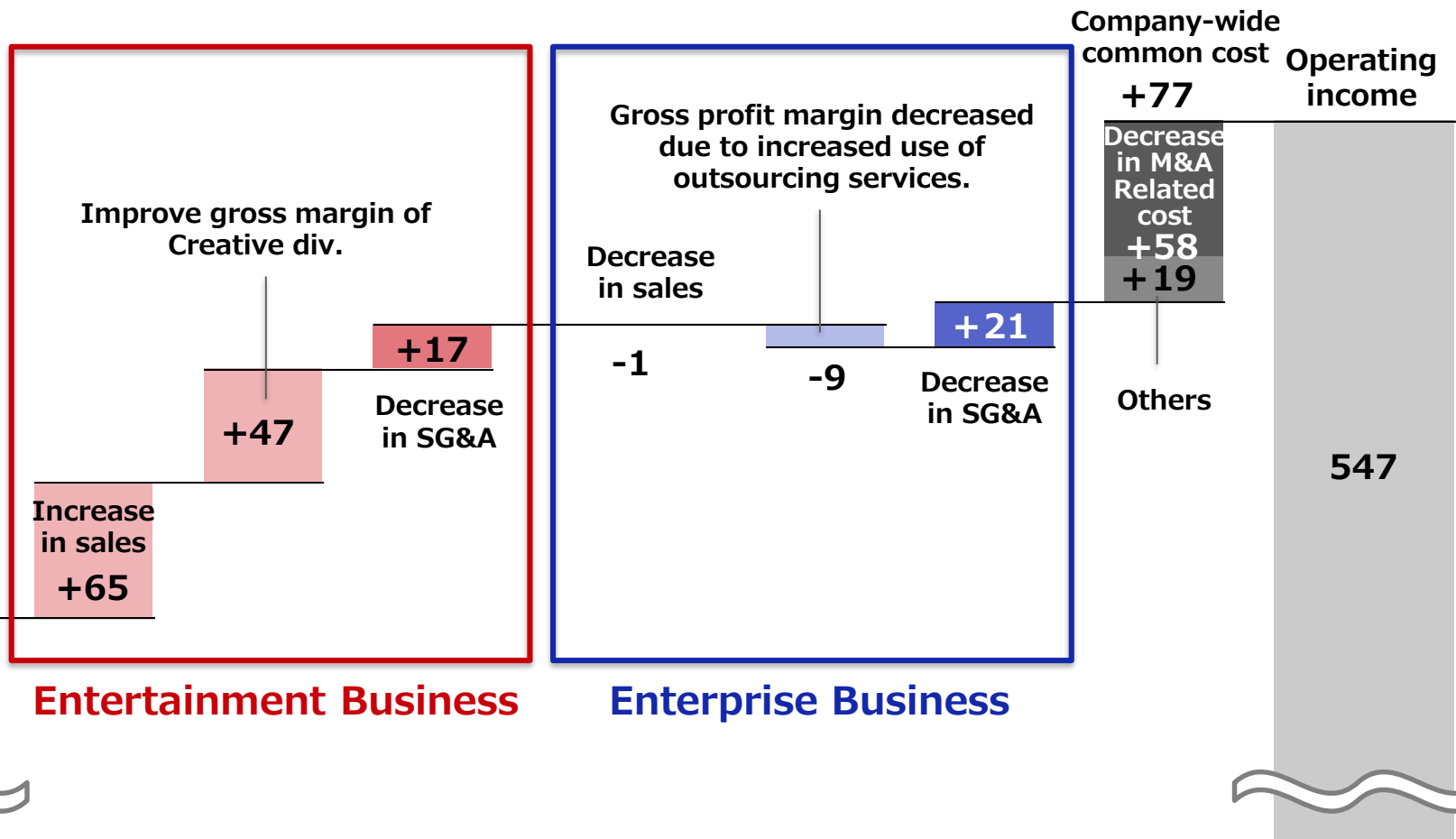
# Analysis of QoQ Changes in Operating Income

- Compared with the Q2 of current year -



Significant increase in profit due to the higher sales of Debugging services and the cost reduction mainly of M&A expenses incurred in Q2.

(Mln yen)



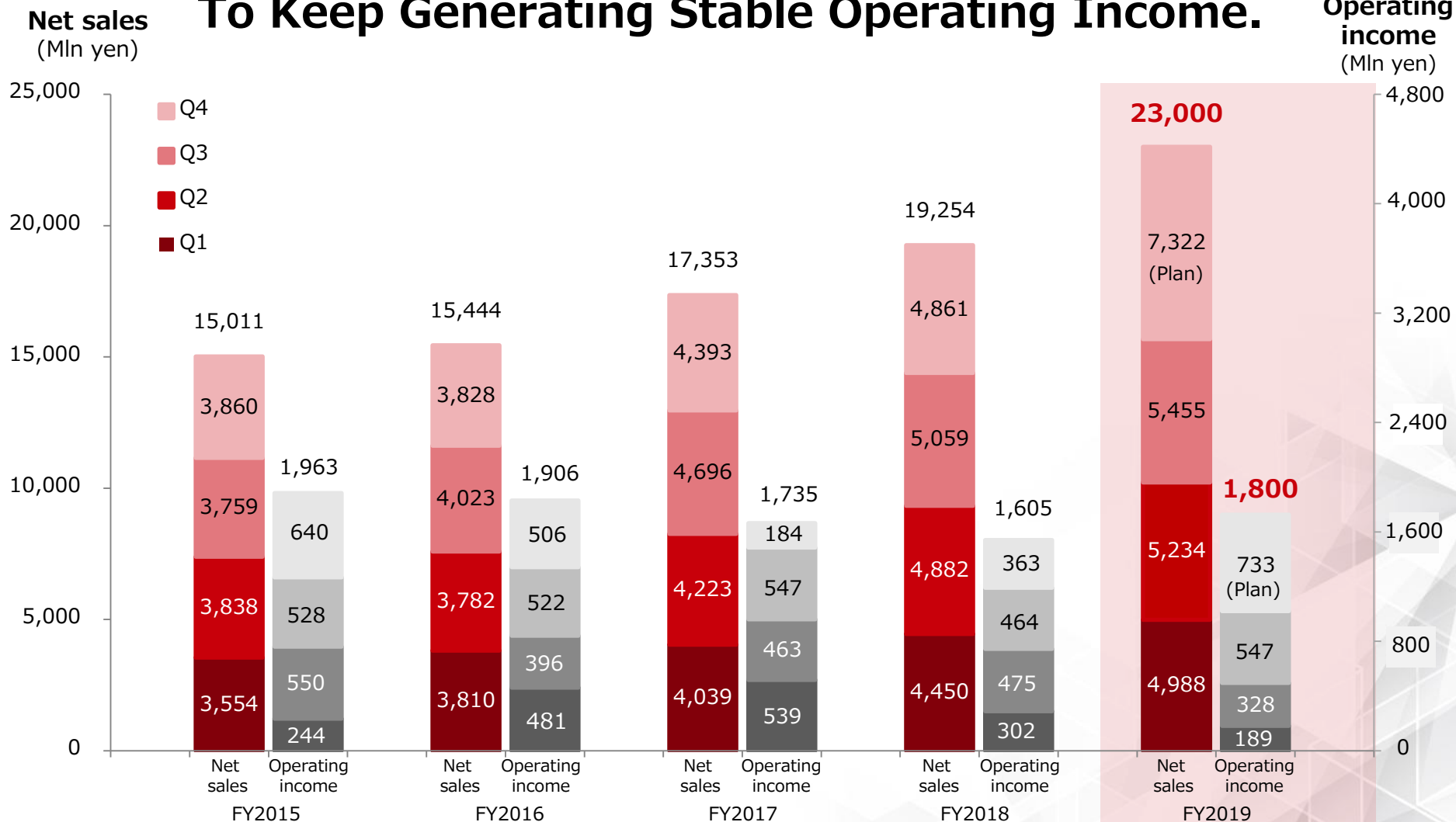
Q2 FY2019

Q3 FY2019

# Trend in Net Sales and Operating Income

Operating income for the third quarter reached **547 Mln yen**, the highest level in two years.

