

## GCC Management® Analysis Report: Scala, Inc. [4845]

July 30, 2019

## Three strategies, such as customization and cloud model use, to win the hearts and the minds of customers in the age of AI/IoT and Industrial Revolution 4.0

This report analyzes corporate value from the perspective of **GCC management**®<sup>01</sup> which emphasizes three elements of **Growth** (in sales), **Connection** (of people and businesses, leading to improve Return on Invested Capital), and **Confidence**.

### Aiming high growth with the “three strategies to win the hearts of customers”

Scala, Inc. is a leading provider of cloud-based communication tools with enhanced security, as SaaS/ASP<sup>3</sup> services, to approximately 1,000<sup>2</sup> companies listed in Japan. It is promoting the “Three strategies to win the hearts and minds of customers,” which are namely 1) optimal customization, 2) stress-free cloud services, and 3) attractive monthly billing. Scala thus achieves more added value and higher efficiency and improves ROIC through **Connection** of its sales people, engineers and with its customers, reduces business risks by achieving sales **Growth** and stability (**Confidence**), and realizes M&As by curbing capital cost and strengthening funding capacity, and maintains high payout ratio. Scala is thereby building a virtuous cycle of value enhancement from the viewpoint of the **GCC management**®.

### Enhanced growth expectation in the age of AI/IoT

In the age of AI/IoT, IT companies are expected to integrate diverse information by use of IT and engage in increased customization. Scala is expected to create a virtuous GCC cycle and grow dramatically as its strategy is centered on customization. Further growth is expected by collaborating with Softbrain Co., Ltd. (SB) [TSE First Section 4779], a major sales support software company with 5,000<sup>4</sup> corporate customers, which became a subsidiary of Scala in July 2016.

### Upside potential of 2-3 times of market cap

The AI market is projected to grow by about 30-40%<sup>5</sup> per year during 2017-2022. Assuming Scala and SB realize such a growth rate, Scala's shareholder value is estimated to be ¥46.7 billion. This amount, which is 2-3 times higher than the current market cap, should be achievable, in light of anticipated growth potential of Scala.

1: A trademark registered by J-Phoenix Research in Japan. A systematic term to describe the concept of corporate value. See “What is an analytical framework of the GCC management®?” in this report.

3: SaaS (Software as a Service) allows customers use applications via a web browser, without installing them on their PCs. ASP (Application Service Provider) is a business providing application functionality to customers over the Internet.

2, 4: Data from the website of Scala and SB; 5: See the note on Page 6 of the report.

Fiscal Item	Sales ¥mn	YoY %	Operating income ¥mn	YoY %	Ordinary income ¥mn	YoY %	Net Income ¥mn	YoY %	EPS ¥	term-end closing ¥ share price	
										High	Low
June 2016	2,693	20.4	616	14.0	1,196	116.2	830	129.6	56.68	684	486
June 2017	10,663	295.8	3,736	505.7	3,728	211.7	2,987	260.7	177.52	1,104	547
June 2018 -3Q Cum.	12,829	20.3	1,546	△ 58.6	1,535	△ 58.8	707	△ 76.3	41.88	1,324	674
June 2018 -3Q Cum.	9,054	12.4	1,225	△ 67.4	1,220	△ 67.6	555	△ 82.2	32.93	883	721
June 2019 -3Q Cum.	12,781	41.2	1,702	38.9	1,692	38.7	754	35.8	44.58	1,207	744
June 2019 Est.	16,600	29.4	2,000	29.3	1,900	29.6	890	25.9	52.57	-	-

(Source) Company Financial Report, Created by J-Phoenix Research Inc. from FactSet

#### Basic report

Written and Edited by  
J-Phoenix Research Inc.

#### Corporate Profile

Headquarters	Shibuya-ku Tokyo
President CEO	Norikatsu Nagino
Established	December 1991
Capital	16,040 thousand yen
Listed	May 2001
URL	<a href="https://scalagr.jp">https://scalagr.jp</a>
Industry	Information & Communication

#### Key Indicators (as of July 29, 2019)

Stock Price	923yen
Highest in 52 weeks	1,324yen
Lowest in 52 weeks	674 yen
Outstanding Shares	16,971,659 stocks
Trading Units	100 stocks
Market Capitalization	15,665 million yen
Prospective Dividend	24.0 yen
Estimated Profit Base EPS	52.57 yen
Estimated PER	17.57 Times
Actual BPS (March 2019)	403.72 yen
Actual PBR	2.28 Times

# 1. Value creating structure and corporate value

"Three strategies to win the hearts and minds of customers" for achieving high growth

Evolving from a sales distributor of database services in line with changing times

## "Three strategies to win the hearts and minds of customers" for achieving high growth

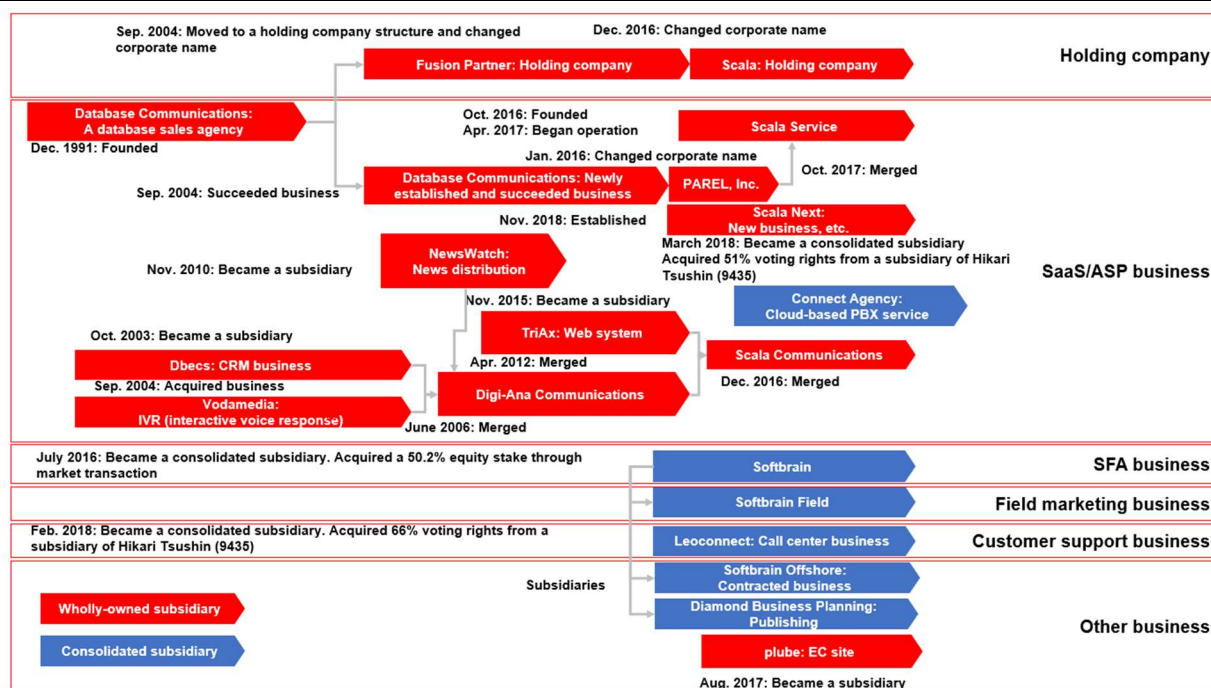
Scala, Inc. is a leading provider of cloud-based communication tools with enhanced security, as SaaS/ASP<sup>3</sup> services, to approximately 1,000<sup>2</sup> listed companies in Japan. It is promoting the "Three strategies to win the hearts and minds of customers," which are namely 1) optimal customization, 2) stress-free cloud services, and 3) attractive monthly billing. Scala thus achieves more added value and higher efficiency and improves ROIC through **Connection** of its sales people, engineers and with its customers, reduces business risks by achieving sales **Growth** and stability (**Confidence**), and realizes M&As by curbing capital cost and strengthening funding capacity, and maintains high payout ratio. Scala is thereby building a virtuous cycle of value enhancement from the viewpoint of the **GCC** management®.

