

7618 PC DEPOT Corporation

Resuming of Solution Services, Mainly for Premium Members

December 15, 2017

First section of Tokyo Stock Exchange (TSE)

Key Points

- The Company launched the member-service-inclusive products in September which clearly entail membership and incorporate premium services on a four-year contract basis. With the new sales system almost in place, the Company has shifted to a more aggressive approach.
- The Company appropriately responded to a case that occurred in August last year where services for an elderly customer were deemed inappropriate. The Company has since created improvement guidelines, and has further improved its customer services by having consumer advisers take part in the creation of a Quality Management Department and a Customer Service Promotion Department. The problems caused by harmful rumors have been fully settled and procedures are being rapidly implemented at stores.
- The Company is making every possible effort to regain trust toward achieving its primary goal of fulfilling its "social mission to solve problems in IT society." The situation is looking up, with customers favorably accepting the improvements. The Company has been checking what is being offered with each service for the roughly 400,000 members. The cancellation rate of service subscriptions has been decreasing and the number of members is close to a transition from a net decrease to a net increase.
- Business earnings bottomed out. The Company has since entered a recovery phase as seen in the following points: (1) a decrease in the cancellation rate, (2) sales from solution services turned positive in October, (3) the increased costs for actions taken by the Company have leveled off, and (4) sales capabilities at stores are recovering. The share buyback (one billion yen) in August demonstrated a positive signal effect that expresses the intentions of the Company.
- The earnings will increase from the second half of the term ending March 2018. The operating income will improve, from 2.1 billion yen and 1.3 billion yen for the first and second halves of the previous term and 1.2 billion yen for the first half of the current term, respectively to 1.4 billion yen for the second half of the current term. The operating income is expected to further increase to 3.5 billion yen and 4.5 billion yen for the terms respectively ending March 2019 and March 2020.
- The Company's business model will enter the next stage. As the Company boosts its service system to further meet customer needs, a more rigid system will be established. This system will capture a higher demand for services and will retain more repeat customers even though costs will increase. Profit is therefore highly likely to recover and grow even higher than before. As profit is expected to achieve a record high in a few years, the Company seems to be in a noteworthy phase.

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Company rating: B

Stock price (December 14, 2017): 864 yen

Market capitalization: 45.5 billion yen (52.622 million shares)

PBR 1.93

ROE 7.9%

PER 24.8

Dividend yield: 1.5%

(except where otherwise indicated, figures are in millions of yen)

Fiscal yearend	Sales	Operating	Ordinary	Net	EPS	Dividend
Mar. 2010	44740	1226	1306	677	17.3	3.9
Mar. 2011	46872	1308	1447	683	19.0	3.9
Mar. 2012	49631	526	684	238	6.0	3.9
Mar. 2013	51359	867	924	441	11.2	3.9
Mar. 2014	53772	2256	357	1536	38.0	4.7
Mar. 2015	51261	3045	3162	1914	42.0	6.9
Mar. 2016	51729	4086	4139	2693	56.9	9.6
Mar. 2017	46417	3402	3467	2269	44.1	13.0
Mar. 2018 (forecast)	45000	2600	2680	1770	34.8	13.0
Mar. 2019 (forecast)	47000	3500	3500	2330	36.4	13.0

Total assets: 34, 225 million yen Net assets: 22,511 million yen Equity ratio: 65.6%

BPS: 448.5 yen

NOTE: ROE, PER and dividend yield are based on the most recent forecast. In October 2013, the Company carried out a share split at a ratio of 1:100, in January 2015, a share split at a ratio of 1:1.5 and in October 2016, a share split at a ratio of 1:1.2. The EPS and dividends for the preceding terms have been revised accordingly. Corrections of financial results from prior terms due to revisions to the balance of accounts receivable were made for the terms covering the term ended March 2012 to the term ended March 2017.

Analysis by: Yukio Suzuki

(Chief Analyst, Belle Investment Research of Japan)

Definition of Company rating: Qualitative evaluation based on criteria such as 1) management capabilities; 2) abilities to grow/maintain the business; 3) possibilities of downward revisions to earnings forecasts. The Company is expressed as a four-level rating where "A" means good, "B" means some degree of improvement is required, "C" means considerable improvement is required, and "D" means the state of the company is extremely grave.

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1. Characteristics: Evolution to stores specializing in Internet device services

Bridging the digital divide is a corporate mission

Throughout the past year, a company-wide effort has been made to respond to a case that occurred in August last year where a contract with an elderly customer was inappropriate. The Company finally started to regain the trust of our customers.

PC DEPOT is prioritizing support for customers struggling to use digital network devices. To this end, the Company is improving its services in a slow and steady manner. These efforts cultivate a service market, enabling the Company to achieve its unique business model. President Nojima says that the Company will take up challenges but will not take excessive risks. The Company will conduct experiments, confirming a new course of action before carefully expanding business.

The Company has been developing IT solution stores known as Smart Life stores that customers can maintain a relationship with over the long term. Instead of merely enjoying the convenience of a neighborhood PC superstore, users can have the Company solve the problems they experience when using IT equipment and networks.

New devices and services are continuously entering the market, which is a characteristic of the information and communication technology market. Customers need support in order to maintain an IT environment that enables them to fully utilize the products and services they use. SLP stores provide services and detailed explanations so that users can make full use of the features of their desktops, notebooks, smartphones, tablets (multi-function mobile terminals), and other devices, as well as meeting any other user requirements as part of a total set.

These services are truly convenient. If consumers use products over a long period of time, in addition to the profit generated at the time they make the purchase, it is quite likely they will start to pay fees for services that make using such products more convenient. To make this happen, users must be satisfied with the convenience provided by the service.

The starting point for traditional retailers is merchandise, but since the Company is both a retailer and service provider, its starting point is also services. It will offer Internet-related services, mainly for devices, thereby building relations with its customers.

The Company generates profits in three ways: firstly, selling products; secondly, through technical fees for product repairs; and third, from monthly fees paid by members who receive ongoing support from the Company. The core of the Company's business in particular is the support fees paid by its premium members, making it unique in the retail industry.

The Company considers its corporate social responsibility (CSR) to lower the digital divide in society. To a certain extent, a digital divide arises between people who can use information and

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communication technologies, and those who cannot. It is not good for society as a whole when people who cannot use these technologies find themselves at a disadvantage. The Company intends to contribute to more convenient and enjoyable daily lives for these lives by supporting them in making the most of IT services. This support service is being provided by PC DEPOT, with its stores acting as a base for such services.

Store development conditions

As of the end of Sept. 2017	(Stores)			Total
	PC DEPOT Large suburban-type stores	Smart Life stores Medium and small stores in metropolitan areas	PC Clinics Counters established as concessions inside consumer electronics superstores	
Directly-managed	18	37	53	108
Subsidiaries	12	1	5	18
FC	3			
Total	33	38	58	129

NOTE: Smart Life stores represent PC DEPOT Smart Life Partner (SLP) stores.

Subsidiaries represent PC DEPOT Stores (Kyushu, Chubu, Shikoku, Shinetsu and Tohoku regions).

PC Clinics represent counters established as concessions inside consumer electronics superstores, and FC represents franchise stores.

Business starts with personal computers

President Nojima (age 58) used to work at Nojima, a consumer product mass retailer (Code No. 7419, listed on the first section of the TSE). The eldest son of Nojima Co.'s founder is currently president of that company, while Takahisa Nojima, his brother, is president of PC DEPOT. He was in charge of supervising stores and merchandise at Nojima Co., but once personal computers began to become popular, he decided to set out on his own and established an independent business. While Nojima is still one of the shareholders of Nojima Co., there is no business relationship between that company and PC DEPOT.

Nojima was 34 years old when he started his business, which is now in its 24th year. In the early days after the founding of his business, many people wanted to own their own desktop or notebook computer, but such hardware was still beyond their reach. In those days, only a limited number of people went all the way to Akihabara, a Tokyo district famous for consumer electronics and Japanese sub-culture, to buy their personal computers. In contrast, Nojima went into business selling PCs in the same way that retailers in general deal with new merchandise. Company business performance steadily improved and in 1999 some five years after its establishment, it became listed on JASDAQ.

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Subsequently, the Company was promoted to the first section of the TSE in November 2015.

As the Internet era emerged in 2000, the Company entered into a new phase. At the time it was listed, it operated about a dozen stores with net sales of 15 billion yen, ordinary income of 800 million yen, and no debt.

At present, desktops, notebooks and related products are commonly sold at consumer electronics superstores. Also, there is a wide variety of specialist computer superstores. When viewed in the broad sense of consumer electronics and computer superstore sectors, the Company ranks in a low position in terms of size, yet is competing on a different playing field to its rivals. The Company is not directly competing with the biggest companies such as Yamada Denki, Edion, and K's Denki, but is differentiating itself from these companies.

Converting franchises to directly-managed stores

When developing its PC DEPOT stores, which are comprehensive specialist computer retailers, the Company allowed K's Denki stores, which are operated by K'S HOLDINGS CORPORATION (Code No. 8282), to become PC DEPOT franchisees. K's Denki was the second PC DEPOT franchisee. It was a beneficial move for both companies in that a consumer electronics superstore began to deal with PCs.

The Company does business in cooperation with K's Denki because, according to Takahisa Nojima, the management concepts of the two companies are quite similar and he felt much empathy with Shuichi Kato, Chairman of K'S HOLDINGS CORPORATION. The Company focuses basically on being a chain store operation that is easy for customers to use, for example by offering self-service sales aside from parts and offering discounts for paying cash instead of points cards.

From the very start, Mr Max Co. (who run general discount stores) and Kitamura Co. (specializing in cameras) also became PC DEPOT franchisees. However, as major operators became dominant in the consumer product mass retailer format, general discount stores found it difficult to sell PCs. The FC stores of Mr Max Co. were bought by the Company and became its subsidiary (currently, PC DEPOT Stores) by 2010.

Aside from PC DEPOT franchises, PC DEPOT PC Clinics which are franchise outlets providing technical services which were established as concessions inside consumer electronics superstores. PC Clinics successfully operated in many of K's Denki stores, and the franchise was then expanded.

As of the end of September 2017, there are 55 directly-managed PC DEPOT stores (including 37 Smart Life stores), 13 stores outside the Kanto region run by the PC DEPOT Stores Co., Ltd. subsidiary (including 1 Smart Life store), and 3 franchise stores, for a total of 71 stores. In addition, there are 53 directly-managed PC Clinics, 5 stores run by the PC DEPOT Stores Co., Ltd. subsidiary.