**To Keep Generating Stable Operating Income.**



# Consolidated Balance Sheets

(Mln Yen)	Q4 FY2018 (As of March 31, 2019)	Q3 FY2019 (As of December 31, 2019)	Change
<b>Total assets</b>	<b>9,832</b>	<b>10,938</b>	<b>1,106</b>
Current assets	7,403	7,710	306
Cash and deposits	4,197	3,882	-314
Notes and accounts receivable-trade	2,724	3,013	289
Noncurrent assets	2,428	3,227	799
Property, plant and equipment	558	627	69
Intangible assets	763	1,390	627
Investments and other assets	1,107	1,209	102
<b>Total liabilities</b>	<b>4,819</b>	<b>5,493</b>	<b>673</b>
Current liabilities	4,192	4,863	671
Short-term loans	1,704	2,506	801
Noncurrent liabilities	627	629	2
Convertible bond-type bonds with subscription rights to shares	508	508	—
<b>Total net assets</b>	<b>5,012</b>	<b>5,444</b>	<b>432</b>
Shareholders' equity	4,763	4,919	155
Accumulated other comprehensive income	28	22	-5
Subscription rights to shares	13	13	—
Non-controlling interests	207	489	282
<b>Total liabilities and net assets</b>	<b>9,832</b>	<b>10,938</b>	<b>1,106</b>



# Q3 FY2019 Financial results by Segment and Full year Forecast of FY2019

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【Notice regarding Earnings by Segment】

- Net sales by segment include inter-segment sales or transfers. Segment income is based on operating income.
- Segments changed from Q1 FY2018. For this reason, the figures for FY2017 and earlier by segment are reclassified to reflect the change in segments, and comparisons are made.

# Summary of Financial Results by Segment

- Improvement of profit in both Entertainment and Enterprise Business.
- Operating income declined due to increased expenses related to M&A.

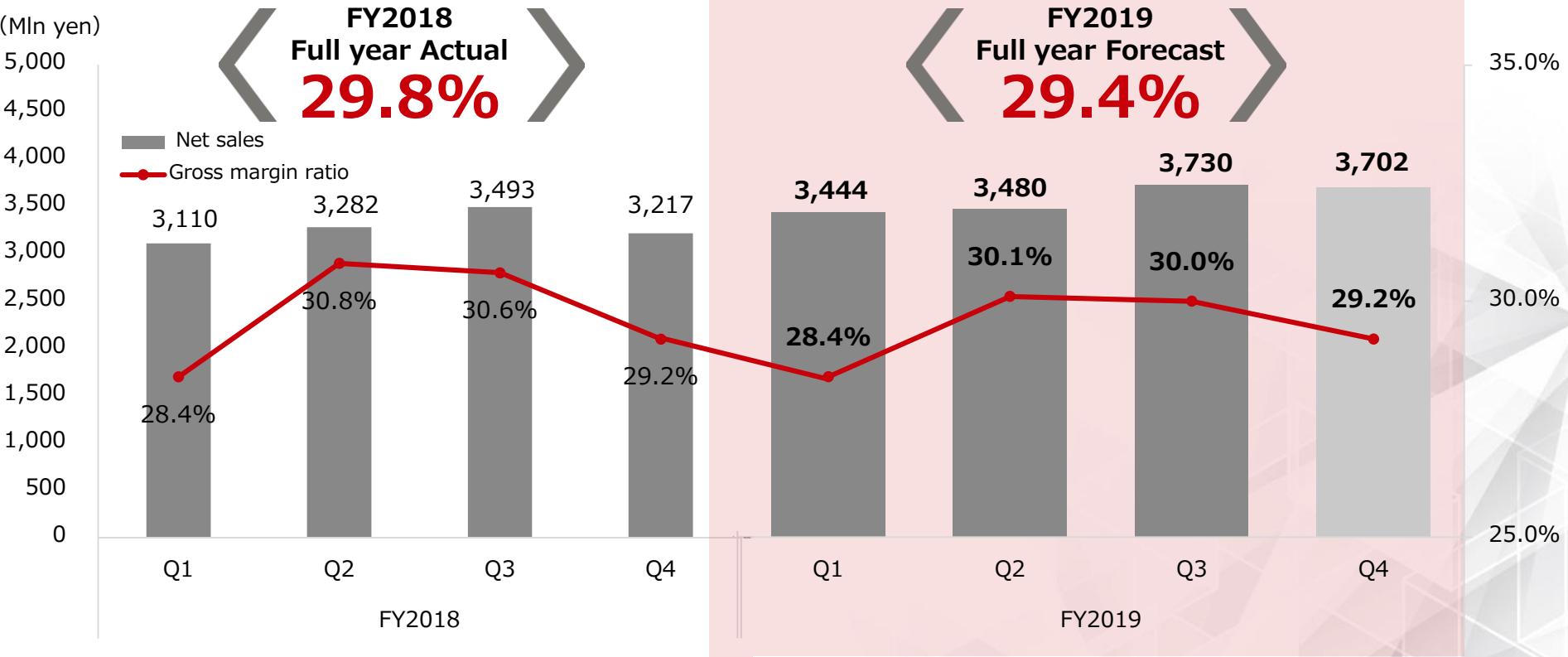
(Mln Yen)	Q3 FY2018	Q3 FY2019	YoY Change
<b>Net sales</b>	<b>14,393</b>	<b>15,677</b>	<b>108.9%</b>
Entertainment	12,074	12,449	103.1%
Enterprise	2,319	3,228	139.2%
Adjustments	-0	—	—
<b>Operating income</b>	<b>1,241</b>	<b>1,066</b>	<b>85.9%</b>
Entertainment	2,351	2,379	101.2%
Enterprise	-195	-167	—
Adjustments	-914	-1,145	—
<b>Operating income margin</b>	<b>8.6%</b>	<b>6.8%</b>	<b>-1.8 points</b>

- Stable growth of mainstay Debugging div. and increase in profit as well.
- Sharp decline in sales from Creative div. mainly due to the weak market trend of mobile games.

(Mln Yen)	Q3 FY2018	Q3 FY2019	YoY Change
<b>Net sales</b>	<b>12,074</b>	<b>12,449</b>	<b>103.1%</b>
Debugging	9,886	10,655	107.8%
Game Console (GC)	3,139	3,583	114.1%
Mobile Solutions (MS)	6,227	6,325	101.6%
Amusement (AM)	520	746	143.5%
Creative	1,495	940	62.9%
Media and others	692	853	123.3%
<b>Segment income</b>	<b>2,351</b>	<b>2,379</b>	<b>101.2%</b>

- Sales contribution of Orgosoft Co., Ltd. acquired in February 2019.
- Maintained Q3 gross margin of 30% thanks to bigger sales and improved operations.
- To keep the almost same gross margin as previous year led by restructuring of test centers' operation even with raising labor cost in Japan.

## Quarterly results of Debugging div.



## ■ Game Console dept. (GC)

Significant increase in sales by some large-scale titles, expecting new record-high annual sales.