## Current business and development since foundation

Being founded in December 1991 as a sales distributor of database services, Scala has expanded its business by adopting the M&A strategy since its IPO in 2001. Scala's current business and its development since foundation are stated below. They show how Scala has flexibly transformed its business in order to promote the three strategies. Such flexible, agile transformation capability is one of Scala's attractive points.

### Scala's businesses and business evolution from the time of its foundation

Business segment	Description of business
SaaS/ASP business	Provision of SaaS/ASP-type services that use automated voice technologies of the browser, telephone, fax, etc. over the Internet or telephone lines
SFA business	Provision of services, such as the licensing of the sales support system, cloud services, customized development, marketing consulting, marketing skill training, and operation consulting and education by using iPad and other tools
Field marketing business	Provision of services related to field activities, marketing research, etc.
Customer support business	Provision of one-stop consulting services related to customer support, such as call center operations and diverse BPOs
Other business	Provision of the EC website for buying and selling battle-type trading cards; contracted development of software; publishing of business-related books, etc.



(Source) Prepared by J-Phoenix Research, based on the FY6/2018 Securities Report

## Needs of customization by each customer in the AI/IoT age

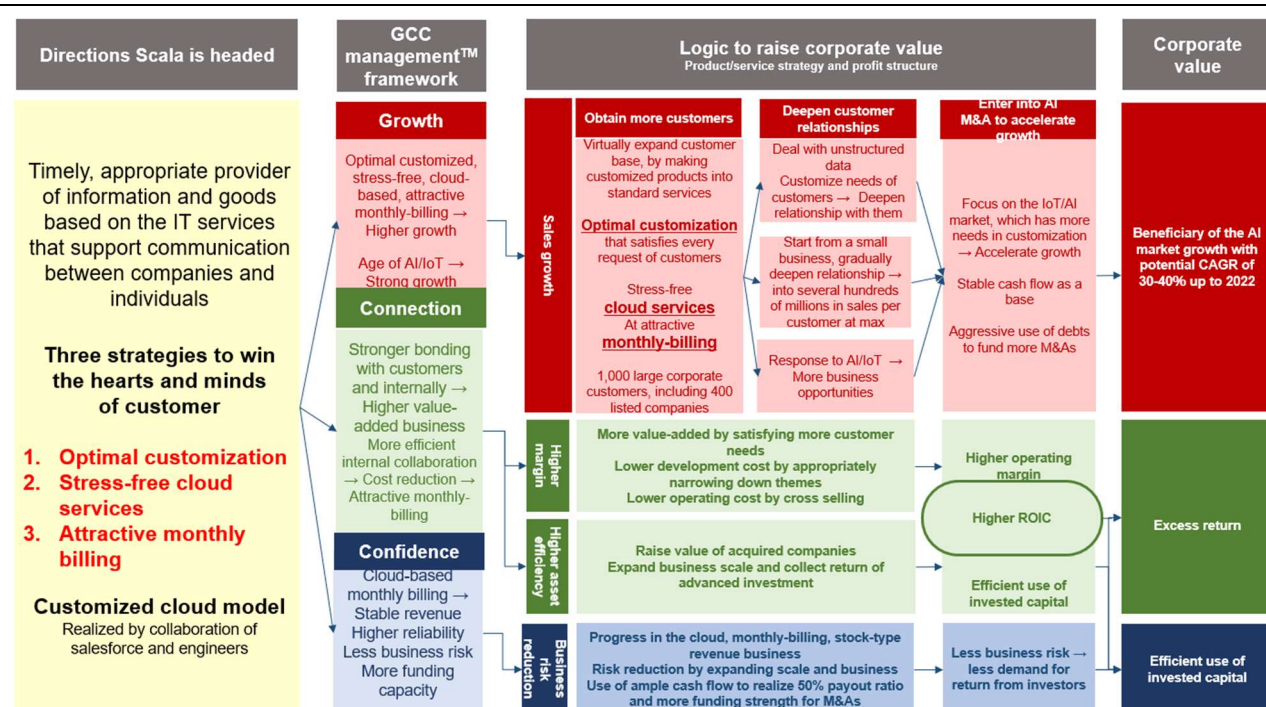
## Rising expectations for growth in the age of AI/IoT

In the age of AI/IoT, IT companies are expected to integrate diverse information by use of IT and engage in increased customization. Scala is expected to create a virtuous GCC cycle and grow dramatically as its strategy is centered on customization. Further growth is expected by collaborating with Softbrain Co., Ltd. (SB) [TSE First Section 4779], a major sales support software company with 5,000<sup>\*4</sup> corporate customers, which became a subsidiary of Scala in July 2016. In the age of AI/IoT, IT companies are expected to integrate diverse information by use of IT and engage in increased customization. Scala is expected to create a virtuous GCC cycle and grow dramatically as its strategy is centered on customization. Further growth is expected by collaborating with Softbrain Co., Ltd. (SB) [TSE First Section 4779], a major sales support software company with 5,000<sup>\*4</sup> corporate customers, which became a subsidiary of Scala in July 2016.

## Mechanism to raise corporate value through the three strategies

In general, corporate value increases with three elements: 1) sales growth; 2) improvement in ROIC; and 3) reduction in business risks. The figure below summarizes Scala's "three strategies to win the hearts and minds of customers" from the GCC viewpoint and how they affect the three elements of corporate value. It reveals how the elements of a virtuous cycle of the strategy toward the enhancement of corporate value are related to each other. Scala is expected to accelerate this virtuous cycle in the age of AI/IoT.