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As such, the Company currently operates 129 stores.

PC Clinic was operated mainly by FC stores until seven years ago, but the Company transformed the FC stores to directly-managed stores. The Company and K's Denki agreed that direct management would be more effective for enhancing service functions of the stores, and so the Company acquired these franchised stores. Currently, the Company operates directly managed PC Clinics inside K's Denki stores.

Ongoing Web business

EJWORKS Co. (ejworks), a PC DEPOT subsidiary is engaged in the IT solution business and has lines of business that include providing internet services and Web content creation. The Internet services market started from around 2000. However, this market has since matured, and a process of survival by natural selection has begun among Internet service providers. The Company is acquiring small-to-midsize providers and working to maintain their customer-oriented services. Customers will experience a seamless transition since they would keep their original email addresses.

Moreover, the Company has recently been utilizing this subsidiary as a support team for its content development and has come to attach more importance to it. The idea is to position it as a new support base for development.

The Company has made use of part-time workers, and it has hired some of them as regular employees.

In April, 70 new graduates joined the Company. The retention rate of employees is high, while the turnover rate is low. As of the end of September 2017, in addition to 815 regular employees, 1,183 part-timers (on an 8-hour shift basis) were working for the Company. Ten categories of tasks are assigned including operations (cashiers and baggers), attending to customers (customer-service personnel), Smart Life Partner (SLP, customer-service personnel), clinic services (preventative and recovery services) and quality improvement; workers are trained to handle the basic tasks involved in one category within one week. They carry walkie-talkies with them in the store in order to help each other by sharing information, which allows them to ensure a high level of customer satisfaction. Many part-time workers have been working for the Company for years, and each year roughly 60 to 70 workers change their status from part time to full time.

Complying with corporate governance: Review of outside directors

Two outside directors resigned under a resolution approved by the general meeting of shareholders held in June 2017 since they had completed the maximum term of eight years prescribed in the

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Company's by-laws. As a result, there are now two outside directors at the Company. The Company is complying with corporate governance as a company with auditors. Mr. Mineo Fukuda, an outside director successively filled the post of director at Recruit Holdings Co., Ltd., KADOKAWA CORPORATION, and Jupiter Telecommunications Co., Ltd. He has extensive experience in the media industry. Mr. Yoshinari Noguchi, an auditor, has long experience in internal audits at Oracle Corporation.

The general meeting of shareholders in June 2017 was held approximately one week later than usual and had between 70 and 80 participants, almost twice that of usual meetings. The number of new shareholders increased, and the Company received more questions than usual such as questions relating to recurrence prevention measures and a request for more precise explanations.

Three topics of discussion were as follows: the appointment of 10 directors, the appointment of an auditor, and the appointment of an accounting auditor. As an audited company, 10 directors (including two outside directors) were reappointed, and Mr. Koji Suzuki assumed the position of corporate auditor. Mr. Suzuki is an entrepreneur who served as Representative Director at Sony Marketing Inc.

The accounting auditor was changed from Ernst & Young ShinNihon LLC to Shinsoh Audit Corporation. Shinsoh Audit Corporation is involved in auditing services at 48 companies, including those listed on the First Section of the TSE.

The reasons for changing the accounting auditor are as follows: (1) An audit corporation was chosen to conclude a new agreement since the term of the current agreement has expired. Shinsoh Audit Corporation was selected considering its size, ability to perform tasks, independence, and internal management, (2) although there were no disagreements with the previous accounting auditor regarding a recent series of corrections that have been made to financial data, conducting a series of auditing procedures put heavy strain on both the Company and the accounting auditor, and (3) based on the above the Company comprehensively decided to establish a relationship of trust with a new accounting auditor.

Most directors who execute business are in their 40s, indicating that management talent has developed. President Nojima established this Company after leaving Nojima Corporation. Regarding the operation of the company, the president is aiming to implement business management suitable to fulfill the need for PC DEPOT to continuously develop in the rapidly-changing IT industry as a public company.

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2. Strength: Profit structure changed into one where services also generate revenue

Specializing in PC-related technical services, keeping the lead position in the industry

The Company is strong in Japan's Kanto region and covers 90% of the population there. Consumers who want to make use of PC DEPOT support services will find there is one within reasonable travel distance. Consumers who buy a desktop or notebook can have a Wi-Fi router set up for them at the store, and can start using their new computer as soon as they get home simply by plugging it in. This saves them from having to do the initial setup themselves. Smartphones also can connect to these Wi-Fi routers. If customers have a problem, they can call the Company's call center and get immediate attention. Users can obtain all these services just by paying a monthly fee.

The Company leads the industry in PC repairs and maintenance services. Moreover, the revenue generated by these services has been growing in double digits annually and as such is demonstrating rapid growth. Although the Company is a middle-standing company in the industry in terms of the number of PCs sold, it has unique service characteristics.

Over last 10 years, while PC DEPOT gradually shifted its business to services, the Company ran into difficulties in 2011 and 2012 when it opened five large conventional-type stores. The earnings fell around this time, and the balance of interest-bearing debt grew to over 7 billion yen.

The Company has achieved a unique presence among its competition with mass home electronics retailers. It has survived well against local competition as a computer specialist although it could not compete against major companies in terms of total sales volume. Under these circumstances, the Company did not overextend itself when opening new stores. It did decide however to become a customer-orientated IT solutions company, by striving to improve its services instead of increasing the sales volume for desktops, notebooks and other hardware. The Company markedly changed its tack to follow this direction in 2005. This was the second turning point for the Company since it was founded.

Providing solutions in combination with various services is the key to success. The Company provides telecommunication services using SoftBank's network (former Y-MOBILE's) as a Mobile Visual Network Operator (MVNO). It also provides fiber-optic network services as a fixed virtual network operator (FVNO). Moreover, when members subscribe to the Company's premium services, they can get any support they need: maintenance, call-center services, anti-virus support, and a "full installation" service when customers replace old PCs.

One of the Company's strengths is this lineup of original services it has developed and runs. No other PC shop is capable of delivering technical services especially data recovery, as speedily as PC DEPOT.

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The Company set its transformation into a store that specializes in services as a part of its policy objectives and has strengthened its commitment to this policy as it entered the Internet era. The Company has also emphasized the sale of store brand products under the name "OZZIO." However, although OZZIO accessories and supplies are highly profitable compared with its other retail lines, the Company is moving further toward providing customers with services.

Trend in constituent ratios of sales Accessories

(% , millions of yen)

	2009.3		2011.3	2013.3	2015.3	2016.3	2017.3	
	Sales	Constituent ratios	Constituent ratios	Constituent ratios	Constituent ratios	Constituent ratios	Constituent ratios	Sales
Goods sales	35572	82.4	75.8	69.0	58.8	49.7	43.4	20099
PC and peripherals	24375	58.5	52.0	46.4	33.7	25.3	23.5	10885
Accessories, supplies, and software	6554	14.6	13.9	12.1	8.5	7.6	6.7	2644
Used items and others	4643	9.3	9.9	10.5	16.6	16.8	14.2	6569
Service sales	11340	17.6	24.2	31.0	41.2	50.3	56.6	26317
Sales from solution services	8726	10.3	18.6	27.3	38.3	47.6	53.7	24984
Royalties and other revenue (FC)	522	1.3	1.1	0.3	0.3	0.2	0.2	75
Internet-related businesses	2090	6.0	4.5	3.4	2.6	2.4	2.7	1258
Total	46912	100.0	100.0	100.0	100.0	100.0	100.0	46417

Note: Sales from solution services include sales of service inclusive products and technical services/fees.

Sales by FCs on which royalties are payable amount to 1,330 million yen in the term ended March 2017.

Unique business model with premium services as its source of income

The Company's solution services consist of three categories of services. The first is the PC Clinic which provides installation along with repair and replacement services. Support for solution services are provided at all stores and is managed by about 1,000 employees.

The second is premium services which solve problems customers are having. The services cover: (1) any type of product; (2) products regardless of how old they are; and (3) products purchased at the stores of other companies. The premium services are separated into six major service plans. The third is solution services which combine content and communication. By subscribing to these services, customers can read digital magazines on their iPad or receive full support for low-priced smartphones. All services are backed up in the cloud (automatic data storage), providing sufficient capability to cope with defective hardware or security issues.

The Company's business model is quite unique, even when compared to companies outside of Japan. The model consists of product sales, service sales, its operation as an MVNO, and other areas. Members enter into a three-year premium service contract. The company bears the cost of support up front, and then recovers it from the fees paid by members.

Customers would like to use the PCs, tablets or other devices they have bought as soon as they get

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home. Takahisa Nojima remembers what that feels like. If after buying a PC for example, a user takes 3 hours to do things such as create a recovery disc, set up anti-virus software, configure the initial settings and set a password, and then comes to a dead end, he or she will be stuck without some help. PC DEPOT's premium services are solutions to help such users over the Internet.

Suppose a customer brings their old computer and member card to a PC DEPOT store, and buys a new one. The store's service personnel will then carry out all the necessary software installations for the customer onto that customer's new computer. The customer takes the new PC home, and is able to use it immediately in the same way as the old one, via the PC DEPOT-branded wireless router, without having to do anything in particular. This is total convenience.

A patent for the Company's router's systems was registered in March 2012. The packages are also cloud-capable. The Company has gradually been expanding and improving these services. PC DEPOT's business model, which generates revenue from service sales, was brought fully into operation in November 2005 and has been steadily expanded since. Conventionally, various technical services such as installing additional memory have been provided for a price. Today, however, when a fixed month fee is paid, a wireless router is leased to enable the consumers to use high-speed internet service with the purchase of just a PC alone.

As mentioned above, PC DEPOT also is an MVNO. An MVNO does not have its own mobile communication network, but provides services under its own brand by renting network space from major carriers. The Company provides services to customers as a telecommunications carrier, rather than acting as an agent for other carriers in exchange for incentives. This makes it possible to provide services that customers may want in a single package and makes for a very convenient premium service.

PC Clinic can readily be used as a one-time-only technical service. Making customers into premium service users is a better strategy in order to retain them as members to whom ongoing services can be provided over a long period time. In addition, PC DEPOT's direct running of PC Clinics facilitates the agile management of PC Clinics. That is why the Company changed its policy and began directly managing PC Clinics.

A mechanism that is impossible for others to copy

The business model at PC DEPOT is unique, and competitors have started to open stores similar to Smart Life stores. Since these competitors have not yet established a system or trained employees to provide premium services at the same level as the Company, the competition has not really become serious.