## ■ Mobile Solutions dept. (MS)

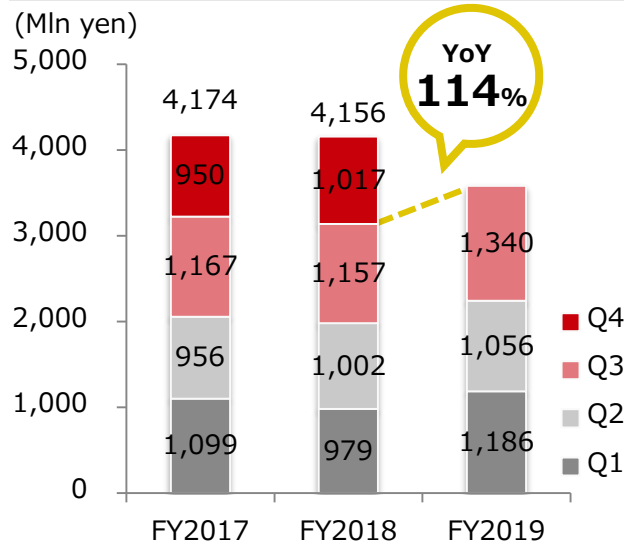
Slowing down of growth rate due to the weak market trend, but expected to remain steady.

## ■ Amusement dept. (AM)

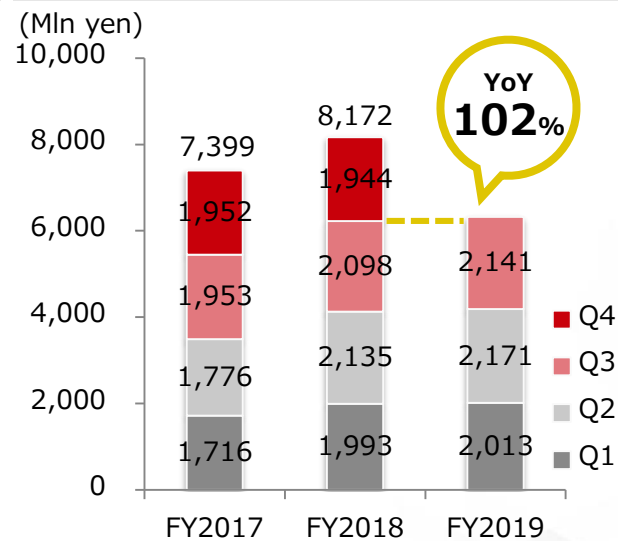
Recovering from the drop of sales by regulatory changes, but still in the unstable market condition.

### Quarterly sales

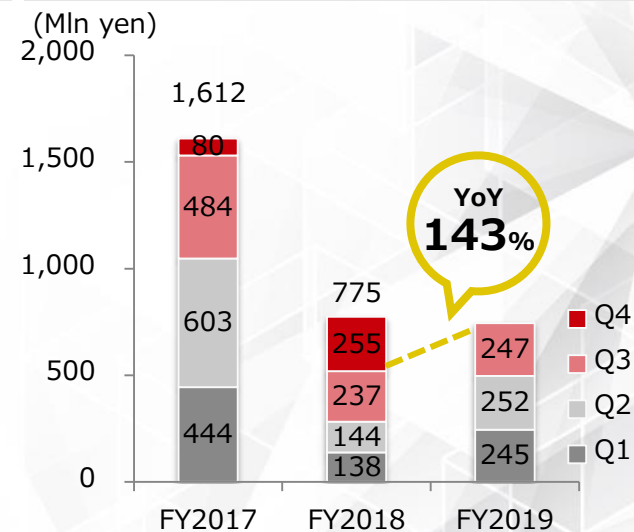
#### Game Console dept. (GC)



#### Mobile Solutions dept. (MS)



#### Amusement dept. (AM)



## ■ Creative

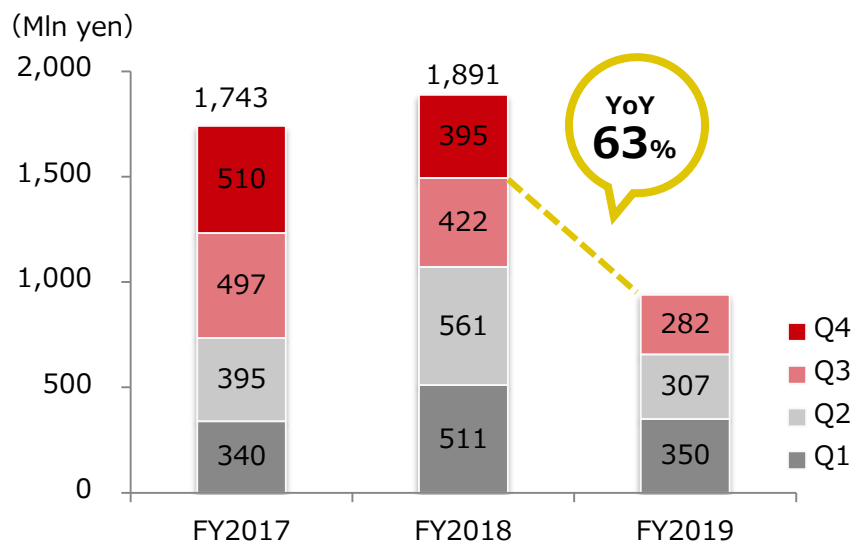
While 2D/3D graphics performed steadily, development of game software declined sharply. And strengthening new promotion initiatives.

## ■ Media and others

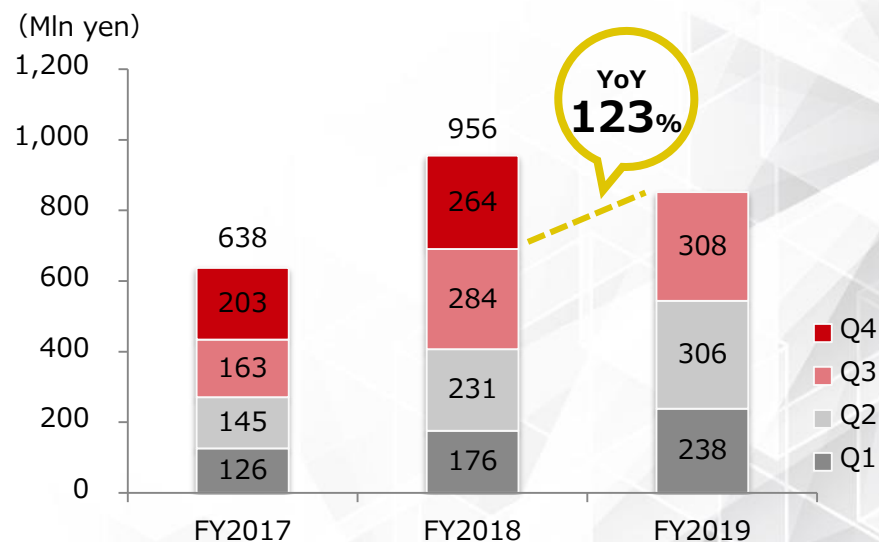
Higher sales in both “4Gamer.net” and customer support services.

### Quarterly sales

#### Creative



#### Media and others



- Becoming profitable in Q3 three months, same as in Q2, and continue to develop the profitable structure.