### Value creating story based on the three strategies



(Source) Prepared by J-Phoenix Research

## Analysis of differentiation and barriers against imitator

## Reasons of differentiation and barriers against imitator

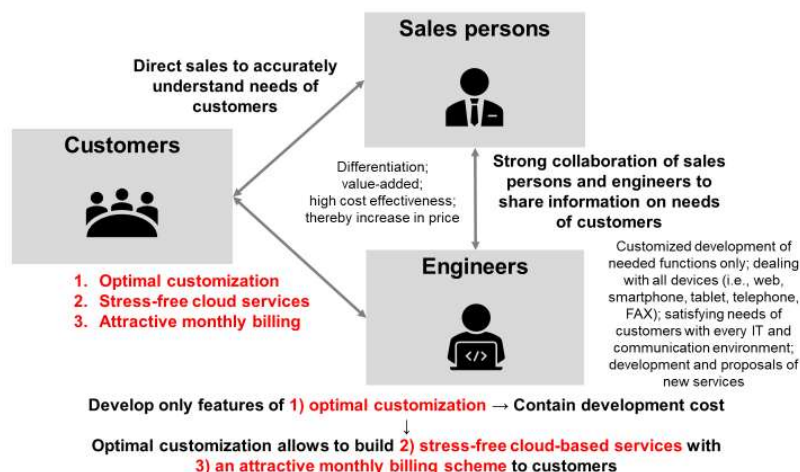
### Leadership of President Nagino, PhD in the AI area

Under the leadership of President Nagi

no, who has a PhD in the AI-related area, came from a subsidiary acquired by Scala in 2003, and was appointed President & CEO in 2013, a strong structure of collaboration among salesforce and engineers has been established. By appropriately capturing needs

of customers and narrowing down the development theme to functions needed by customers, Scala is able to promote the "three strategies to win the hearts and minds of customers," which are namely 1) optimal customization, 2) stress-free cloud services, and 3) attractive monthly billing. This mechanism is illustrated below.

### Three strategies to win the hearts and minds of customers



**Customization of needs and attractive pricing lead to a high customer retention rate and low risk in collecting receivables**

(Source) Prepared by J-Phoenix Research, based on an interview with the company

Direct salesforce members identify and ascertain the needs of customers and feed the information back to the development team, and engineers develop new services on that basis. This creates a virtuous cycle at Scala. As basics, sales persons visit customers, make direct sales, directly identify their needs, and provide solutions or propose new services to fill their potential needs. This is a beneficial scheme for both customers and Scala: Customers have their needs, which could normally be realized as contracted development, satisfied as a part of the cloud-based SaaS/ASP service, while Scala can avoid risk of their developed service becoming unsalable. Cloud services ordinarily are difficult to customize but Scala willingly customizes its services for each customer, as one way to be differentiated from its competitors.

Based on needs captured from direct members of the salesforce, Scala also improves service functions and develops new services. Even in the case of existing services, its average transaction amount per customer can be raised if the services are customized and meet particular needs of a customer. In addition, Scala's services can be implemented in any IT or communication environment as its services can be used with diverse communication devices including the Web, smartphones, tablets, telephones, and fax machines.

Attractive pricing also allows Scala to realize a high customer retention rate and low risks in collection of receivables. Scala's income model, which is primarily consisted of accumulated monthly billings, enables it to realize stable earnings.



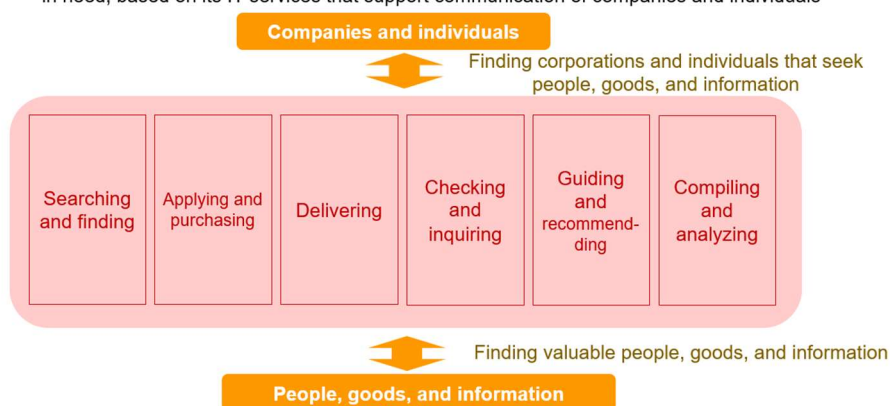
Customized services  
that are difficult to be  
imitated by large-  
scale IT companies

## Value provided by Scala

Thanks to the virtuous cycle of developing new services and new products, combined with aggressive acquisitions of companies and businesses, Scala is now engaged in a wide range of businesses with the aim of timely providing information and products in need, based on its IT services that support communication of companies and individuals as summarized below.

### Value provided by Scala

Scala is engaged in a wide range of businesses with the aim of timely providing information and products in need, based on its IT services that support communication of companies and individuals



(Source) Prepared by J-Phoenix Research, based on Scala's results briefings

## Reasons of being difficult to be imitated

No large-scale IT company has a business model similar to that of Scala. Cloud service providers mainly develop all-inclusive types of packaged products and are not typically concerned with customization. In case they are concerned, they charge a hefty sum for development cost.

## Scala's differentiating, hard-to-imitate business model: Current status, outlook and potential risks

	Scala's differentiating strategy	Why other companies cannot imitate Scala	
		General cloud-based SaaS/ASP companies	Contracted developers
<b>Current status</b>	Leadership of President Nagino, PhD in AI, Tokyo Institute of Technology  Close working structure of salesforce and engineers  Proper understanding of needs and cost-contained development → <b>Optimal customization</b>  Good operation that secures excess return  Continual customizing; <b>Cloud based and monthly billing</b> → Stable profit  3 strengths to develop customers and deepen business with existing customers (targeting large companies)	Main focus on development of all-inclusive SaaS/ASP products; less focus on flexible customization to meet needs of customers   Seek return on investment with monthly billing, with little customized development and little additional development expense Do not pursue collaboration of salesforce and engineers to promote customized development	Thorough customization but lack of flexibility in billing by charging all expenses to customers  Persistent problems of customers with cost risks and on how to share contracted development cost with customers  Hard to introduce cloud services and monthly charging
<b>Future</b>	Scala's three strategies to become more effective in the age of AI/IoT	Need to develop a customized strategy, befitting the age of AI/IoT	May benefit from increased effectiveness of customization in the age of AI/IoT
<b>Potential risks</b>	Less well-known → Hard to develop new customers Out-of-control risk occurrence at SB during the process of strategy integration	Difficulty to change the corporate culture of selling packaged SaaS/ASP	Intensified problems of customers with cost risks and on how to share contracted development cost with customers

(Source) Prepared by J-Phoenix Research

At the end of the spectrum, contracted developers customize software but charge all expenses to customers, combined in one payment. Cloud-service SaaS/ASP providers or contracted developers would not readily consider adopting a business model to customize the product and charge monthly billing at affordable rates. It would therefore be difficult for these companies to suddenly transfer themselves into Scala's type of business model.

### Future outlook

As mentioned above, Scala with its management style is expected to grow dramatically in the age of AI/IoT. Lack of progress in integration with SB and unexpected events can be risks but there is no sign to suggest these at present.