The Company is a retail service company for personal devices that provides solution services under

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a membership system. With no other companies pursuing a solution-service-based business model in the same manner as the Company does, the Company is building up to become the one and only business of its type.

Even if another company tried to provide such services, it would be extremely difficult to (1) train the personnel required for technical services, (2) tolerate a decline in profits in the early stages due to the shift to a service income type business, and (3) provide an extensive service menu from now onwards. We can therefore say that the Company's superiority over its rivals is significant.

Service income tends to increase in accordance with new PC sales. Moreover, service income has increased rapidly along with increasing sales of smartphones and tablets. Most individual own not only one device but rather multiple devices. Also, families own multiple devices. Needs for dependable services rise according to the number of devices owned, which makes it easier for the Company to have such users as regular customers.

The Company provides services by assigning experts in each service category and having them work as a single team. It has spent more than 10 years developing this system, which has become a business model that constitutes part of its corporate culture.

Convenient services — "Just Show up and Buy a New PC"

Up until now, people have visited PC DEPOT only when they need something related to PCs; however they now visit PC DEPOT for almost any type of Internet devices, including smartphones, tablets, printers, and fax machines.

Under such conditions, the key is the cloud. The Company has launched full-fledged "Comprehensive Cloud Services." Now that stable server operation has been secured, the Company will currently be able to provide new services from here onwards.

One of the typical new services is "Just Show up and Buy a New PC." The Company provides its premium members with an automatic data backup service for Internet devices such as PCs and backup data reproduction services at store counters using a patent-pending proprietary comprehensive cloud system.

Since data on PCs are backed up, when you buy a new PC, you don't need to bring your own PC to the store to take data from it. Customers can have their new PCs ready for use with no hassles since the general mirroring service (backup of the same data on the cloud) provided by the Company allows them to save the data from their PCs onto the cloud. Their smartphone data is also saved on the cloud via PCs. Investments in such services are not big investments compared to that involved in the creation of a new store so the Company can gradually expand this service.

It will prove difficult for other companies to offer the same service. The Company has enhanced the

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PC Clinic functions at its stores. It has trained and developed engineers with expertise in PCs, smartphones, and the Internet. The Company has already thus created a mechanism through which it can make profits. Even if mass home electronics retailers try to imitate its model, it is difficult for them to develop the same functions by deploying such personnel at their stores.

Specialist services are needed even with the reinvention of Internet devices

The position of leading player in personal communications has shifted from personal computers to smartphones. Cloud systems will become the main infrastructure. Computers used to be at the core of the internet, but are now giving way to net devices embedded in appliances, cars and homes, making them useable anywhere. Software is required to control such functions, and services are also required to make full use of this software. The Company is committed to providing these services, and has set as its objective the adopting of a strategy to expand its business to cover Internet devices and not to limit its services merely to computer-oriented goals.

Further added value with FVNO

When customers who joined the service using FVNO switch over to the Company's fiber-optic network service, the communication fee listed as a service sale is 4,000 to 5,000 yen per month. While profit margins will be higher compared to conventional agency commissions, profit ratios for services will decrease.

FVNO services will also support fixed-line services. So far, the Company has provided services by attaching its Wi-Fi router to the ends of optical fiber lines, but now it has become possible to provide services including fixed optical lines.

The Company will have to compete with mobile phone shops of carriers. In the competition, each company will make the most of its characteristics. The Company will have existing members subscribe to FVNO services and make the advantages of the Company's unique services known to customers.

Smartphone with original support—JUST PRICE FON

- 5 models with contract period plans of 2 years and 3 years
- Smartphone (hardware), MVNO, and premium services are integrated.
- Two types of plans are available with monthly charges of 2,990yen and 3,990 yen.
- The charges include payment for smartphones and support fees.
- Additional fees are required for options such as a flat rate service for phone calls and a wireless LAN at home.

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Low-priced smartphones: premium service for smartphones is also provided

The Company is one of the retailers of mineo, Y!mobile and UQ mobile, and customers can also purchase the Company's original support service for smartphones for a monthly fee of 1,000 yen. Apart from that support service, the Company sells its original low-priced smartphones that come with its support services. There are two models at monthly charges of 2,990 yen and 3,990 yen with a three-year contract period. The Company expects that some new users will not know how to handle low-priced smartphones by themselves and will reach out to the Company for help.

Major carriers have unlocked smartphone SIMs. Up to now, the subscriber identity module (SIM) cards have been locked. In other words, the SIM card, which records information such as phone numbers that identify individuals, can only be used on particular mobile phones.

Overseas, any mobile phone can be used as one's own phone merely with the insertion of one's SIM card. In other words, if one has a SIM card, one can easily buy new smartphones. One may own two to three smartphones allowing their use for different purposes.

Premium services were added to PCs and premium services for smartphones are now provided on a full-scale. The Company started to sell Just Price Fon at the end of April 2016. This original smartphone sold by an MVNO comes with original support services. Presently, stores offer five models at monthly charges of 2,990 yen and 3,990 yen.

Demand for premium services especially for PCs is growing and the number of subscribers is increasing. One subscriber receives multiple services with the PC as the base unit. Nowadays it is common for one household to possess multiple PCs and smartphones.

Moreover, the needs for multiple support on a basis of smartphones without PCs are increasing. Some people have purchased low-priced smartphones at other mass home electronics retailers but found they could not use them easily. More and more of these people are visiting the Company stores for support. Just Price Fon is so to speak, a "moderately priced smartphone." This was released under the Company's own brand label. Hardware, software, and support are integrated into this service.

Smart Life stores are fashionable and convenient: Specialization in services

Smart Life stores display less merchandise than conventional stores. Smartphones and tablets now occupy more of the display shelves. The store format is based on the Company's new store concept, "providing services that customers need in a single package instead of simply selling products."

The variety of professional accessories in a store may not satisfy the needs of PC aficionados, but this poses no problems since customers can ask for an item at the store counter and the store will obtain it for them soon after. The name of the counter for responding to customers' needs (such as computer repairs) changed from PC Clinic to Dr. Smart, and staff members now wear a new uniform.

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People want to use the IT services they need immediately without having to deal with anything inconvenient. Tablets and other devices are provided with content services pre-installed and with all necessary configuration completed. This convenience allows customers to use their tablets with these services without having to do any cumbersome preparation. The customers neither need to configure the initial settings while staring at user guides nor do they have to call several call centers and ask for help.

The Company also advises customers on Internet connections and fees for each PC, smartphone and tablet that they are now using, thereby allowing them to lower the fees for all of their devices or to switch to more convenient service packages.

The "Smart Pack" billing plan is also coming into wide use, which includes a hardware device, software, and Internet connection in a single package. This package allows customers to use hardware, software and an Internet connection by simply paying a monthly fee instead of having to buy a hardware device and paying a monthly fee for the necessary software and Internet connection. Although this is a type of three-year loan of an amount determined by subtracting the product's estimated residual value at the end of the loan term from the product's sticker price, since customers are already familiar with the billing plans of Japanese cell phone carriers, which require a two-year subscription, they will find this system acceptable.

The Company has embarked on full-scale store innovation. The PC DEPOT logo includes the terms "Low Price" and "The Computer Superstore," and its image is that of a PC supermarket, but in some areas this image no longer reflects the reality. Therefore, these two terms were removed from the logo of the new stores.

Smart Life stores will not just sell products; they will create packages and provide customers with the solutions that they want. Their customers will become members who will use the services they offer over long periods of time. PC DEPOT's president, Takahisa Nojima, stressed that the approach for Smart Life stores will not be to simply display products and ask customers to choose the ones they like. Instead they will be offered a one-stop service to provide them with the Internet communications that they want. Consequently, the atmosphere at these stores will be different to that of conventional stores and customer counters will be placed centrally within them.

Inventories decrease in Smart Life stores. By helping free customers from the burden of choosing products and services themselves, the role of these stores will be to provide the services needed by customers, as a result reducing inventories. However, a fixed level of account receivables will accumulate on the balance sheet because the merchandise will be in the form of packages made up of hardware, software, and content with sales being collected in the form of monthly charges.

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Gaining service members by troubleshooting for our customers

In-store arrangements like those of Smart Life stores are found in Europe, but the Company's business model, which allows it to retain customers mainly through providing services, does not exist either in the West or in Asia.

The inspiration for this business model dated back more than 10 years. At first, the Company started by giving preference to customers who were not familiar with PCs. In those days, there was a perception that PC users were somehow a different "tribe" or subculture of people. President Nojima, however, aimed to make customers of people who were not skilled at using PCs. He tried to provide free help to people who were unable to use PCs easily and those who wanted to reset their frozen PCs.

Next, he gave priority to serving "people who have difficulties." He dug deep into the technical support business and made it a tool for differentiating his company from others. Thinking that it would be more convenient to receive service continually by paying monthly fees than paying fees every time a technical problem occurred, he launched a monthly fee system in 2006. Today, the service has been refined into a scheme that can provide services when users face any type of technical trouble. The convenience of the premium service has been enhanced as more women and families use PCs.

The Company has been committed to increasing the number of its premium members. Detailed data is collected and tracked for each area in order to maximize the number of customers who become premium members when for example, they buy a computer, visit to have a repair done, or replace their PC.

Premium members have been increasing at a very high rate. However, this does not make money in the short term. The Company needs to make an up-front investment for each router which takes a year to recoup from the monthly premium service fees. However, once the initial outlay has been covered, profit is generated at a fixed rate from the second year onward.

The sales of services are growing steadily. What this means in practice may be somewhat difficult to understand for people not directly involved however, the Company's policy is clear. Sales incentives like those given by manufacturers for product sales are included in product sales. Sales from premium services, repair, maintenance, and one-off service plans are classified as service sales.

3. Medium term business plan: Improvement in customer trust and a full rollout of member-service-inclusive products

Review of this year

Looking back on this year, President Nojima emphasizes the following two points: (1) The internal

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reform has been developed and established. Engineers in charge of repairs fully understand the stores, devices and services, and can also read customer behavior. On the other hand, due to productivity varying among the stores, it took time for the sales side of the Company to raise to a level of service to customers while increasing its added value; and (2) The responses of member customers have already returned to a calm state, and there are cases where the users who once cancelled the membership came back. In other words, the Company feels more confident that the number of customers will substantially increase if the Company can provide them with accurate advice on the services they really need.