(Mln Yen)	Q3 FY2018	Q3 FY2019	YoY Change
<b>Net sales</b>	<b>2,319</b>	<b>3,228</b>	<b>139.2%</b>
System Testing	<b>911</b>	<b>1,489</b>	<b>163.3%</b>
IT service / Security	<b>1,407</b>	<b>1,738</b>	<b>123.6%</b>
<b>Segment income</b>	<b>-195</b>	<b>-167</b>	<b>—</b>

## Topics 1

**Acquired LogiGear Group**  
with rich knowledge and business records  
in test automation solutions

### [Strong points of LogiGear Group]

- **25years** corporate history in Silicon Valley
- Led by **top experts** in the testing market
- **Automated test tools** as LogiGear's original
- Approx. **500 test engineers** in Vietnam

## Topics 2

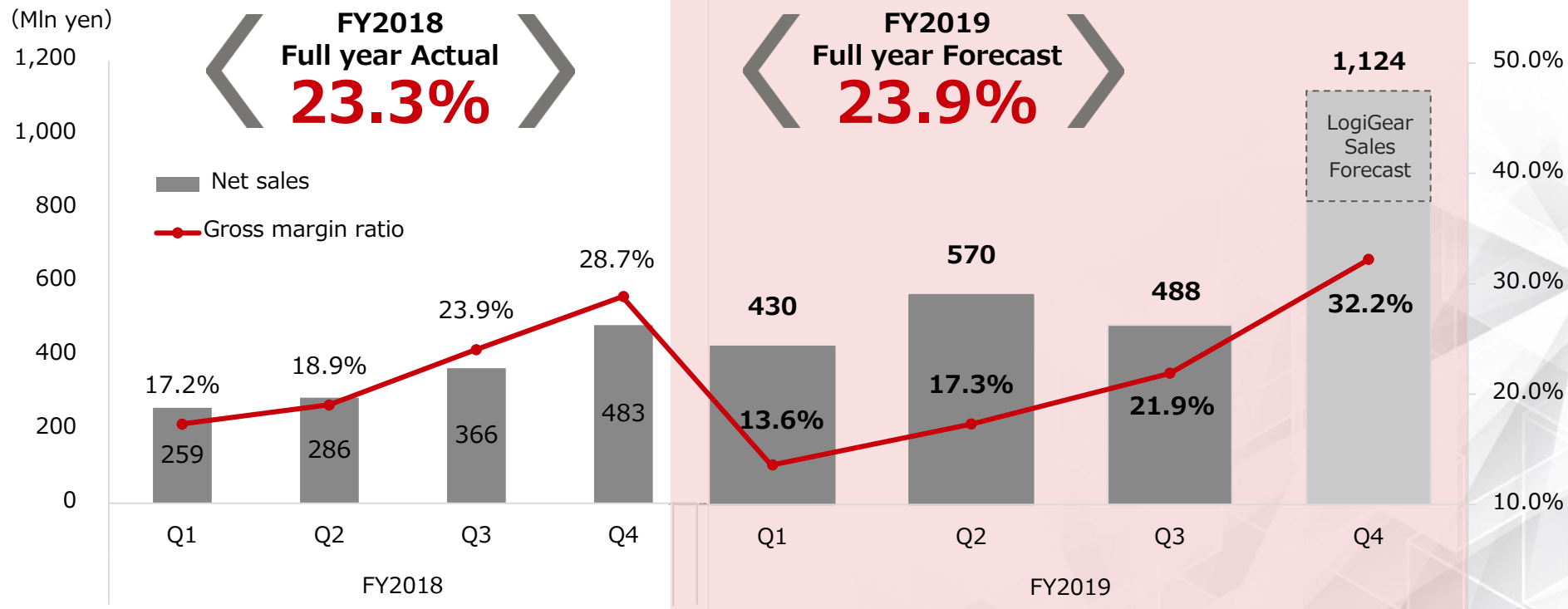
**Established JV with LAC Co., Ltd.**  
to expand the security business

### [Outline of Joint Venture Company]

- Company Name : Red Team Technologies Co., Ltd.
- Representative : Takuya Okada
- Business Activities : White hacker service and technical support
- Investment Ratio : DIGITAL HEARTS HOLDINGS 60%  
LAC 40%

- Gross profit margin improved thanks to several high-margin projects, despite the smaller Q3 sales compared to Q2.
- LogiGear Group, acquired in August 2019, is expected to be consolidated from Q4.
- Aiming for further improvement in gross margin through test automation service and others.

## Quarterly results of System Testing div.





## ■ System Testing

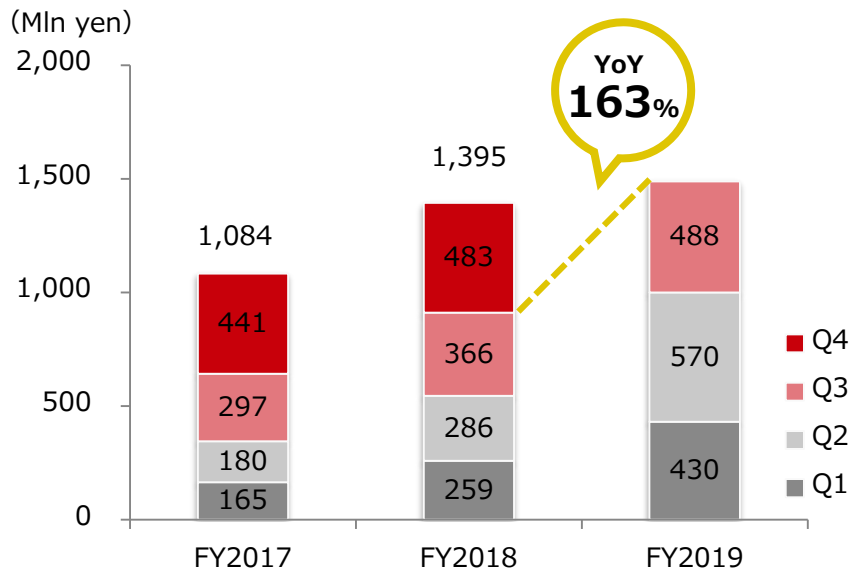
Significant increase in sales due to the steady development of new customers and the expansion of transaction volume per company.

## ■ IT service / Security

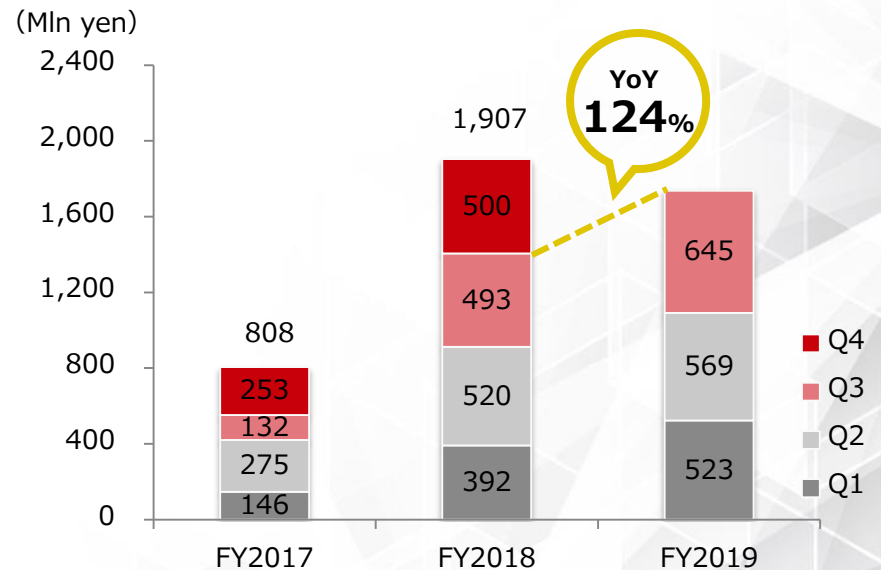
Strong performance in both system development and security services.  
Established of a joint venture with major domestic securities company LAC Co., Ltd.