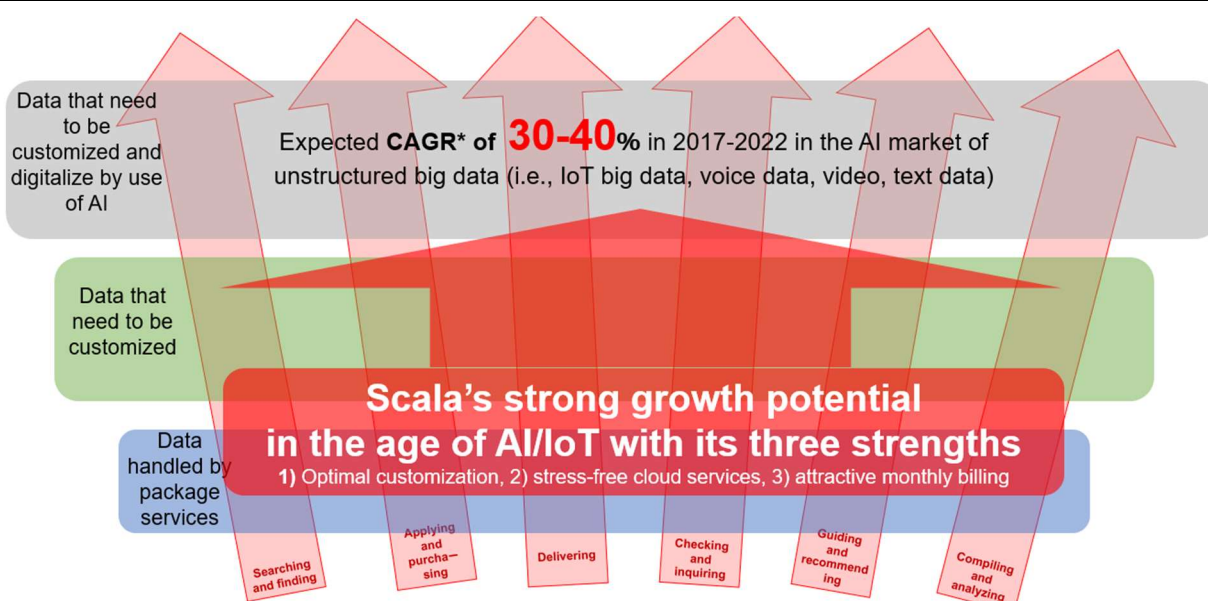
The figure on the previous page summarizes Scala's current situation with its differentiated, hard-to-imitate strategy business model, as well as future outlook and potential risks/measures.

## Business opportunities in the age of AI/IoT

### Changing characteristics of data in the age of AI/IoT and its significance to Scala

As aforementioned, IT technologies will enable information which was not digitally stored as data in the past to be integrated in the age of AI/IoT. As data targeted in AI become more diversified, IT companies will be required to make more customized responses. In addition, enhanced security demand will lead to an increased need for cloud-based stress-free services. Unsurprisingly, the importance of containing monthly costs will also emerge. In such environment, Scala can be expected to grow dramatically by promoting three strategies of 1) optimal customization, 2) stress-free cloud services, and 3) attractive monthly billing in the age of AI/IoT.

### Growing business opportunities in the age of AI/IoT and Scala's positioning



\* Surveyed by an independent IT consulting and research firm, ITR Corporation (published on 12/11/2018, estimating CAGR of 35.6% in 2017-2022. Source: <https://www.itr.co.jp/company/press/181211PR.html>  
According to the Nikkei Newspaper article "IDC Japan announced projection of spending in the global AI system market," the spending in AI systems will more than double to \$79.2billion in 2022 vs. 2019 with a projected CAGR of 38.0% in 2018-2022.

(Source) Prepared by J-Phoenix Research, based on an interview with Scala, etc.

## The impact of SB must be taken into account in evaluating Scala's corporate value

## The impact of SB in evaluating Scala's corporate value

In evaluating Scala's corporate value, the impact of SB, a listed subsidiary of Scala with 50% voting rights, must be taken into account. Scala fully consolidates SB in its consolidated financial statements. In the evaluation of corporate value, only a portion of SB attributable to Scala must be included. SB's impact in the first nine months of FY6/2019 is summarized below. It is estimated to account for roughly a half of Scala's consolidated figures and to contribute 30-40% to Scala's corporate value.

### Business results of the first nine months of FY6/2019 and full-year forecasts

[Million yen, unless otherwise stated]

	Scala				Relationships with Softbrain (SB)*	
FY6/2019	Results			YoY Improvement	Corresponding business	Attribution to Scala's business
First nine months	SaaS/ASP	Sales revenue	3,010	28.1%		
		Segment profit	609	36.4%		
		Profit margin	20.2%	1.3% points		
	SFA	Sales revenue	3,592	14.4%	Sales innovation	100%
		Segment profit	703	29.8%		
		Profit margin	19.5	2.2% points		
	Field marketing	Sales revenue	2,912	17.5%	Field marketing	100%
		Segment profit	228	22.8%		
		Profit margin	7.8%	0.4% points		
	Customer support	Sales revenue	2,073	1,026.0%		
		Segment profit	43	430.0%		
		Profit margin	2.0%	2.0% points		
	Other	Sales revenue	1,192	35.1%	System development	App. 50% of sales revenue
		Segment profit	117	238.3%		
		Profit margin	9.8%	4.3% points	Publishing	
Consolidated	Sales revenue (Progress of full-year plan)	12,781 (76.9%)	41.2%	FY12/2018: Results Revenue 9,188 Operating profit 1,233 Net profit 796		
	Operating profit (Progress of full-year plan)	1,702 (85.1%)	38.9%			
	Profit margin	13.3%	△0.2% points			
	Net profit	1,138	34.9%	FY12/2019: Company forecasts Revenue 9,930 Operating profit 1,320 Net profit 840		
	Attributable to minority shareholders	384	33.3%			
	Attributable to parent company	754	35.8%			
Full-year forecasts by Scala	Consolidated	Sales revenue	16,600	29.4%	Profit attributable to parent company Net profit: App. 40%	
		Operating profit	2,000	29.3%		
		Profit margin	12.0%	0.0% points		
	Full-year forecasts exclude SB's impact	Net profit	1,340	26.2%	Scala's voting rights of Softbrain as of Dec. 31, 2018 50.23%	
		Attributable to minority shareholders	450	27.1%		
		Attributable to parent company	890	25.9%		

(Source) Scala's financial summary and presentation materials for institutional investors; SB's financial summary, securities report, and presentation materials for institutional investors