Future management

The Company will focus on three points in future management. The first point is the work way reform, by which the Company has shortened business hours. The Company has shifted the closing time of the stores which used to stay open until 8 or 9 p.m. to around 7:30 p.m. While the customers come to our stores with problems, if we can quickly understand and respond to the problems, it will result in greater customer satisfaction and shortened waiting time. This will also prove effective in fostering a workforce. The training of new employees has been making progress and it is likely that they will soon become a substantial part of the workforce.

Secondly, the Company will focus on the importance of PCs in the educational market and make an effort to restore the role played by the PC. The Company will emphasize not only the smartphones but also the smooth connection to smartphones with the PCs as a base. On the other hand, low-priced smartphones are not the Company's main products and focusing on IoT is regarded as a little bit premature even if the use of IoT will eventually spread to homes.

Thirdly, the Company will make work creative and highly value-added through the development of new customers. While people seeking cheap products go to other shops, the Company will aim to attract customers to our stores for excellent services. Consultation on membership is increasing. General customers who are not the members of our services also visit our stores with their smartphones or PCs purchased at other shops when problems occur.

Further progress in review of member services: Making services appropriate for elderly people

Criticism spread on the Internet in last August concerning a contract made by an elderly person that did not seem to match his usage circumstances. The main point of contention was whether or not the cancellation charge imposed when the elderly person's son canceled the service, and the actual conditions of services received were appropriate.

Services for members have two aspects: one is the service provided by specialists when a piece of

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hardware breaks or software stops functioning because the user does not know what to do. Another is the service when a user feels that spending time on reading manuals and making inquiries by telephone is troublesome and would like to entrust these tasks to someone else, despite being able to perform them on their own. Both of these are maintenance-type services providing support when problems occur. However, this varies greatly between individuals.

Moreover, there is another type of service—services included with products purchased in installments. The Company calls these "service-inclusive products." Some subscribers can choose the purchase method. For example, a subscriber purchases a PC as a product from a single payment and not in installments. Smartphones are purchased in installments and not in a single payment which is common.

This would not have been necessary for an elderly person visiting the store who had subscribed to the Family Wide 10 Devices plan at that time. At that time, the elderly person would not have needed to pay 5,500 yen per month as the Single Plan for One Device costs 2,500 yen per month. But if a household only has one person but that person intends to use a PC, smartphone and tablet with Wi-Fi at home, it would require the Personal Plan for Three Devices, which costs 4,000 yen per month.

Cancellation charges vary depending on cases such as (1) cancellation within the first month of admission to membership, (2) cancellation after one year, and (3) cancellation after three years. The Company expects to collect payment based on the assumption that the customer is on a three-year installment payment plan. Therefore, when a contract period ends up being shorter than three years, customers are required to pay the outstanding amount of hardware in use. This is also the commonly used method.

The Company makes the policies on how to sell the services and what price to set on services. If a service does not meet customers' needs, that service will not sell. If unnecessary services are offered, customers can request to have those services removed.

Based on the writer's many years of experience in the financial industry, financial transactions with elderly people require meticulous care. Even though elderly people agree on conditions at the time of contract signing, they sometimes claim that they have never been informed of certain items. In the IT industry in this case, the incident was considered to go against the essence of the service, which is to provide support for digitally illiterate users. For this reason, the case came under criticism.

Continued to respond promptly

President Nojima took the criticism to heart and implemented four measures. First, a department specializing in quality management was established and an officer in charge was appointed. Secondly, to introduce an external point of view for service development, the Company is adopting ideas from

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consumer advisers. Thirdly, improving customer satisfaction is being emphasized more in the in-house employee performance evaluation system. Finally, as part of an enhancement of risk management, the Company involved experts to strengthen governance. The Company announced that it will make every possible effort to contribute to society as an IT solution store by implementing these reform measures.

In November 2016, the Quality Management Department was established. While the existing Sales Department tends to focus on sales management, the Quality Management Department monitors the quality of the products and services provided to customers to make sure that they are customer-first services.

The Company implemented measures to promote the improvement of premium service contracts.

(1) If a contract is seen as inappropriate at that time for usage by any of the roughly 400,000 service subscribers, the Company will allow making changes to the plan or will allow cancelling contracts at no charge provided that the customer returns the devices that were provided.

(2) In the past, when customers aged 75 or older subscribed to a new service, changes in plans and the cancellation of contracts were free of charge if made within the first month. The Company changed this practice and today when customers aged 70 or older subscribe to a service: (i) the Company checks with a family member or a third party; and (ii) changes in plans and the cancellation of contracts are free of charge for the first three months.

(3) For new subscribers aged 75 or older, the Company will accept changes in plans and the cancellation of contracts for free regardless of the time of the subscription. The main point is that the Company will check with a family member or a third party when any elderly people aged 70 or older subscribe to a new service.

Moreover, the Company: (1) assessed and confirmed customer service usage situations through direct mail and calls to all members; (2) set up counters for members to exclusively use at stores to provide explanations and information, as well as to confirm the details face-to-face; and (3) assigned new quality management staff for the premium service at stores and created a system to double check contracts, independently from confirmation by store staff. The Company has assigned 100 quality management staff at stores for the above. These actions have been taken at full swing since September 2016.

A series of these actions has been developed and is being established. The Company has entered a phase where the new business model can be used normally.

Not easily influenced by the sales volume of PCs, tablets and smartphones

The Company will learn from this case (inappropriate services contrary to customer needs) and will focus on store operations and personnel training in the next one to two years.

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The market for PCs, tablets, and smartphones is saturated, and sales volumes are expected to decrease. However, demand for the Company's services has been increasing and has been barely affected by the sluggish sales volume in the market.

Changes constantly occur in the industry such as the launch of new products and services, and the termination of existing services. As a result, more customers seek support since they cannot master the use peripherals and software as well as PCs, smartphones, and tablets. Since the Company's services are not available in many people's neighborhoods, the Company should be able to acquire new customers by opening new stores.

One issue is how best to provide services to customers. In the Company business model, stores solve the difficulties customers are facing and earn revenue in the long run by providing solution services. The time required to serve each customer becomes longer with good customer service. Higher customer satisfaction will result from a good relationship between the stores and customers. Quick customer throughput is not the priority.

Opening a large number of Smart Life stores by renovating existing ones

The Company continues to open new Smart Life stores by renovating and reopening existing stores. The Company will also open new stores, with more focus on central Tokyo than in the case for current stores.

Smart Life stores transformed from existing PC DEPOT stores already have a certain level of recognition and regular customers. The key to their success is how many new service-oriented customers they can acquire. Smart Life stores can be set up even if the location is less than favorable. As the service grows, and the percentage of total sales that it represents increases, profitability will further improve as a result.

Costs for renovation are lower than those for opening new stores. Moreover, a marked impact can be noted. Comparing the situations before and after renovation, the profitability of renovated stores is about 20% higher than that of existing ones. The expenditures required to open a new store with an area of 400 to 500 *tsubo* could be used for the renovation of four stores each with an area of 300 *tsubo*. Furthermore, the probability of recouping investments is higher, and the returns are also higher. Therefore, such moves are given first priority.

On the other hand, there remains considerable room for new Smart Life store openings. As a new-type store with emphasis placed on providing services, we estimate there are approximately 200 locations where these stores could be opened. The Company will first open stores primarily in the Kanto region to enhance its brand power through providing community-based services. The Company reckons that it requires 100 to 200 *tsubo* of land in Tokyo's 23 wards and 200 to 300 *tsubo* of land in

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the greater Tokyo area if it plans to effectively open a Smart Life store in a vacant space.

Store development history of PC DEPOT

Number of stores at the end of each term	(Stores)											
	1995.3	2000.3	2005.3	2010.3	2011.3	2012.3	2013.3	2014.3	2015.3	2016.3	2017.3	2017.9
PC DEPOT												
Directly managed	1	10	28	43	44	48	50	46	36	28	23	18
Smart Life store								4	15	25	31	37
Subsidiaries				4	4	12	11	11	13	13	13	12
Smart Life store												1
FC		8	32	17	17	5	5	5	3	3	3	3
PC DEPOT PC Clinics												
Directly managed					30	46	49	49	52	52	53	53
Subsidiaries						1	1	1	0	5	5	5
FC				24	6	7	7	7	6	1	0	0
Total	1	18	60	88	101	119	123	123	125	127	128	129

New Smart Life store openings: Central Tokyo

The Setagaya-Kinuta Store was the first new Smart Life store. Customers are now steadily increasing there. Many customers are bringing in hardware purchased from other companies for repairs, thus increasing the store's customer base. This store was launched on a full-fledged basis in March 2016 and the Company invested around 400 million yen in this store opening due to its wide floor space of 990 square meters. However, this is an exceptional case. The Company usually invests roughly 200 million yen in stores with a floor space of 330 to 495 square meters, and roughly 40 million yen in stores that have all their fixtures and furnishings.

Since this is the first new Smart Life store, the store does not have any existing customers. It did not attempt to attract customers with product sales as traditional PC DEPOT stores do. Instead, first the store encourages customers to visit and then it attempts to gain their acceptance by providing them with services in which they can readily seek advice if they encounter any problems. It takes some time for the store to build up its popularity; however, customers will start relying on the store when they have difficulties with their smartphones, PCs, and tablets. Local residents will also appreciate having such a store located in Setagaya.

Many people want the solution services provided by PC DEPOT. The Company launched the Aoyama Store in December 2015 and the Azabu-Juban Store in March 2016 as city-center stores in Tokyo. These stores target new customers living in central Tokyo. Customers visiting the Aoyama Store live in the neighborhood. More female customers than expected are visiting the store. The number of customers is increasing and a generation of people somewhat younger than seniors is

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visiting the store.

The Aoyama Store is located on the first floor of the new Aoyama Quartz Tower (a comprehensive medical facility). The store will occupy two floors with an area of 231 square meters. This will be a new small-sized SLP store and the first store within the circle of the Yamanote Line. The Company has been building up a base of members by targeting people living within a two-kilometer radius of the store. The Aoyama Store is located in a premium location along a main street. Company President Nojima believes that the Aoyama Store will be a symbol of the Smart Life store, and other stores to be opened in central Tokyo will not need to be situated along a main street if people living within one to two kilometers can locate it easily.

Located in central Tokyo, this store will provide high-quality services and support fitting the area. The store also expects people visiting central Tokyo to visit Smart Life store in Aoyama to learn about its excellent services and entice them into local Smart Life store visits.