### Quarterly sales

#### System Testing



#### IT service / Security



**From the second half, to be the investment recovery phase.  
Aiming for higher sales and profits year-on-year, while keeping the  
initial plan unchanged**

(Mln Yen)	Full year FY2018 (Actual)	Full year FY2019 (Forecast)	YoY Change
<b>Net sales</b>	<b>19,254</b>	<b>23,000</b>	<b>119.5%</b>
Entertainment	15,951	17,130	107.4%
Enterprise	3,302	5,870	177.7%
<b>Operating income</b>	<b>1,605</b>	<b>1,800</b>	<b>112.1%</b>
Operating income margin	8.3%	7.8%	-0.5 points
<b>Ordinary income</b>	<b>1,651</b>	<b>1,830</b>	<b>110.8%</b>
<b>Profit attributable to owners of parent</b>	<b>1,575</b>	<b>1,250</b>	<b>79.3%</b>

# Progress of the Second Start-up Period

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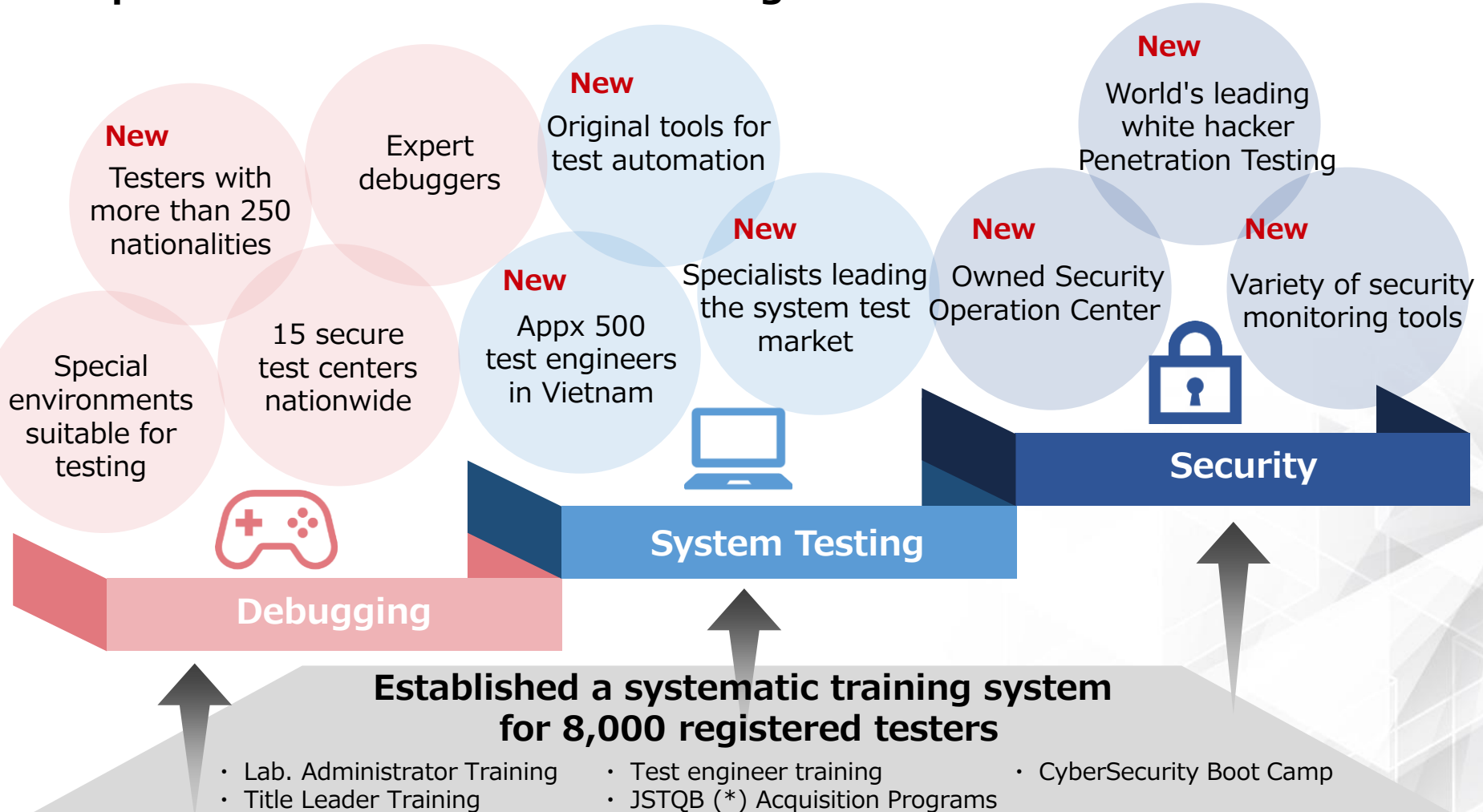
(These pages from P19 to P24 are extracted from the Q2 presentation material disclosed on November 11, 2019.)

To be the Asia's No.1 company for comprehensive testing Solutions

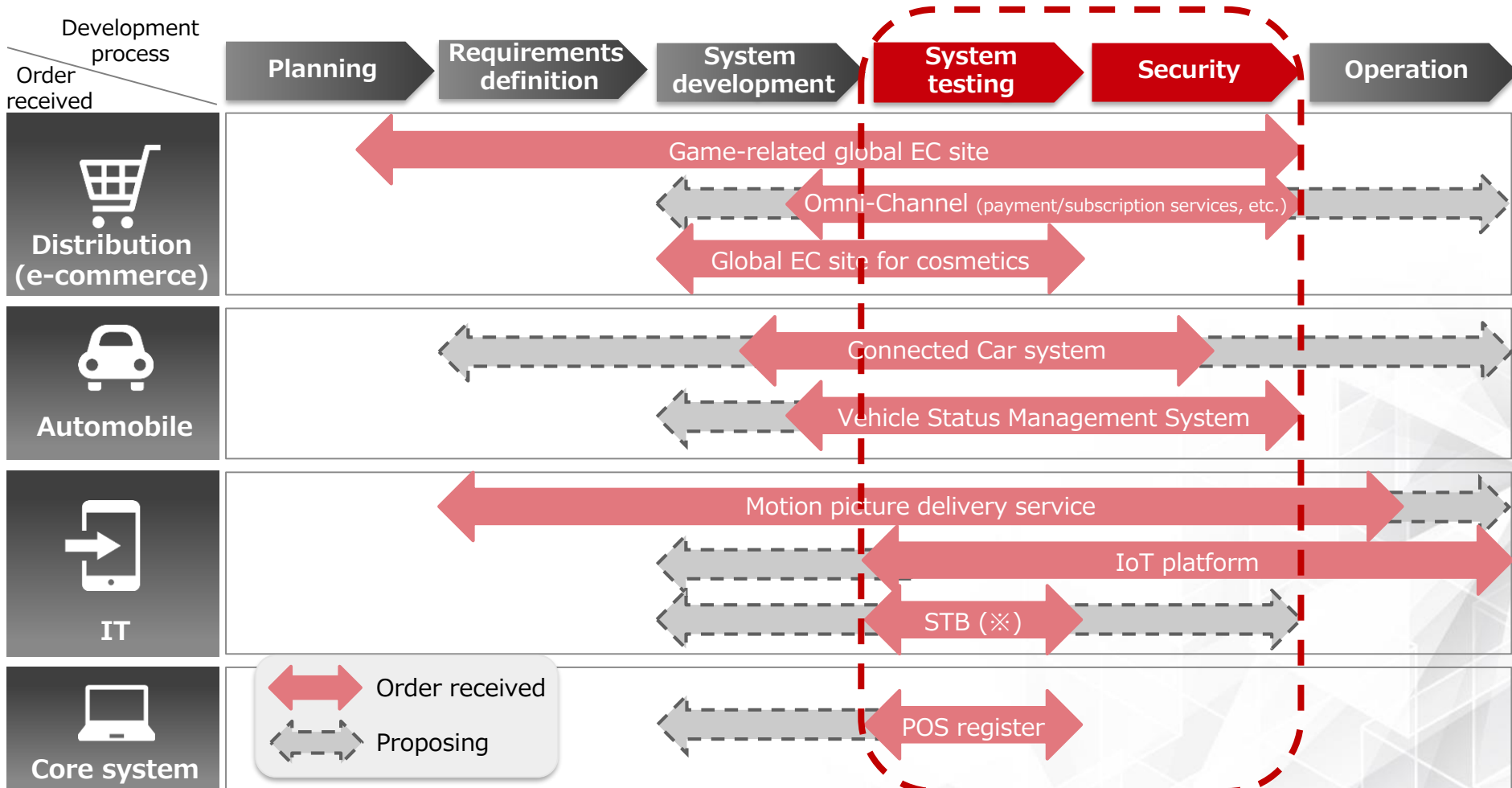
# Human Capital × Technology



## Strengthening of human capital and technologies to provide various services reacting to new demands in the market



Increased number of projects acquired in a wide range of development processes as services are diversified and improved quality