**Scala's  
corporate  
value at  
¥29.5 billion  
excluding  
the impact  
of SB**

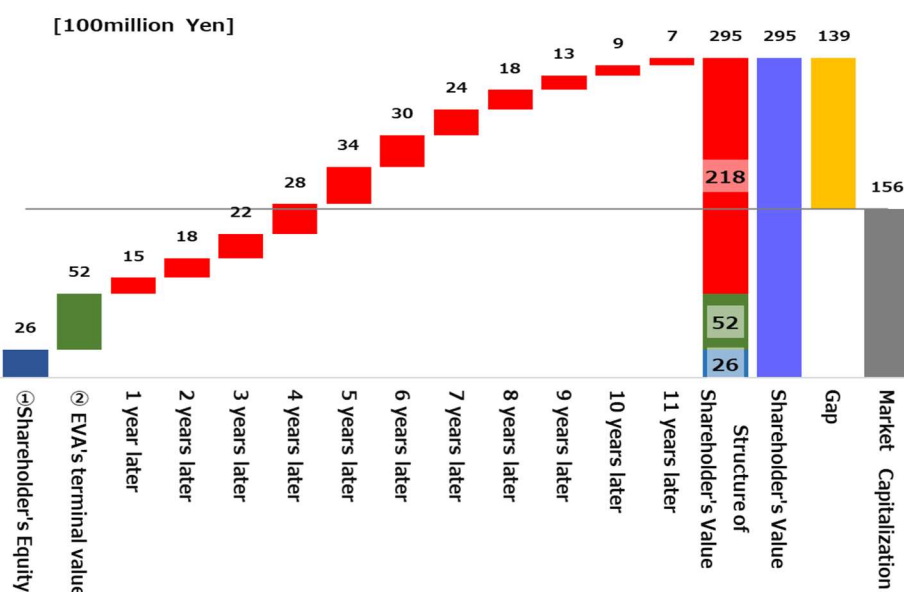
## Estimated shareholder value of Scala, excluding the impact of SB

Japan's AI market is expected to grow by 30-40%\* per year during the period of 2017 to 2022. The calculation of shareholder value is based on the assumption that Scala's business excluding SB will increase by 30% p.a. for five years since 2017 and gradually decline to zero growth in 2031, and that the ratio of invested capital excluding goodwill to sales stays at a certain level. Other assumptions and results of calculation are stated below. In sum, Scala's shareholder value is estimated to be ¥29.5 billion. As a simple assumption, the entire invested capital is considered shareholders' equity and the calculation excludes excess assets. The market cap used as for reference is based on the closing price of May 24, 2019. Other assumptions, details on the calculation method, and glossary of technical terms used in the table are available in the section "Reference material: Another way to estimate corporate value by use of ROIC and excess return."

\*See the text on page 6.

### Scala's shareholder value: assumptions and estimated results, excluding synergies with SB

	2019.06	2020.06	2021.06	2022.06	2023.06	2024.06	2025.06	2026.06	2027.06	2028.06	2029.06	2030.06	2031.06
Sales	69	89	116	151	196	255	309	354	391	419	440	455	455
Operating income	6.1	8.0	10.4	13.5	17.5	22.8	27.5	31.6	34.8	37.3	39.2	40.6	40.6
Operating margin	8.9%	8.9%	8.9%	8.9%	8.9%	8.9%	8.9%	8.9%	8.9%	8.9%	8.9%	8.9%	8.9%
Sales growth rate	57.9%	30.0%	30.0%	30.0%	30.0%	30.0%	21.0%	14.7%	10.3%	7.2%	5.0%	3.5%	0.0%
NOPAT margin	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%
Invested capital turnover ratio	37.7%	37.7%	37.7%	37.7%	37.7%	37.7%	37.7%	37.7%	37.7%	37.7%	37.7%	37.7%	37.7%
WACC	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%
ROIC = NOPAT margin ÷ invested capital net sales ratio	15.9%	15.9%	15.9%	15.9%	15.9%	15.9%	15.9%	15.9%	15.9%	15.9%	15.9%	15.9%	15.9%
ROIC / WACC (value created with the original hand of 1 y	3.0円	3.0円	3.0円	3.0円	3.0円	3.0円	3.0円	3.0円	3.0円	3.0円	3.0円	3.0円	3.0円
NOPAT	4	5	7	9	12	15	18	21	23	25	26	27	27
Invested capital × WACC	1	2	2	3	4	5	6	7	8	8	9	9	9
EVA	3	4	5	6	8	10	12	14	16	17	18	18	18
EVA = NOPAT - invested capital × WACC	3	4	5	6	8	10	12	14	16	17	18	18	18
Value created in each year	52	15	20	26	34	44	40	34	27	21	16	12	0
Discount Rate	100%	95%	90%	86%	81%	77%	73%	70%	66%	63%	60%	57%	54%
Present value of EVA	52	15	18	22	28	34	30	24	18	13	9	7	0
Invested capital ① Origin	26												
Over profit value (Permanent value of EVA of this ten	52												
Growth value (Present value of increase in EVA) ③	218												
Non-business asset value ④	0												
Corporate value = ① + ② + ③ + ④	295												
Interest-bearing debt, etc.	0												
Shareholder value	295												



On the basis of the closing price on July 29, 2019

(Source) Data from J-Phoenix Research, FactSet, Nikkei NEEDS, etc..



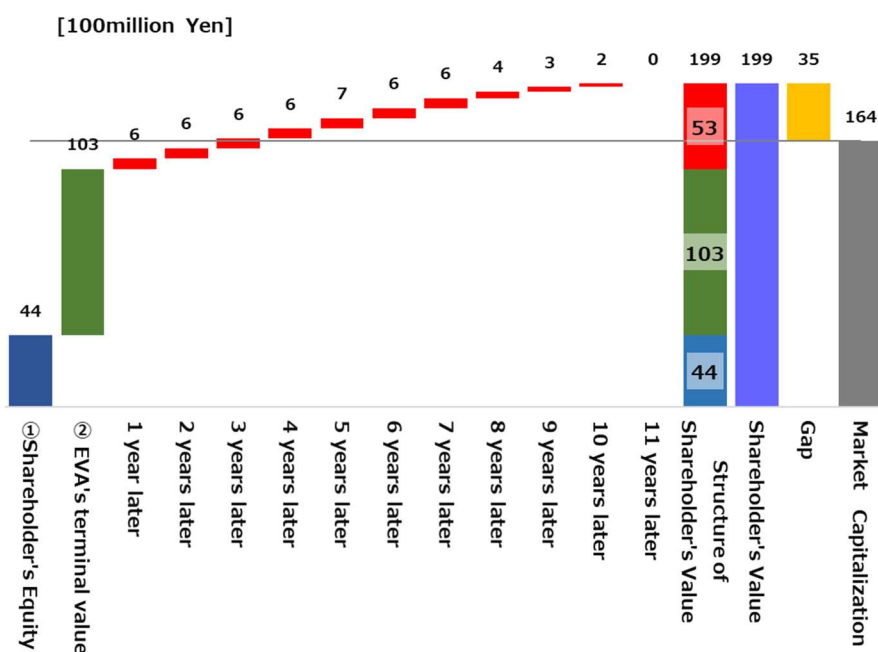
**SB's  
corporate  
value at  
¥19.9 billion  
without  
synergy with  
Scala**

## Estimated shareholder value of SB, assuming no synergy with Scala

The calculation is based on the assumption that SB should continue to grow according to the medium-term business plan: specifically, growth of 6-7% per year in the next five years, subsequent gradual decline in growth, and 0% growth after 10 years. Assumptions are that the ratio of invested capital to sales stays unchanged and operating margin stays at the same level as stated in the medium-term business plan. Other assumptions and the result of calculation are stated below. SB's shareholder value is calculated to be ¥19.9 billion.