City-center small type stores and acquiring regular customers

Types of stores launched can be categorized as Version 0 (V0), Version 1 (V1), and Version 2 (V2). An example of V0 is the Azabu-Juban Store, which is a very small store. This store focuses on services, and product lineups are limited. Even so, the store will be moderately successful due to its location close to the station. An example of V1 is the Himonya Store which is a little larger and has more product lineups. The Company will start more aggressive operations in the city center with these V0 and V1 type stores. Large stores are categorized into V2, and the Inagi-Wakabadai Store is now operating on a test basis. Once the Company is confident of business prospects for large stores shifting to Smart Life stores, demand for services will further increase. The Company will open new stores in central Tokyo, focusing on five urban districts: Shinjuku-ku, Shibuya-ku, Chuo-ku, Chiyoda-ku, and Shinagawa-ku.

The Company launched the new Smart Life Roppongi Store in July 2017. This is the fourth store following the Aoyama, Azabu-Juban, and Lalaport Toyosu Stores in Tokyo's 23 wards. The store is a city-center super-small type Version 0 (V0) store, the same type as the Azabu-Juban store.

Since new Smart Life stores do not have existing customers, gaining store recognition is of utmost importance. Moreover, these stores do not display low-priced merchandise, unlike regular mass home appliance retailers. The leaflets distributed in Roppongi introduced some of the store's features to customers, such as (1) a new-style comprehensive specialty store, (2) a store that provides sales, repair, and Internet services, and (3) a store that assists local customers in using their PCs and smartphones with enjoyment.

President Nojima uses the words "Please drop by" and "We will assist your smart IT life." The

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launch went as expected and will gradually continue to attract customers.

The ongoing shift to Smart Life stores has been extended to large-scale stores

The Tama New Town Store was renovated in June 2016. It was renewed from a large-scale store with a floor space of 600 *tsubo* into a Smart Life store with a floor space of 300 *tsubo*, with the remaining space being subleased to other company. The company also commenced to transform the stores run by the PC DEPOT Stores Co., Ltd. into Smart Life stores. The Nagano Store was renewed in September 2016.

Large PC DEPOT stores with services provided at Smart Life stores are Smart by Solutions. This type of store was first opened in September 2014 and has been implemented at traditional directly-managed stores since the end of September 2017.

The Company introduced Smart by Solutions (S×S) at the Tomisato-Interchange Store in Chiba. The company also started transforming the stores with orange signboard that is used by the PC DEPOT Stores Co., Ltd. into Smart Life stores. This store has been installed with counters similar to that in Smart Life stores which has the blue signboard of large conventional stores and not that of Smart Life stores. Large PC DEPOT stores are renovated with a Smart Counter installed inside just as done in Smart Life stores.

New store openings and shift to Smart Life stores

	2014.3	2015.3	2016.3	2017.3	2018.3 (forecast)	2019.3 (forecast)	2020.3 (forecast)
PC DEPOT stores							
Directly managed・Subsidiaries		3					
Smart Life store (new)		1	3	2	1	3	4
Smart Life store (renovated)	4	10	7	5	9	7	7
PC Clinics							
Directly managed		2		1			
Total	4	16	10	8	10	10	11

NOTE: Forecasts by an analyst are marked (forecast).

Future store development

The transformation to Smart Life stores amounted to 38 stores and traditional PC DEPOT stores amounted to 30 stores. These stores are also expected to be transformed into Smart Life stores and the renovation program will last for at least three years.

New stores in central Tokyo will need more time to make a profit. 1) Since these stores do not have existing customers, it will be necessary to increase the members over time. 2) The number of users and the level of recognition will increase in a two-year period. 3) Therefore, the Company intends to

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carefully expand its business with the approach of opening a new store when an attractive property has become available.

The renovated stores have a completely new store image, which shows itself in its relationship with customers. There is now more time to listen to customer requests through face-to-face communication since the new stores are not meant for selling products. More families, couples and groups with women will visit the stores. The Company wants people visiting the stores to become regular and long-time customers as the SLP stores offer new type of relationship with them. Renovation per store costs between 70 to 100 million yen and stores under renovation will be closed for about a month and a half. PC Clinics are an exception and will continue operating to provide repair services. The renovation program will last at least three years, assuming that seven stores are renewed each year.

The Company will gradually open new stores. The Company can afford to launch two to four stores per year and could accelerate the pace of launch in the future.

Service menus of PC Clinics (examples)

		(yen)	
		Member	General
Service	12 tickets for quick lectures	5000	30000
Setting-up	Windows Updates	0	6000
	Creating recovery media for customer PCs	6000	8000
	Solving printer problems	500	3000
	Installing additional memory/replacing memory	1000	3000
Security measures	Deleting spyware	0	5000

NOTE: "Member" refers to a service member of PC DEPOT; "General" refers to others. Consumption tax is not included.

Responding to service demand: Renewing the menu for premium services to make it easier to understand

The Company changed all menus for membership services to make the selection process easier. The menu for premium services was renewed in February 2017, where the plans are offered according to the usage situation rather than the number of devices owned, which was how the previous service plans were based.

The plans include: 1) PC plan with a monthly fee of 2,500 yen (Internet connection to be setup by the member), 2) Home network plan with a monthly fee of 3,500 yen (home Wi-Fi), 3) Multi-network plan with a monthly fee of 4,500 yen (at home and outside), and 4) Smartphone plan with a monthly

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fee of 1,000 yen.

Customers receive various services. Therefore, it is not appropriate to consider the Company's service fee income by looking at the number of members multiplied by the average membership fee. Some customers visit stores for repairs, others for specific services. Some customers subscribe to premium services and once they have received the Company's services, they come to realize that being maintenance-free is advantageous and that additional services will also be useful. More customers will use the cloud service. What is going to happen next? As the quality of services is improved, customers will be upgraded.

The Company plans to steadily expand service lineups and shift to prices corresponding to service expansion. The focus is shifting to improved software with increased security and improved usability with increased router speed.

In March 2015, the Company launched a member support system, called JIMAS, which comprehensively increases the efficiency of services. (JIMAS stands for Jitaku (home) Internet device Multi-Assistant System). Customers are invited to join the service with a device management system. Under this service, the condition of certain devices is constantly monitored with a dedicated application installed on the device. If a device is lost, it can be locked remotely. These services allow the Company to manage digital information and store it as customer records. Using these records, customer service can be further enhanced.

Premium service

(yen/month)

Plan (From February 2017)	3 year plan Monthly fee	2 year plan Monthly fee	1 year plan Monthly fee	Usage environment
PC plan	2500	—	3300	Internet connection to be setup by the member
Home network plan	3500	—	4800	Home Wi-Fi Support for up to 5 devices
Multi-network plan	4500	—	5800	At home and outside With smartphone support Support for up to 5 devices
Assembled PC plan	3000	—	4300	Support for assembled PC
Smartphone plan	—	1000	—	Data support
Mobile Internet plan	7000	—	—	Mobile wireless support Includes mobile Support for up to 5 devices

NOTE: Initial administration fee is 5,000 yen (3,000 yen for smartphones). The monthly fees are subtracted on pro-rata basis in the event of cancellation during the contract period.

Simultaneous release of "Member-service-inclusive products" on September 22

Service-inclusive products are now referred to as "Member-service-inclusive products" to clarify

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the concept. In other words, this means that a customer can purchase service-inclusive products only after becoming a member of the Company's program.

Of course, it is possible for a customer to purchase just products only. The customer may also select an appropriate service from various service menus. However, the Company will strive to improve the mechanism that attracts members for a long time, by further meeting customers' needs and increasing customer satisfaction through services and products combined together.

The Company launched member-service-inclusive products in September. Since the Company will increase the line of products from now on, sales from solution services in the second half of the current term are expected to increase year-over-year. The sales from solution services in October have already shown an increase of 1.2% year-over-year since last July.

However, these service-inclusive products will start contributing to earnings with a slight time lag. These products have a mechanism similar to four-year installment sales, where the Company puts much effort at the time of selling and offers various services. Since the cost will be collected as part of the monthly service fees, these products will start contributing to earnings after six months or one year.

(1) Value Pack provides the multi-network plan of premium services (4,500 yen per month) with the Apple's MacBook Air (13 inch, 128 GB) for a monthly fee of 5,500 yen. On the iPhone, it is possible to share images and data via MacBook. MacBook's data allows a smooth transition from iPhone 7 to iPhone X.

(2) The Company has launched the "Membership Solution Hardware Plan" available for both existing members and new customers. This Plan allows users to use devices such as iPhone8 in addition to a series of premium services. For example, by combining multi-network plan with iPhone 8, the user can use network services for a monthly fee of 2,000 yen (under a four-year plan) after paying 20,000 yen for the phone at the time of purchase. As usability will be improved by connecting iPhone and MacBook, the Company will promote the sale in such combination.

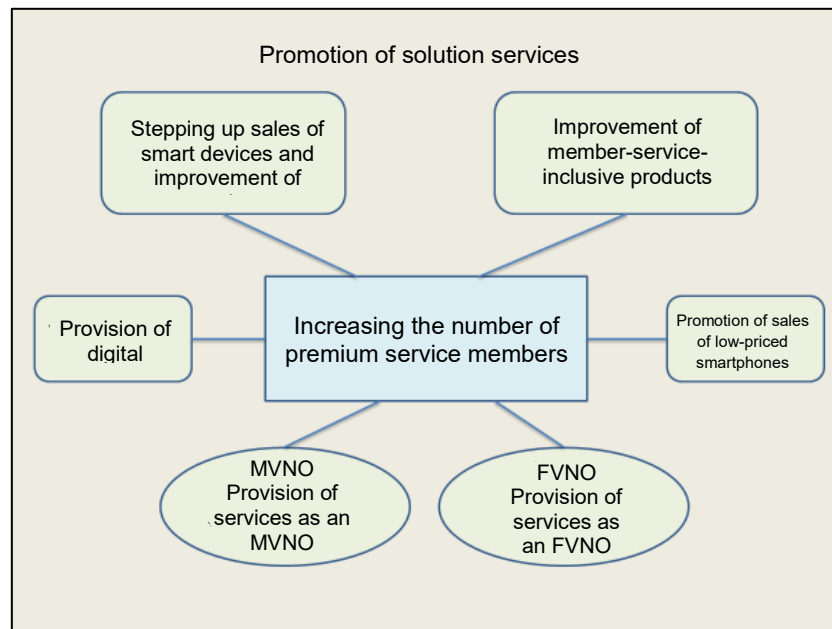
(3) When members subscribe to the Company's premium services, they can use iPad 2017 (9.7 inch, 32 GB) for a monthly fee of 1,000 yen. Similar services will be launched in the future.