## Orders for trial of test automation projects

### Examples of Test Automation Trial Orders

#### Case1 Mobility services software



##### Test Description

Fatal Failure Detection

##### Trial period

2 months

##### Status

Completion of the trial  
Entering into this Agreement

#### Case2 Game Platform



##### Test Description

In the tutorial  
Test automation

##### Trial period

2 months

##### Status

During a trial

#### Case3 Office Integration Software



##### Test Description

Automating Regression  
Tests

##### Trial period

1 month

##### Status

Completion of the trial  
Negotiating for this Agreement

#### Case4 Connected Car system



##### Test Description

Automating Regression  
Tests

##### Trial period

Undetermined

##### Status

From the end of November  
2019  
Start Trial

### Client's expectations for our groups

1. **Improve product quality** : Automation of areas where testing was inadequate due to human and time constraints
2. **Knowledge of automation** : Technical support for companies that cannot automate because of lack of knowledge and know-how
3. **Improving test quality** : Execute highly accurate tests without human errors, etc.

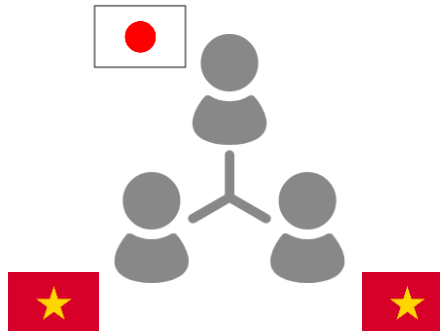
## Strengthened a cross-group service structure to acquire more test automation projects

Strengthening professional sales resources to suggest test automation



- ✓ Periodic study sessions
- ✓ Developing Sales Engineers

Increase in the number of bridge engineers connecting Japan and Vietnamese sites



- ✓ Strengthening the adoption of Vietnamese engineers in Japan
- ✓ Interchange of human resources between Japan and Vietnamese sites

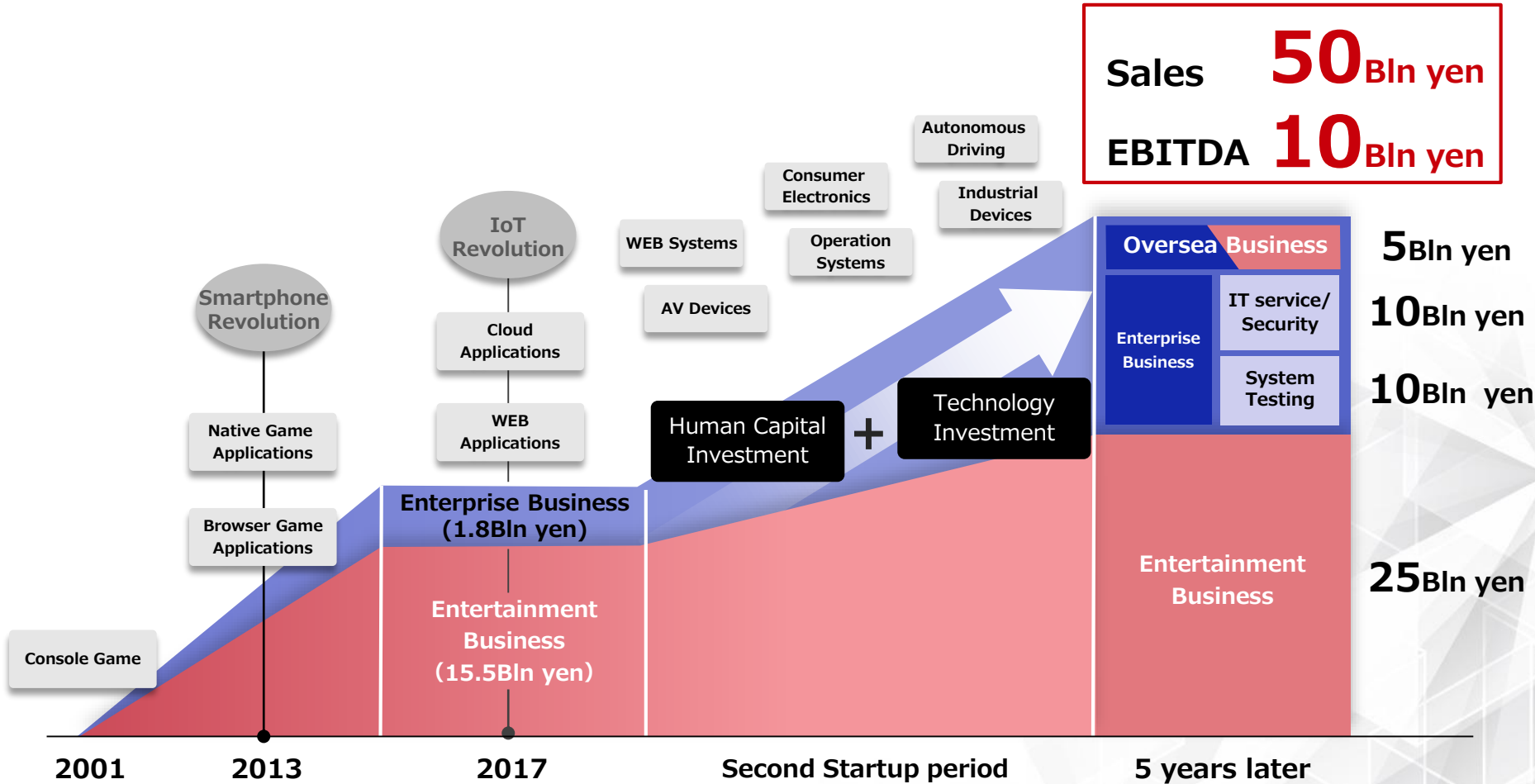
Development of automation tools for the Japanese market



- ✓ To develop tools specifically for testing Japanese Web/ apps
- ✓ Collaboration of tools to automate the entire process of multi-terminal verification



## To be the Asia's No.1 Company for Comprehensive Testing Solutions



# Appendix

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# Why You Should Invest in DIGITAL HEARTS

Employment creation  
for more than  
**8,000** testers



Ratio of  
external officers of  
**40.0%**



One of the few  
testing focusing companies  
in Japan



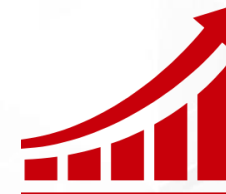
Business that supports  
**Digital security**



Foreign staff  
members of more  
than  
**20** nationalities



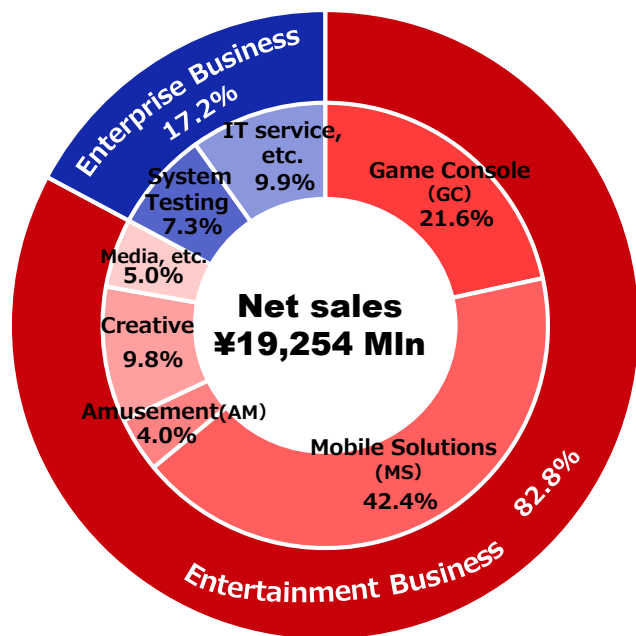
High market growth rate\* with  
CAGR at **27.5%**



\*Data on the growth rate of the market of outsourced software testing services for 2017 to 2021, prepared by DIGITAL HEARTS in reference to a range of data.