### SB's shareholder value: assumptions and estimated results, excluding synergies with Scala

	2019.12	2020.12	2021.12	2022.12	2023.12	2024.12	2025.12	2026.12	2027.12	2028.12	2029.12	2030.12
Sales	99	106	113	120	128	137	146	156	163	168	172	172
Operating income	13.2	14.1	15.0	16.0	17.0	18.2	19.4	20.7	21.7	22.3	22.9	22.9
Operating margin	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%
Sales growth rate	8.1%	6.7%	15.0%	15.0%	15.0%	15.0%	15.0%	10.5%	7.4%	5.1%	3.6%	0.0%
NOPAT margin	9.2%	9.2%	9.2%	9.2%	9.2%	9.2%	9.2%	9.2%	9.2%	9.2%	9.2%	9.2%
Invested capital turnover ratio	21.6%	21.6%	21.6%	21.6%	21.6%	21.6%	21.6%	21.6%	21.6%	21.6%	21.6%	21.6%
WACC	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%
ROIC = NOPAT margin ÷ invested capital net sales ratio	42.5%	42.5%	42.5%	42.5%	42.5%	42.5%	42.5%	42.5%	42.5%	42.5%	42.5%	42.5%
ROIC / WACC (value created with the original hand of 1 yen)	5.8円	5.8円	5.8円	5.8円	5.8円	5.8円	5.8円	5.8円	5.8円	5.8円	5.8円	5.8円
NOPAT	9	10	10	11	12	13	13	14	15	15	16	16
Invested capital × WACC	2	2	2	2	2	2	2	2	3	3	3	3
EVA	8	8	9	9	10	10	11	12	12	13	13	13
EVA = NOPAT - invested capital × WACC	8	8	9	9	10	10	11	12	12	13	13	13
Value created in each year	103	7	7	7	8	9	9	10	7	5	4	0
Discount Rate	100%	93%	87%	81%	75%	70%	65%	61%	57%	53%	49%	46%
Present value of EVA	103	6	6	6	6	7	6	6	4	3	2	0
Invested capital ① Origin	23											
Over profit value (Permanent value of EVA of this term) ②	103											
Growth value (Present value of increase in EVA) ③	53											
Non-business asset value ④	25											
Corporate value = ① + ② + ③ + ④	203											
Interest-bearing debt, etc.	-4											
Shareholder value	199											



On the basis of the closing price on July 29, 2019

(Source) Data from J-Phoenix Research, FactSet, Nikkei NEEDS, etc.

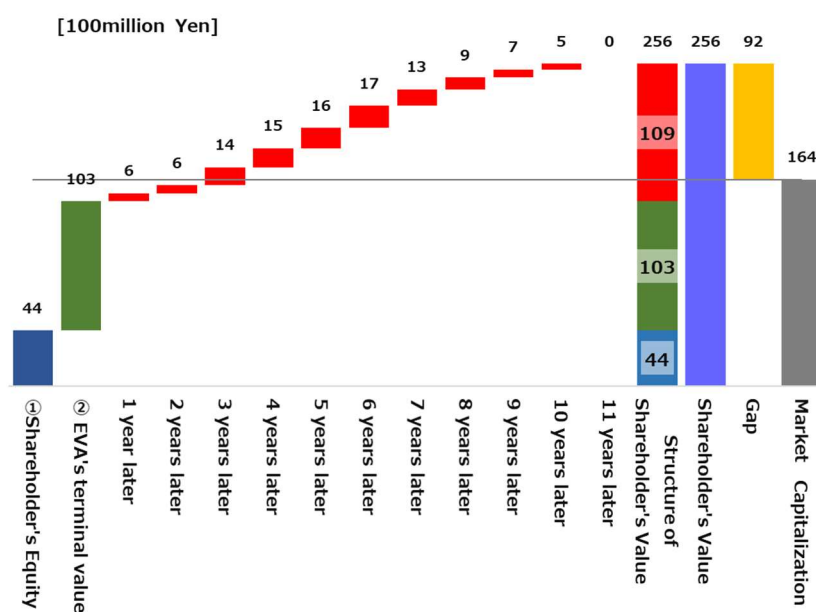
**SB's  
corporate  
value at ¥25.6  
billion with  
synergy with  
Scala**

## Estimated shareholder value of SB, with synergy effects

Assuming collaboration between Scala and SB advances, SB's growth rate may significantly improve as both companies should increase cross sales and SB can provide Scala's services to 5,000 customers in its customer network. While it is difficult to make specific estimates, based on the assumption that SB generates Scala's average sales amount of ¥7 million per customer to 1,000 of its 5,000 customers, this should boost SB's sales by ¥7.5 billion and its sales in FY12/2025 can exceed ¥20 billion. To put it in another way, if a compound annual growth rate of 15% is realized between FY12/2021 and FY12/2025, boosted by full-scale collaboration, SB's sales in FY12/2025 could reach ¥20 billion, implying SB's shareholder value of ¥25.6 billion.

### SB's shareholder value: assumptions and estimated results, including synergies with Scala

	2019.12	2020.12	2021.12	2022.12	2023.12	2024.12	2025.12	2026.12	2027.12	2028.12	2029.12	2030.12
Sales	99	106	113	130	149	172	198	218	234	247	255	255
Operating income	13.2	14.1	15.0	17.3	19.9	22.8	26.3	29.0	31.2	32.8	33.9	33.9
Operating margin	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%	13.3%
Sales growth rate	8.1%	6.7%	15.0%	15.0%	15.0%	15.0%	15.0%	10.5%	7.4%	5.1%	3.6%	0.0%
NOPAT margin	9.2%	9.2%	9.2%	9.2%	9.2%	9.2%	9.2%	9.2%	9.2%	9.2%	9.2%	9.2%
Invested capital turnover ratio	21.6%	21.6%	21.6%	21.6%	21.6%	21.6%	21.6%	21.6%	21.6%	21.6%	21.6%	21.6%
WACC	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%	7.3%
ROIC = NOPAT margin ÷ invested capital net sales ratio	42.5%	42.5%	42.5%	42.5%	42.5%	42.5%	42.5%	42.5%	42.5%	42.5%	42.5%	42.5%
ROIC / WACC (value created with the original hand of 1 yen)	5.8円	5.8円	5.8円	5.8円	5.8円	5.8円	5.8円	5.8円	5.8円	5.8円	5.8円	5.8円
NOPAT	9	10	10	12	14	16	18	20	22	23	23	23
Invested capital × WACC	2	2	2	2	2	3	3	3	4	4	4	4
EVA	8	8	9	10	11	13	15	17	18	19	19	19
EVA = NOPAT - invested capital × WACC	8	8	9	10	11	13	15	17	18	19	19	19
Value created in each year	103	7	7	18	20	23	27	21	17	12	9	0
Discount Rate	100%	93%	87%	81%	75%	70%	65%	61%	57%	53%	49%	46%
Present value of EVA	103	6	6	14	15	16	17	13	9	7	5	0
Invested capital ① Origin	23											
Over profit value (Permanent value of EVA of this term) ②	103											
Growth value (Present value of increase in EVA) ③	109											
Non-business asset value ④	25											
Corporate value = ① + ② + ③ + ④	260											
Interest-bearing debt, etc.	-4											
Shareholder value	256											



On the basis of the closing price on July 29, 2019

(Source) Data from J-Phoenix Research, FactSet, Nikkei NEEDS, etc.