Member-service-inclusive products as mentioned in (1) above will collect the cost over a four-year contract period. Since the need for replacement by new products arise after two or three years, there is a high possibility of entering into a new contract within four years.

Service-inclusive products are selling well. Performance has hit bottom in the first half of the current term, and is expected to improve from the second half, initially at a slightly slow rate and then accelerate from the second half of the next term. Service-inclusive products at one point increased to account for 15% of sales from solution services. The proportion of sales from solution services is

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expected to gradually increase to 5% and 10% of the total.



Various support is available for IoT and AI

Smart speakers are regarded as premature so far. Although this is currently a hot topic, the Company intends to observe the enhancement of functions and sales pace for a while before adding them to its service menu.

In the medium-term, the 5G network services will start in 2020. There will be various new movements such as the programming education to be required at elementary schools and digital textbooks to be implemented. While smartphones are becoming the mainstream, there is still demand for PCs and sufficient reasons to use the PC at home.

The new devices and services of IoT and AI will rapidly spread to homes. President Nojima believes that the base of the technology is in PCs. To put it more plainly, he believes that the area where the Company's engineers and support teams play an active role will expand rapidly.

If IoT devices start to be used in various areas including watches, healthcare, and residential gateways, their services will be needed. For instance, when a customer buys a smartwatch, that person can choose from several options, such as buying the unit alone for 50,000 yen, or paying a monthly fee that includes having full settings made to connect with smartphones, and after-sales maintenance.

The Company is developing services, one after another including a device lock in case of loss of the device, smartphone data automatic storage in the cloud, and backup systems that connect

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smartphones, PCs and the cloud in a system. Patent applications have also been made.

To make full use of IoT, there will be a variety of service-inclusive products with a monthly-fee membership, like Premium Service Solution & Things. Use of devices such as smartphones expands new connectivity in areas including healthcare, wearable computing and networks, security, entertainment and content, and lead to development of new uses. Contract details including liability exemptions are expected to change.

The Company will pursue IoT for personal use while maintaining PCs as a platform. Companies such as Google Inc., Apple Inc., and Amazon.com, Inc. will begin providing new services. Robots will be used in homes. Regardless of circumstances, the introduction of a new network will require new support. This is the Company's raison d'être in specialized areas.

From the term ended March 2016, "technical services/fees" changed to "solution service sales" due to an increase in sales of products that integrate hardware and software services. Another reason for the change is an increase in services with printers, iPads, and fiber-optic networks.

In new solution services, accounts receivable from sales including service fees are on the increase.

In Smart Life-based businesses, it takes three to four years to collect the full amount of revenue from products and services. Products sales are recorded under accounts receivable.

The accounts receivable increases as Smart Life-based sales rise. For example, iPad Air + magazine sales are growing. These are recorded first as product sales and then as service sales. The monthly fee charging service for tablets and printers is designed to sell hardware first and then collect its price through monthly fees. In other words, this means that accounts receivable grow on the balance sheet.

Accounts receivables increased by 600 million yen in the term ended March 2013, by 1.9 billion yen in the term ended March 2014, by 4 billion yen in the term ended March 2015, and by 3.8 billion yen in the term ended March 2016. Using different words, the Company needed more working capital as such accounts grew. If the Company makes progress in collecting monthly fees, however, the amount of working capital needed will not increase as it is currently doing, because a balance between outstanding accounts receivable and required working capital will gradually be achieved.

An increase in accounts receivable will also require enhanced credit management. In sales at conventional merchandise stores, the individual credit risks arising from customers paying by credit card are assumed by the credit card companies, but such risks accompanying sales at Smart Life stores must be taken on by the Company. In the event that a customer becomes unable to make monthly payments for any reason, the Company will have to assume that customer's debt.

In principle, as the Company sells products and services to individual customers who use IT products, it performs identification and usage checks very carefully before the sale. Volume sales to

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corporate customers are outside the scope of its business. In many cases, the Company may turn down a bulk purchase even from an individual customer because it is unsure whether such products and services are actually for private use. As is obvious from the above, credit risks are well controlled by stores and therefore there is no need to worry about such risks.

Changes in gross profit of products and services (provisional)

	2013.3		2014.3		2015.3		2016.3		2017.3	
Overall sales (consolidated)	51359	100.0	53772	100.0	51261	100.0	51729	100.0	46417	100.0
Service sales (consolidated)	12622	24.6	16194	30.1	19696	38.4	24631	47.6	24984	53.8
Goods sales (consolidated)	38737	75.4	37578	69.9	31565	61.5	27098	52.4	21433	46.2
Cost of services	3176	25.2	4676	28.9	5520	28.0	7443	30.2	6710	26.9
Overall gross profit (consolidated)	16114	31.4	18273	34.0	19472	38.0	21715	42.0	21249	45.8
Service gross profit (provisional)	9446	74.8	11518	71.1	14176	72.0	17188	69.8	18274	73.1
Goods gross profit (provisional)	6668	17.2	6755	18.0	5296	16.8	4527	16.7	2975	13.9

NOTE: Goods sales includes other services (royalties, Internet-related).

Figures in the column next to sales amount are a ratio of each segment sales to overall sales.

Provisional values are not necessarily accurate; these are approximations as reference data.

The quality of services is its source of competitiveness: active use of "Platinum Partners"

The Company does not merely sell hardware such as PCs and tablets, but offers services. This is a system under which convenient solutions are provided on a continual basis for a monthly fee. Some 60% of visitors to PC Clinics are those who bought products at other stores. That means they interested in something other than low prices. PC Clinics support PCs owned by our customers, which brings about efficiency.

When considering the profits generated by products sales and from service sales from a perspective of operating profit levels, a clear-cut breakdown of levels on classified into products and services is nearly impossible to achieve. The reason why this cannot be done is that the Company's management does not differentiate between products sales and service sales. Even though each staff member at stores has their own role, everyone provides both products and services. These sales are not differentiated when assessing employee performance. One pattern used involves a customer buying a product and subscribing to a service, thus becoming a regular customer of PC DEPOT, who naturally comes back again to buy some other product.

However, even when profits derived from product sales and from service sales are viewed from the perspective of operating income under certain prerequisites, the structure in which service sales are highly profitable remains unchanged. In the competition to capture this demand for services, the Company has an advantage that is furthered by its track record over the years and its personnel. Originally, the Company core policy of differentiation from its competitors is to provide services

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requiring time and effort for customers who are having difficulties using their purchases, but not for customers who do not require any follow-up services after purchase. Such customers are the main target of other companies.

Response to the rise of internet shopping

There is some concern that internet shopping might be a threat to over-the-counter sales. In fact, some people browse products at stores but actually buy them online, because of the prices.

This scenario is fine for those users who are able to make full use of their newly purchased hardware. However, others are in great need of convenient services in case they do not understand how to use their new hardware fully or are faced with some problem. That is where the Company has a chance to show what it can do. Basic sales of products such as iPhones or iPads do not make much profit. But if customers subscribe to premium services, the relationship with them can be maintained for a long period time, and service sales will contribute to earnings. In that sense, the Company is continuing to handle new products in a proactive way.

Pursuit of lifetime value

PC DEPOT has been evolving to achieve a brand new type of format by completing a total makeover of PC mass retailers. After transformation to Smart Life stores, stores experience changes in comparison from their previous formats, in that (1) customers stay in the stores longer, (2) more female customers visit, (3) customers revisit more frequently, and (4) customers consult with employees about various matters. The extent of sales in terms of customer hardware purchases changes little after renovation. However, sales from providing service are certain to increase. In other words, the stores gain long-term customers.

A short interval between visits means that visitors revisit the store again sooner once they have bought a product or service. Increasing numbers of female visitors represent the fact that needs for digital devices in households have risen and people wish to have a better command of them. In this sense, President Nojima has hit the bull's eye.

"Lifetime value" is a concept in which the time span during which a customer uses a product is considered to be that product's "lifetime." The value of the customer to the business in a general sense during the lifetime of that product is raised, allowing the Company to generate sales accordingly during that time. The Company's service sales do grow but in the normal growth pattern for services they become profitable only in the second or third year of a three or four-year contract. Service quality should be improved so that members are encouraged to buy more products from the same store. Of course, member numbers are bigger at existing stores than at new stores. New stores should initially

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compete in terms of products sales and then gradually increase the number of customer members from then onwards.

The number of service subscription members is increasing, so the "lifetime value" of a particular level can be ensured depending on the terms of the members' subscriptions. PC DEPOT is meeting the challenge of expanding a business model that is dependent on a customer base formed of members who subscribe to its services. The Company operates while carrying out analysis of its service sales.

Aiming to achieve an ordinary income to sales ratio of 10% and ROE of 15%

President Nojima has set management goals of an ordinary income to sales ratio of 10% and ROE of 15% as the key performance indicators (KPI). If the proportion of income from services increases in the current business model, a profitability ratio of 10% can definitely be achieved.

Assuming the monthly fee for membership services is five thousand yen, if the number of members grows to one million, the income from services could reach 60 billion yen. How will the Company capture customer demand for those services? The market will be paying attention to its strategy for the deployment of stores and the development of a new service menu.

The shift to Smart Life stores has sped up the transformation from a flow-based business model to an asset-based one. Connections between customers and the Company have become stronger. Connections between customers and the Company have certainly become stronger. Moreover, giving consultations to customers also serves to increase contact with them. Members of the service system exhibit several usage patterns, which cannot be explained only by the number of members and average values such as the average unit price. The conventional pattern has been service on a per-household basis. However, in the age of cloud services, the personal management of data has become important, and accounts for individual users are therefore important. The nature of services will also be further diversified.

There are four challenges. The first challenge is to secure locations for opening new stores. The second challenge is the manner of attracting customers. Since opening new stores in the form of Smart Life stores is intended in particular to obtain customers who need services, more ingenuity is required in attracting customers for this purpose than for mainly selling products that the Company used to focus on. Because sales that originate from rendering services to members become the core, the time period for recouping investment tends to be longer than in the past. On the other hand, as more and more customers become members, profitability can be easily maintained.