(References) Websites related to Global Pure Play Software Testing Services Market 2017-2021 and Global Software Testing Market 2017-2021

## Debugging and System testing are our core business

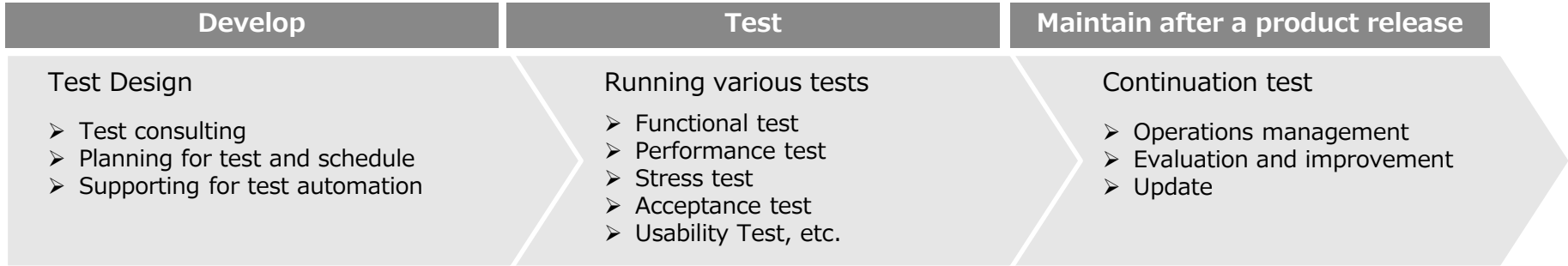


### Sales breakdown by segment (FY2018)

※Sales of each segment and unit include inter-company sales and/or transfers.

Business Segment	Sub-segment	Percentage	Description
Entertainment Business	Debugging	21.6%	<b>Game Console (GC)</b> Debugging for console games, online games, and arcade games
		42.4%	<b>Mobile Solutions (MS)</b> Debugging for mobile games
		4.0%	<b>Amusement (AM)</b> Debugging for pachinko/slot machines
	Creative	9.8%	Game development and CG content development
	Media and others	5.0%	Managing one of Japan's largest game information site "4Gamer.net", customer support, etc.
	Enterprise Business	System Testing	7.3%
IT service / Security		9.9%	System development, IT support, Customer support, Security, etc.

## Our Services



## Outline of Services

Service	Description	Main client	Barriers to entry	Outsourced Projects Ratio
<b>Debugging</b>	Detection of bugs in games from a player's perspective.	– Game makers	<p>High</p> <ul style="list-style-type: none"> <li>↑ A license for purchasing dedicated equipment for debugging is required.</li> <li>↑ Knowledge and expertise on human resource management to accommodate changeable development schedules are required.</li> </ul>	High
<b>System Testing</b>	Detection of bugs in enterprise systems from a test-engineers' knowledge.	<ul style="list-style-type: none"> <li>– SIers</li> <li>– Development vendors</li> <li>– Core system enterprises</li> </ul>	<p>Middle</p> <ul style="list-style-type: none"> <li>↑ Human resource shortage in IT Industry</li> </ul>	Low

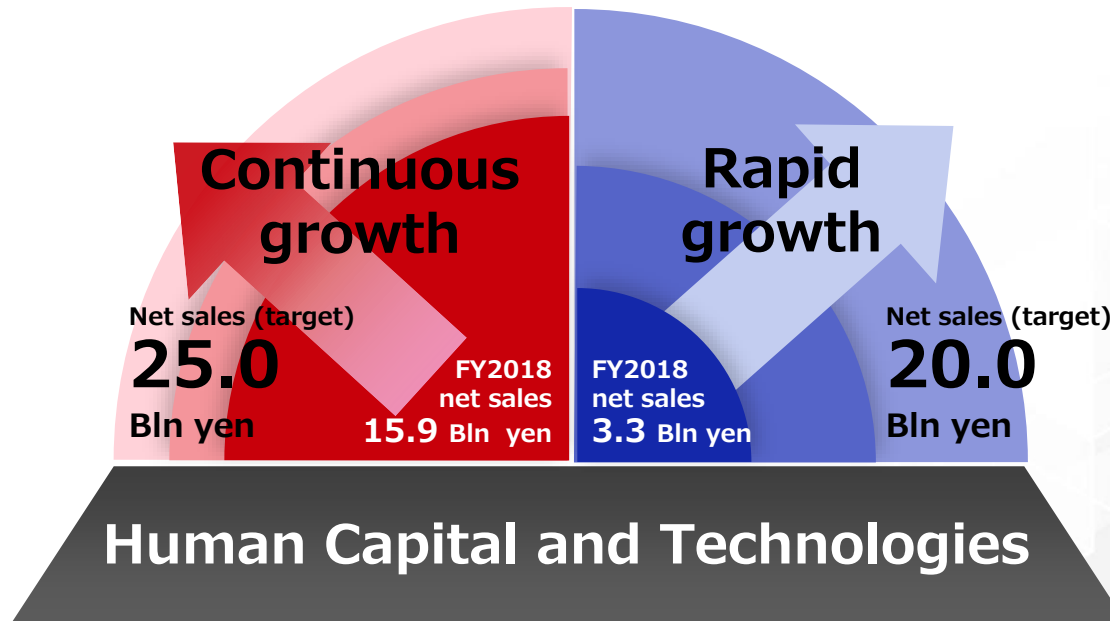
## Pursue the growth of the mainstay Entertainment Business and make the Enterprise Business another primary source of revenue

### Entertainment Business

- The game market is growing steadily
- ◆ Strengthen collaboration within the Group to provide comprehensive support for game development, including not only debugging but also the development of outsourced services and localization
- ◆ Continue expanding the business, targeting net sales of 25.0 billion yen

### Enterprise Business

- The outsourcing of test processes is accelerated, due in part to the serious human resources shortage in the IT industry
- ◆ Accelerate investment in human capital and technologies for business expansion
- ◆ Position this field as the growth driver and aim for net sales of 20.0 billion yen



## Major risks

## Countermeasures

### 1. Leakage of confidential information

- Prohibiting staff members from bringing personal items into the test room
- Physical security measures including access control with fingerprint authentication and the installation of security cameras
- Introduction of a personal reference system that applies to all registered testers

### 2. Obsolescence of existing services by technological innovation

- Focusing on the application of the latest technologies, including a test automation project
- Focusing on the development of new services to improve added value

### 3. Reduction of productive population in Japan

- Developing internal training programs that will enable the active participation of members with diverse generational, racial, and other backgrounds
- Securing human resources strategically by using overseas offices as well

### 4. Expansion of corporate acquisition and new businesses

- In-depth market research and due diligence
- Reducing risks by building a system for appropriate business management after acquisition