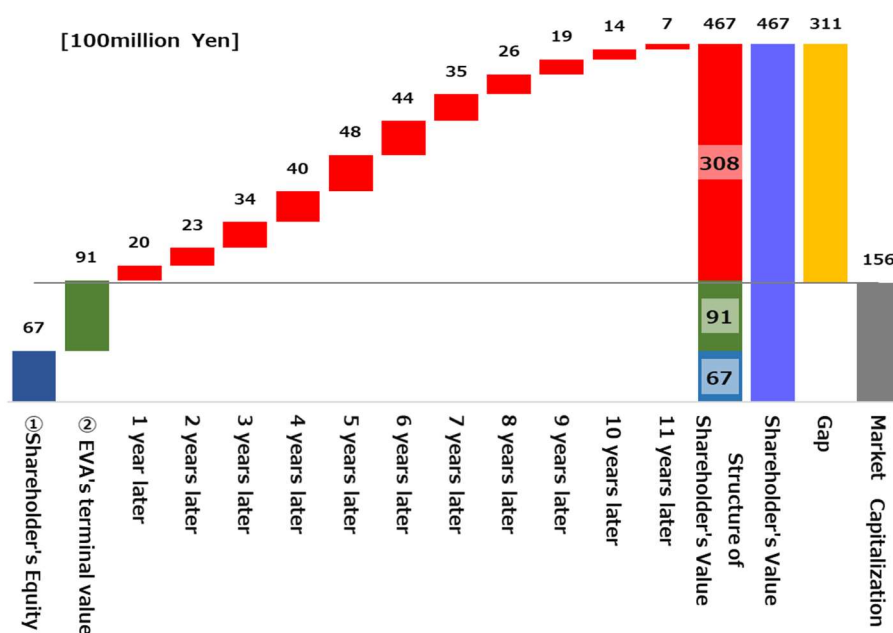
**Scala's  
corporate  
value  
estimated at  
¥42.0-46.7  
billion**

## Calculation incorporating only the value attributable to the parent company's equity

Next, Scala's consolidated-based shareholder value is calculated by evaluating Scala's shareholder value which excludes the impact of SB, and Scala's portion of SB's value based on its voting rights of SB at Scala's capital cost. Scala's shareholder value with synergy impact is calculated as ¥46.7 billion (Scala's shareholder value ex. SB of ¥29.5 billion and Scala's equity-portion value of SB of ¥17.2 billion. The latter is evaluated higher as Scala aggressively uses debt and its capital cost is higher.) In the meantime, Scala's shareholder value without synergy impact is estimated to be ¥42.0 billion. This suggests that Scala's upside potential is about three times its market cap of ¥13.8 billion as of May 24, 2019.

### Scala's shareholder value: assumptions and estimated results, including synergies with SB

	2019.06	2020.06	2021.06	2022.06	2023.06	2024.06	2025.06	2026.06	2027.06	2028.06	2029.06	2030.06	2031.06
Sales	166	193	227	278	343	424	502	568	620	660	690	706	706
Operating income	20.0	22.8	26.1	31.6	38.4	46.8	55.1	62.1	67.6	71.8	74.9	76.3	76.3
Operating margin	12.0%	11.8%	11.5%	11.4%	11.2%	11.0%	11.0%	10.9%	10.9%	10.9%	10.9%	10.8%	10.8%
Sales growth rate	29.7%	16.4%	17.4%	22.7%	23.1%	23.6%	18.6%	13.1%	9.2%	6.4%	4.5%	2.2%	0.0%
NOPAT margin	5.2%	5.3%	5.3%	5.4%	5.4%	5.5%	5.5%	5.5%	5.5%	5.5%	5.5%	5.5%	5.5%
Invested capital turnover ratio	43.7%	42.0%	40.5%	38.4%	36.8%	35.6%	34.6%	34.0%	33.6%	33.4%	33.2%	33.3%	33.3%
WACC	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%
ROIC = NOPAT margin ÷ invested capital net sales ratio	11.9%	12.6%	13.2%	14.0%	14.7%	15.4%	15.9%	16.2%	16.4%	16.5%	16.6%	16.6%	16.6%
ROIC / WACC (value created with the original hand of 1 yen)	2.3円	2.4円	2.5円	2.7円	2.8円	2.9円	3.0円	3.1円	3.1円	3.1円	3.1円	3.1円	3.1円
NOPAT	9	10	12	15	19	23	28	31	34	36	38	39	39
Invested capital × WACC	4	4	5	6	7	8	9	10	11	12	12	12	14
EVA	5	6	7	9	12	15	18	21	23	25	26	27	25
EVA = NOPAT - invested capital × WACC	5	6	7	9	12	15	18	21	23	25	26	27	25
Value created in each year	91	21	26	39	49	61	60	50	40	30	23	12	-28
Discount Rate	100%	95%	90%	86%	81%	77%	73%	70%	66%	63%	60%	57%	54%
Present value of EVA		91	20	23	34	40	48	44	35	26	19	14	7
Invested capital ① Origin		117											
Over profit value (Permanent value of EVA of this term) →		91											
Growth value (Present value of increase in EVA) ③			308										
Non-business asset value ④			55										
Corporate value = ① + ② + ③ + ④			572										
Interest-bearing debt, etc.			-105										
Shareholder value			467										



On the basis of the closing price on July 29, 2019

(Source) Data from J-Phoenix Research, FactSet, Nikkei NEEDS, etc..

## 2. Evaluation by the GCC management<sup>®</sup> framework

### Evaluating by the GCC management framework

### Combining Maslow's five-tier human needs and the corporate value's three elements

### What is an analytical framework of the GCC management<sup>®</sup>?

**Integrating financial and non-financial information that capture the hearts and minds of all stakeholders**

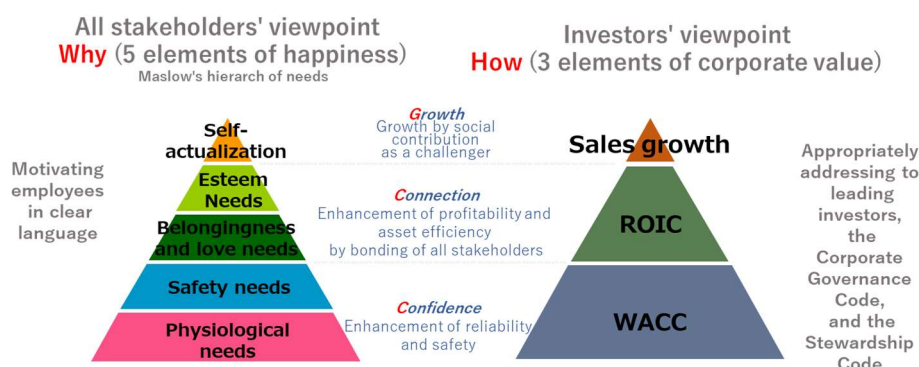
The GCC management<sup>®</sup> is an analytical framework developed by J-Phoenix Research in order to evaluate sustainability of shareholder value by integrating non-financial information and financial information with a focus on the happiness of all stakeholders. Happiness of investors is measured by a framework of three elements of corporate value, while happiness of employees is measured by the five-tier model of human needs, created by Abraham Maslow, a prominent American psychologist. People can feel happy when their five needs are satisfied. For example, a company with a built-in framework to raise happiness of employees should be determined as more sustainable than a company with the same shareholder value but without this framework.