The third challenge is employee training. While the Company has been achieving success in technical training, which is its area of expertise, it is important for it to nurture employees at the level immediately below the store manager. For example, to what extent are the staff members responsible

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for quality management, store operations, and technical services able to pay careful attention to what is happening throughout an entire store? In this regard, the Company has been hiring retired and talented office workers as part-time working seniors to raise the level of courtesy and service to customers in stores.

The fourth challenge is governance in its daily operations. Rather than selling products, the stores provide services and then recruit customers as members by providing solution services. On the other hand, products are sold in the form of installment sales accompanied by services. The Company emphasizes a stock-type business, not a flow-type business. In this situation, the governance at stores in its broad sense includes the management of customer information and the full-time and part-time employees, and this management needs to be appropriately implemented.

Balance sheets

(millions of yen, %)

	2012.3	2013.3	2014.3	2015.3	2016.3	2017.3	2017.9
Current assets	14076	13888	18368	19771	25381	26123	24730
Cash and deposits	2083	2982	4679	2370	4754	7726	8989
Accounts receivable-trade	3495	3969	6731	9609	13249	11202	8651
Inventories	7285	5986	5775	6548	6128	6103	6059
Fixed assets	9052	8942	8644	9336	9622	9506	9494
Tangible fixed assets	4941	5073	4836	5013	5041	4857	4925
Goodwill	406	155	10	5	1	0	0
Guarantee deposits	1466	1387	1349	1639	1810	1750	1730
Lease deposits	1272	1268	1248	1275	1323	1403	1373
Total assets	23128	22831	27012	29108	35004	35629	34225
Current liabilities	9225	9009	9758	11647	12271	6786	6857
Accounts payable-trade	3506	2087	3506	1691	1245	1230	1081
Short-term loans payable	2100	2550	900	4520	5200	0	0
Long-term loans payable (within one year)	1518	1849	1727	1447	1044	2125	2012
Fixed liabilities	4449	4149	3915	2428	1347	5830	4856
Long-term loans payable	3809	3479	3244	1796	751	5265	4282
Net assets	9464	9671	13342	15032	21334	23011	22511
Interest-bearing liabilities	7428	7879	5871	7764	7197	7391	6294
Interest-bearing liabilities ratio	32.1	34.5	21.7	26.7	20.6	20.7	18.4

Response to working capital is also important

As sales from member-service-inclusive products rise, accounts receivables increase and the Company needs more working capital. But this poses no problems since the Company is able to sufficiently cover its needs even if there should be 10 billion yen increase in the future.

On the balance sheet as of the end of March 2017 and the first half of the term ending March 2018, accounts receivable posted a decrease due to an intentional reduction in sales of service-inclusive products. In connection with this the free cash flow increased.

Looking back on the year, the growth of Smart Life stores has spurred sales of services. The types

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of customer segments have changed and the efficiency of fixed assets has increased. In the term ended March 2016, while capital investment reached 1.3 billion yen, accounts receivable increased by 3.8 billion yen and most of this amount originated from installments receivable related to premium services. For example, when a Just Price Fon (a low-priced smartphone) is sold, a payment for the hardware of 30,000 yen will be collected as part of the monthly service fees. The 30,000 yen is in other words, the credit sales price.

Even though the accounts receivable increases, the Company will not remove this from the balance sheet. Since the Company is fully aware of its customer attributes, there is virtually no risk of irrecoverable debt. The Company can manage with funds on hand and handle loans without any problem.

There are no major financial concerns. So how should the Company make efficient use of its free cash flow from now on? Well, the Company will be able to put more effort into investing in human resources and start to consider R&D-type open innovations. As a financial strategy, the Company considers a sound financial position to be an equity ratio of at least 50% and a degree of indebtedness within 25%.

Cash flow trends

	2012.3	2013.3	2014.3	2015.3	2016.3	2017.3	2018.3 (forecast)
Cash flow from operating activities	-635	1597	2010	-2512	516	4292	5970
Net profit after tax	-95	537	1848	1790	2742	1325	1770
Depreciation	691	728	685	781	897	943	900
Amortization of goodwill	296	259	145	5	4	0	0
Accounts receivable	-1014	-476	-2783	-2903	-3640	2034	3500
Inventories	-1785	1299	210	-772	420	24	50
Accounts payable	1088	-1421	1417	-1816	-449	-16	-250
Cash flow from investing activities	-2537	-994	-441	-1436	-970	-1090	-900
Tangible fixed assets	-1691	-844	-332	-797	-604	-830	-750
Intangible fixed assets	-140	-135	-374	-260	-291	-178	-150
Free cash flow	-3172	603	1569	-3948	-454	3202	5070
Cash flow from financing activities	2752	295	127	1637	2837	-229	-3650
Long-short term borrowings	2964	451	-2007	1892	-767	394	-2000
Common stock issuance	0	0	2289	0	3983	0	0
Common stock repurchases	-25	0	0	-1	0	-5	-1000
Cash dividends paid	-153	-155	-153	-253	-380	-612	-650
Cash and cash equivalents at end-term	2083	2984	4679	2370	4754	7726	9146

The Company raised 2.3 billion yen through equity financing in January 2014. In terms of the usage of these funds, the Company allocated 900 million yen to opening new stores, 1.1 billion yen to renovating existing stores, and 300 million yen to improving its IT system. Through financing in

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November 2015, the Company raised 4.0 billion yen. The usage of the funds can be broken down to 1.5 billion yen for renovation to Smart Life stores, 1.0 billion yen for new Smart Life store openings, 500 million yen for system investment and 1.0 billion yen for working capital. As the number of outstanding shares increased by 12.6%, a dilution occurred relative to the extent of this increase. However, the dilution can be more than absorbed by the future growth in profits.

4. Near-term operating results: Earnings to recover from the beginning of the second half of this term with the examination of member services nearly complete

Earnings for the term ended March 2017 fell due to the review of membership services since the second half

For the term ended March 2017, the Company reported net sales of 46,417 million yen (down 10.3% YoY), operating income of 3,402 million yen (down 16.7% YoY), ordinary income of 3,467 million yen (down 16.2% YoY), and a net income of 2,269 million yen (down 15.7% YoY).

The results above were due to the substantial decline in performance in the second half, caused by the review of the Company's business structure triggered by the case in August last year. Operating income in the first half was 2,133 million yen and 1,269 million yen in the second half.

The Company reported higher sales and profits in the first quarter, lower sales and higher profits in the second quarter and lower sales and profits in the third and fourth quarters. The impact of and responses to the problem regarding services to an elderly customer, which occurred in August had a significant effect on earnings. Sales and profits declined considerably, due to factors such as assignment of in-house personnel to the Quality Management Department, narrowing of product offerings, disposal of product inventories and voluntary restraint on advertising and promotional activities. Though customers were gradually coming back, the number remained low.

The Company made steady progress in confirming current member service situations through direct mail and phone calls. Since the Company assigned 300 in-house personnel to the newly established Quality Management Department, there is currently a shortage of sales staff in the stores. Although promotion activities resumed to some extent in November 2016, the sales effort made at the end of the year was not sufficient due to the staff shortage.

Regarding product sales, the gross profit from product sales decreased due to disposal of long-term inventories. Sales of service-inclusive products decreased because not enough attention was paid to that area due to the sales staff shortage.

Sales from solution services (on a year-over-year basis) in the third and fourth quarters were heavily

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affected by the case that occurred in August. A decline in sales was caused by the reduction in the number of premium service members and the lower sales of service-inclusive products.

Quarterly results
(millions of yen)

	Net sales				Operating income
	Products	Solution services	Internet-related	Total	
2016.1Q	5482	6782	314	12598	1344
2016.2Q	4261	6682	322	11285	789
2016.3Q	4955	5792	315	11100	577
2016.4Q	5400	5727	306	11433	692
2017.1Q	4639	5755	302	10713	585
2017.2Q	4284	5693	315	10305	595

Results for first half of the term ending March 2018 confirmed to have bottomed out

In the first half of the term ending March 2018, the Company reported net sales of 21,018 million yen (down 12.0% YoY), an operating income of 1,180 million yen (down 44.7% YoY), an ordinary income of 1,228 million yen (down 43.9% YoY), leading to a significant decrease in profit.

While there was a large decline in the profit margin due to strong performance in the first half of the previous term, the first half of the current term was in the bottoming-out phase. Operating income was basically within our expectations and the Company was able to stop a deterioration in earnings at this level.

Product sales declined by 8.4% year-over-year, and sales from solution services declined by 15.0% year-over-year. Sales from solution services declined partially due to cancellation of premium services but largely due to voluntary restraint in sales of service-inclusive products. The Company reviewed its internal quality management and sales system and focused on confirming customer service usage situations. These responses are nearly complete and sales of new service-inclusive products have started in late September.

By quarter, the products including PCs sold better in the second quarter than in the first quarter. Sales from solution services totaled 5.76 billion yen (6.81 billion yen YoY) and 5.69 billion yen (6.66 billion yen YoY) respectively for the first and second quarters, showing nearly the same level.

Since the case in August last year, the Company has become committed to reviewing services for existing customers and confirming their situations. For that purpose, in the second half of the previous term, the Company voluntarily refrained from conducting advertising and promotional activities, offering service-inclusive products and opening or renovating stores. The Company gradually restarted

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these actions in the first half of the current term. The Company strengthened its targeted promotional activities and renovations and also restarted the sale of service-inclusive products.

On the balance sheet, accounts receivable decreased by approximately 2.5 billion yen as of the end of September 2017. This is due to progress in collection of receivables, after the voluntary restraint in the sale of service-inclusive products since the second half of the previous term. Since sales from service-inclusive products will increase from here onward, accounts receivables will increase again from the next term.

Changes in the percentage of total sales accounted for by service sales

(million yen, %)

	Term Ended March 2013		Term Ended March 2014		Term Ended March 2015		Term Ended March 2016		Term Ended March 2017		Term Ending March 2018	
	Service sales	As a percentage of total sales	Service sales	As a percentage of total	Service sales	As a percentage of total	Service sales	As a percentage of total sales	Service sales	As a percentage of total	Service sales	As a percentage of total sales
1Q	3025	24.8	3689	30.3	4505	36.2	5635	46.1	6807	54.0	5755	53.7
2Q	3083	25.8	3894	31.8	4681	39.3	5995	48.7	6657	59.0	5693	55.2
3Q	3223	23.5	4215	30.6	5229	38.3	6491	47.6	5793	52.2		
4Q	3329	24.7	4396	28.2	5281	39.9	6510	48.0	5727	50.1		

In terms of cash flows, investments slightly increased. Renewal of stores into Smart Life stores were carried out at 6 stores at a high rate during the first half of the current term (2 stores and 3 stores in the first and second halves of the previous term, respectively).