# Summary of Earnings by Segment

(Mln yen)		FY2014	FY2015	FY2016	FY2017	FY2018
<b>Entertainment Business</b>	<b>Net sales</b>	<b>11,609</b>	<b>12,696</b>	<b>13,544</b>	<b>15,568</b>	<b>15,951</b>
	<b>Segment income</b>	<b>1,915</b>	<b>2,379</b>	<b>2,453</b>	<b>2,966</b>	<b>3,086</b>
Debugging	Net sales	9,430	10,455	11,524	13,186	13,103
	Game Console (GC)	3,604	3,449	3,483	4,174	4,156
	Mobile Solutions (MS)	3,554	4,994	6,262	7,399	8,172
	Amusement (AM)	2,272	2,012	1,778	1,612	775
Creative	Net sales	1,675	1,729	1,465	1,743	1,891
Media and others	Net sales	504	512	554	638	956
<b>Enterprise Business</b>	<b>Net sales</b>	<b>1,713</b>	<b>2,382</b>	<b>1,952</b>	<b>1,892</b>	<b>3,302</b>
	<b>Segment income</b>	<b>50</b>	<b>71</b>	<b>203</b>	<b>-14</b>	<b>-226</b>
System Testing	Net sales	380	681	758	1,084	1,395
IT service / Security	Net sales	1,333	1,701	1,193	808	1,907
Inter-segments adjustments	Net sales	-39	-70	-52	-108	-0
	Segment income	-447	-486	-750	-1,215	-1,254
Consolidated total	Net sales	13,285	15,011	15,444	17,353	19,254
	Operating income	1,517	1,963	1,906	1,735	1,605



## Review of shareholder return policy

**Actively invest in medium- and long-term growth as the second startup period. Change the shareholder return policy for this purpose in consideration of the balance between internal reserves and shareholder returns.**

### ■ FY2018 or before:

Paid stable dividends in accordance with the consolidated business results, **with DOE of 7% as a guide**. Also provided **shareholder benefits** to shareholders who held our shares as of March 31 every year.

### ■ FY2019 and after:

Pay stable dividends in accordance with the consolidated business results, **with the lower limit of the dividend payout ratio at 20%**. **Abolish the shareholder benefit plan** from the viewpoint of shareholder equity.

## Shareholder returns in FY2019

	Interim dividends	Year-end dividends	Annual total dividends	Shareholder benefits
FY2018	6.5 yen	6.5 yen	13.0 yen	(Holders of one or more units of shares) <b>Rice gift cards (3 kg)</b> (Holders of two or more units of shares) <b>Rice gift cards (6 kg)</b>
FY2019 (forecast)	7.0 yen	7.0 yen	14.0 yen	<b>Up 1.0 yen</b> —

\* We will acquire treasury shares flexibly by considering the necessity in light of our capital policy, the impact on our financial strength, and other factors, after securing funds for investment in growth.

# Corporate Profile

Company Name

DIGITAL HEARTS HOLDINGS Co., Ltd.

Capitalization

¥300,686,000

Location

3-20-2 Nishi-Shinjuku, Shinjuku-ku,  
Tokyo

Shares Issued

23,890,800 Shares

Incorporated

October 1, 2013

Fiscal year end

March 31

Representative

President and CEO, Genichi Tamatsuka

Number of Employees

1,328 (Consolidated)

Stock Exchange

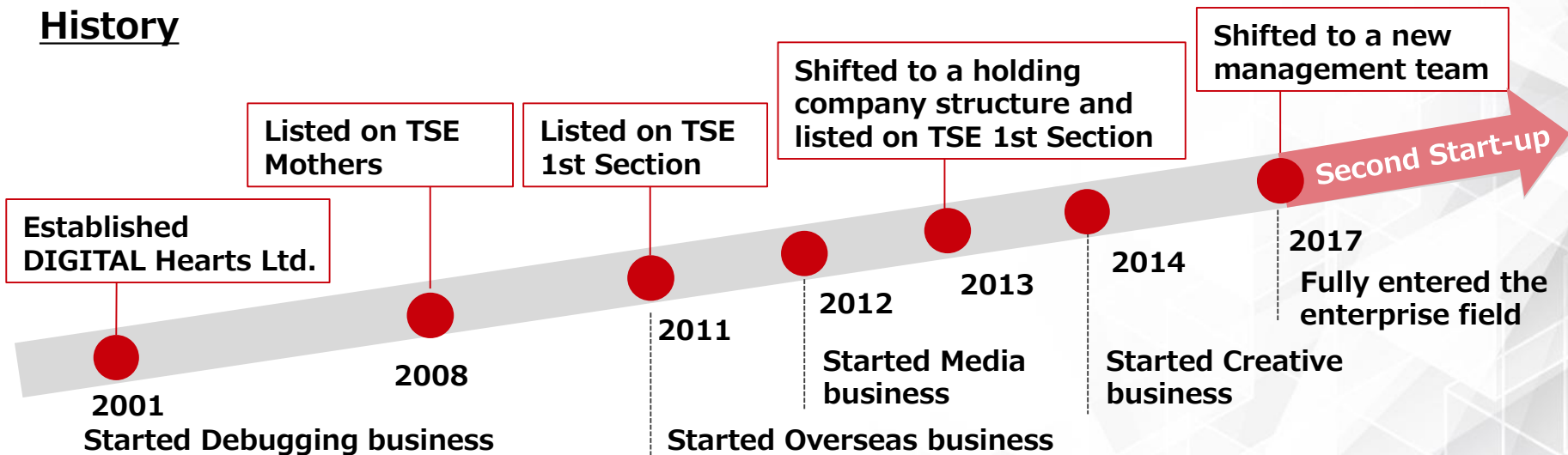
Tokyo Stock Exchange The 1st Section  
(code : 3676)

Group Companies

Domestic:9  
Overseas:6

(As of December 31, 2019)

## History



(As of December 31, 2019)

## DIGITAL HEARTS Co., Ltd.

Entertainment Business

Enterprise Business

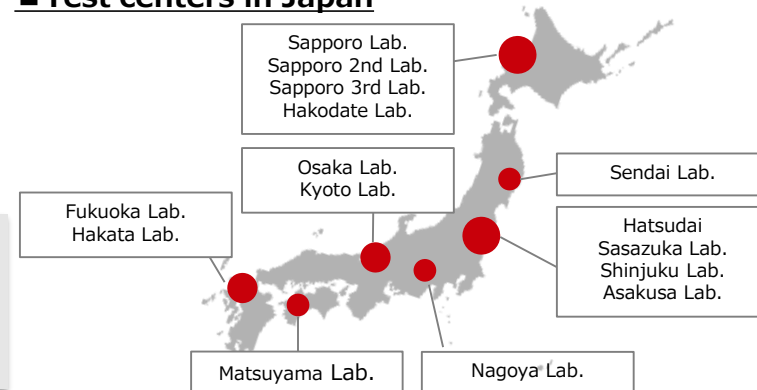


Business Activities : Game debugging, Localization, System testing, System development, Security, etc.

[Strengths]

- **Over 8,000** registered testers
- **Over 1.5 million** bug data
- **15** test centers (Lab.)
- **Over 4,000** equipment for testing

### ■ Test centers in Japan



## DIGITAL HEARTS USA Inc.

Entertainment Business



Business Activities : Localization, etc.

## DIGITAL HEARTS (Shanghai) Co., Ltd.

Entertainment Business



Business Activities : Game debugging, Localization, etc.

## Orgosoft Co., Ltd.

Entertainment Business



Business Activities : Game debugging, Localization, etc.

## ANET Corporation

Enterprise Business



Business Activities : System testing, System development, etc.

## LOGIGEAR CORPORATION

Enterprise Business



Business Activities : System Testing, Test Automation Support, System Development, etc.

## DIGITAL HEARTS GNT VIET NAM COMPANY LIMITED

Enterprise Business



Business Activities : System testing, etc.

## FLAME Hearts Co., Ltd.

Entertainment Business



Business Activities : Game development and CG content development

## Aetas, Inc.

Entertainment Business



Business Activities : Operation of a game information site, "4Gamer.net", etc.

## ZEG Inc.

(Affiliated company)

Enterprise Business



Business Activities : Driving test and data collection for the automotive industry



DIGITAL HEARTS HLDGS.

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