The sales figure for the first half of the current term was 46.9% (47.1% a year earlier), exceeding 44% as estimated in the Company's plan at the beginning of the term. The ratio of sales, general, and administrative expenses to net sales increased to 41.3% (38.1% a year earlier). The Company opened only one store, the Roppongi Store, during the current term. Renewed stores are seeing a double-digit increase in customers.

Stores returned to a normal routine—the number of members will shift from a net decrease to a net increase

The increase in the number of new subscribers has exceeded the decrease in the number of existing members. The number of members will shift from a trend of net decrease to a net increase on a monthly basis.

Most stores are getting used to the new quality management system. The Company has assigned in-house personnel to be responsible for quality and has been prioritizing the allocation of human resources to check subscribers' usage of the services listed in their contracts. In addition to an increase

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in personnel expenses, there is also now a need to narrow down sales. As 300 employees were transferred to the Quality Management Department, there were an insufficient number of personnel providing sales services to customers at stores. To cope with this situation, the Company has narrowed its sales product range and service-inclusive product sales.

The number of cancellations has been decreasing, and the stores are reverting to normal operation. Meanwhile, the number of new members is increasing. While customers give us a variety of feedback, problems concerning services for elderly customers that were widely criticized on the Internet have not appeared. The cancellation rate has declined to such a level that it no longer needs close attention. Renovated stores are also seeing an increase in customers. The new Setagaya-Kinuta Store has begun to get operations on track. Among the small-scale stores located in central Tokyo, the Azabu-Juban Store in particular is exhibiting good performance.

The Company started posting leaflet advertisements again and has also started full-fledged sales promotion activities that take into consideration the shortage in personnel after narrowing down the products and services provided.

New products leading the business

The basic structure of the premium service has not been changed; however, its menu has been reviewed. Various payment methods have been prepared for membership fee payment such as payment at the time of contract, payment in one year, payment in three years and payment in four years so that customers can choose a payment method along with a clear understanding of it. Ideas from consumer advisers are being reflected in this.

Members subscribing to services necessarily want to contact stores when inquiring about how to use devices and about updating software, malfunctions, and replacement purchases. In the IT business, many new products for consumer use come out on the market every year. One of the hottest trends this year is a full-fledged roll-out of smart speakers using voice recognition technology. Following the Amazon Echo and Google Home, Microsoft is also expected to launch this as a new product.

The PC market is regaining some momentum. The Company also intends to increase sales of member-service-inclusive products while properly responding to customer needs.

When new products are released, the first users who purchase them can deal with any issues they encounter by themselves. These products are then purchased by users who cannot use them well, but would still like to use them. These people require some form of support. That is where the Company's Smart Life stores come into play.

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Effects from the new sales service system will appear in the days ahead

The need for support will not decrease. Rather, the number of subscribers will increase because sales activities for customers have significantly improved. The new system was fully launched in the term ending March 2018. Education and training for routinely introducing new quality services will be gradually established and will increase productivity. The Company has been continuously training its employees to achieve the above.

Comparison of earnings forecasts

	(millions of yen, %)					
	2015.3	2016.3	2017.3	2018.3 (forecast)	2019.3 (forecast)	2020.3 (forecast)
Net sales	51261	51729	46417	45000	47000	50000
Gross profit	19472	21715	21249	21150	22000	24500
Ratio to sales	38.0	42.0	45.8	47.0	46.8	49.0
SG&A expenses	16426	17628	17846	18550	19000	20000
Ratio to sales	32.0	34.1	38.4	41.2	41.2	40.0
Operating income	3045	4086	3402	2600	3500	4500
Ratio to sales	5.9	7.9	7.3	5.8	7.4	9.0
Ordinary income	3162	4139	3467	2680	3500	4500
Ratio to sales	6.2	8.0	7.5	6.0	7.4	9.0

Earnings will start to improve in the second half of the term ending March 2018

After bottoming out at 1.2 billion yen in the first half of the current term, the half year operating income will be 1.4 billion yen in the second half of the current term and respectively 1.6 billion yen and 1.9 billion yen in the first and second halves of the next term. A growth in solution services sales by 10 to 15% year-over-year appears a reasonable figure.

The Company's plan for the current term ending March 2018 includes net sales of 46,600 million yen (up 0.4% YoY), an operating income of 2,420 million yen (down 28.9% YoY), an ordinary income of 2,500 million yen (down 27.9% YoY), and a net income of 1,650 million yen (down 27.3% YoY). Profit is still forecasted to decrease.

Thanks to a temporary increase in sales as a result of cancellations, profits in the previous term declined slightly less than the decrease included in the target revised during the term. This will affect the performance in the current term and the decline in operating profit this term will be slightly larger. As shown in the planned operating profit of 1,050 million yen in the first half (down 50.8% YoY) and 1,370 million yen in the second half (up 10.3% YoY), the Company expects a recovery to start in the second half.

The plan for this term is based on the following assumptions: a growth in sales on a same-store basis by 100% (89.7% in the previous term); a growth in solution services sales by 100% (100.8%); and a gross profit ratio of 44% (45.6%). The Company expects that the solution services business will

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recover considerably toward the second half. In fact, the gross profit of services has been increasing partly due to a temporary reduction of service-inclusive products.

As sales and service systems are established at stores, service-inclusive products have also started to gradually be effectively reintroduced in time. In terms of store development, the Company is prioritizing the renewal of stores into Smart Life stores. The Company limits the opening of new stores to those cases where the location needs to be secured for certain reasons. The Company is accelerating its renovation of current stores from 5 stores in the term ended March 2017 to 9 to 10 stores in the term ending March 2018. Customer service and profitability have already been proven to increase after the renovation so the effectiveness of store renovation is a reasonable certainty.

In the second half of the current term, profitability will improve due to the following: 1) the number of members will start increasing, 2) the number of premium service contracts will start increasing after bottoming out, 3) the gross profit from products sales is improving, and 4) the temporary increase in sales, and normalizing of general, and administrative expenses. The operating results are thus expected to exceed the Company's plan.

On the balance sheet, while accounts receivable decreased, cash and deposits increased. This is due to the progress in collection of receivables. Since service-inclusive products will be actively promoted from the second half of the current term, working capital requirements will inevitably arise. Launch of new products and services will be implemented and the results in the term ending March 2019 are expected to further improve.

5. Evaluation: Regaining customer trust and shifting to an active approach

Full-fledged recovery in earnings

The Company has set the mid- to long-term goal of an operating income ratio to sales of 10% which is not a difficult figure to achieve. Before the incident occurred, the operating income ratio improved to 8.0% in the term ended March 2016. The ratio is forecasted to decline to 6.0% in this term, but this will be the bottom of its decline.

Solution services are accepted by customers and the need for these services will continue to broaden. The profitability of member services will improve as membership increases. More customers will want to use member-service-inclusive products together with support plans.

The sales mix of the Company will continue to shift to more solution services, and the content of these services will also change. In the near term, the Company will aim to achieve sales of 50 billion yen and an operating profit of 4.5 billion yen.

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The Company's business model remains unchanged. Since the Company will bolster the service system that further meets customer needs, a more rigid system will be established. In this system, more demand for services will be captured and more repeat customers will be retained even though costs will increase. Profit is therefore highly likely to recover and grow higher than before.

As the basic business model is still thriving, earnings should recover with more momentum starting this second half. Profit is expected to achieve a record high in a few years.

Regained trust and future expectations

The Company carried out a market purchase of treasury stock (share buyback) for approximately one billion yen (equivalent to 2.9% for a maximum of 1.5 million shares) in August. This share buyback was regarded as an indication of confidence in its operating results and was viewed favorably by the markets.

The Company had temporarily narrowed down the product offerings considerably. However, the company will become even stronger if employees get used to new governance, including 1) quality management of customer services, 2) promotion of customer services to improve customer satisfaction, and 3) an internal framework for legal affairs and compliance, and that fact that such governance works effectively. The demand for service is high, and the Company is now able to enhance product offerings since the new system has been getting on track.

President Nojima is confident that the results will recover to former levels when the internal structure gets used to the new framework and service capabilities improve. Trust from existing members and the local communities is still in the recovery phase. We intend to pay close attention to a further enhanced business model from PC DEPOT two years from now.

The Company 1) sold traditional goods (products), but 2) changed to selling services that make the usage of goods convenient, and 3) is selling services that are integrated with goods (solution services) now. If existing stores are able to increase sales as a whole by accommodating demand for services, the Company will manage to maintain growth by rolling out four to five stores a year steadily.

Service subscribers will continue to increase. The Company has been rebuilding trust and is focusing its attention on heightening the effect from its stock. Customers of the service system exhibit several usage patterns: some users own several pieces of hardware, while others subscribe to the service system so that their family members can use it. By making these users members of its service system, the Company will have a greater scope for offering services in the future.

It was in 2005 that the Company took the decision to shift its revenue source from selling PCs to providing services. Over the past eight years, the Company has promoted the shift of its business model. It is almost certain that the Company's business model will retain its niche existence after it

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overcomes this problem. The Company has been promoting a shift to a stock-type profit structure based on service sales. In order to take more time to confirm the effect of trust building, the Company is rated B. (Please refer to the front page for an explanation of corporate ratings.)

The number of shareholders was 6,513 as of the end of September 2017. The shareholder special benefit plan distributes a 1,000 yen gift certificate (or 2,000 yen PC Clinic store voucher) for 100 shares, a 2,000 yen gift certificate (or 4,000 yen PC Clinic store voucher) for 400 or more shares, or a 3,000 yen gift certificate (or 6,000 yen PC Clinic store voucher) for 1,000 shares or more. Since shareholders can use gift certificates for online shopping, PC DEPOT stores need not be nearby. Increasing that number further will be effective in unifying customers and shareholders. Increasing that number further will be effective in unifying customers and shareholders. In terms of returning profits to shareholders, the Company conducted a 1:1.2 stock split with September 30, 2016, as the record date and decided to pay a dividend of 13.0 yen per share after the stock split.

Based on a stock price of 864 yen as of December 14, 2017, PC DEPOT has a PBR of 1.93, an ROE of 7.9%, and a PER of 24.8, with a dividend yield of 1.5%. The Company stock price will be further adjusted in the market, reflecting factors such as the progress of service improvements for about 400 thousand members, increase in new members, trends in service sales, and the timing for improving earnings.

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