The concepts that associate the five levels of needs with the three factors of corporate value are Growth (in sales), Connection (of people and businesses, leading to improve Return on Invested Capital), and Confidence. JPR has defined "Excess return generated from a strategy that incorporates the enhancement of happiness of all employees under the GCC concept" as Happiness Value Added<sup>®</sup>.

The enhancement of happiness is "why such a company exists," the raison d'être of a company, while the viewpoint of corporate value is "how the enhancement of happiness is associated with its value." Use of this framework makes it easy to explain the concept of creating corporate value to its employees. Moreover, this facilitates disclosure of non-financial information, which is required for complying with the Stewardship Code. It also facilitates (1) integration of financial and non-financial information, (2) management in consideration of ROIC and capital costs (addressing corporate governance), and (3) systemization and visualization in coping with ESG and SDGs\*.

\* Environment, Social, and Governance (ESG) has been globally increasingly recognized as three indispensable viewpoints for long-term growth of companies. Social Development Goals (SDGs) were adopted at the United Nations Summit in September 2015 by 193 member countries to be achieved in 15 years from 2016 to 2030. Attaching importance on both ESG and SDGs, long-term investors are anticipated to increase investment in listed companies which are highly evaluated in these viewpoints.

### Analysis of creating corporate value that becomes established in the minds of all stakeholders, using the GCC management<sup>®</sup>



#### The following elements are also incorporated:

- (1) Integration of financial and non-financial information;
- (2) management being conscious of ROIC and capital costs (addressing corporate governance);
- (3) systemization and visualization in coping with ESG and SDGs

**Maximizing Happiness Value Added<sup>®</sup>**

(Source) J-Phoenix Research



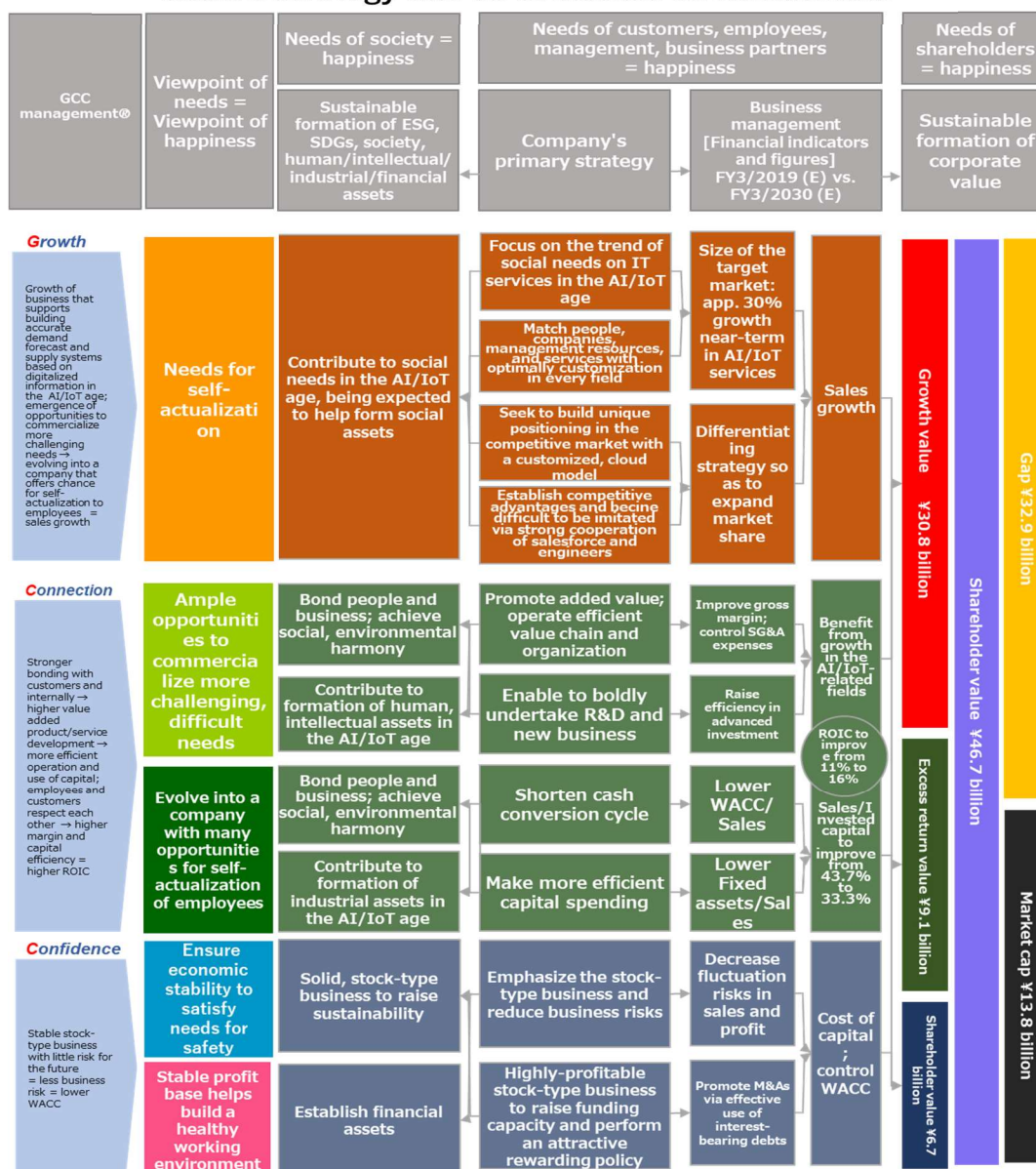
The analysis of Scala's strategy using the GCC management<sup>®</sup> analytical framework is shown below. Scala's strategy appears to be highly sustainable, seeking a virtuous cycle of raising happiness and corporate value.

## Evaluating Scala from the GCC management<sup>®</sup> framework: Strength in creating highly sustainable corporate value



Development of Happiness Value Added<sup>®</sup>

Scala's analysis:  
Its strategy to improve happiness of  
all stakeholders and corporate value can be comprehensively organized  
**Scala's strategy can be evaluated as sustainable**



(Source) J-Phoenix Research

### 3. Corporate Summary and History

#### Corporate Data

Corporate name	Scala, Inc.
Established	December 11, 1991
Representative	Norikatsu Nagino
Location	Ebisu Prime Square Tower, 1-1-39, Hiroo, Shibuya-ku, Tokyo, 150-0012 Japan
Capital	1,604 million yen
Fiscal year end	June
Listing	Tokyo Stock Exchange First Section [4845]
Employees	487 (as of December 31, 2018; consolidated base) Full-time and contracted employees only

(Source) Prepared by J-Phoenix Research based on corporate materials

#### Corporate group organization (as of March 31, 2019)



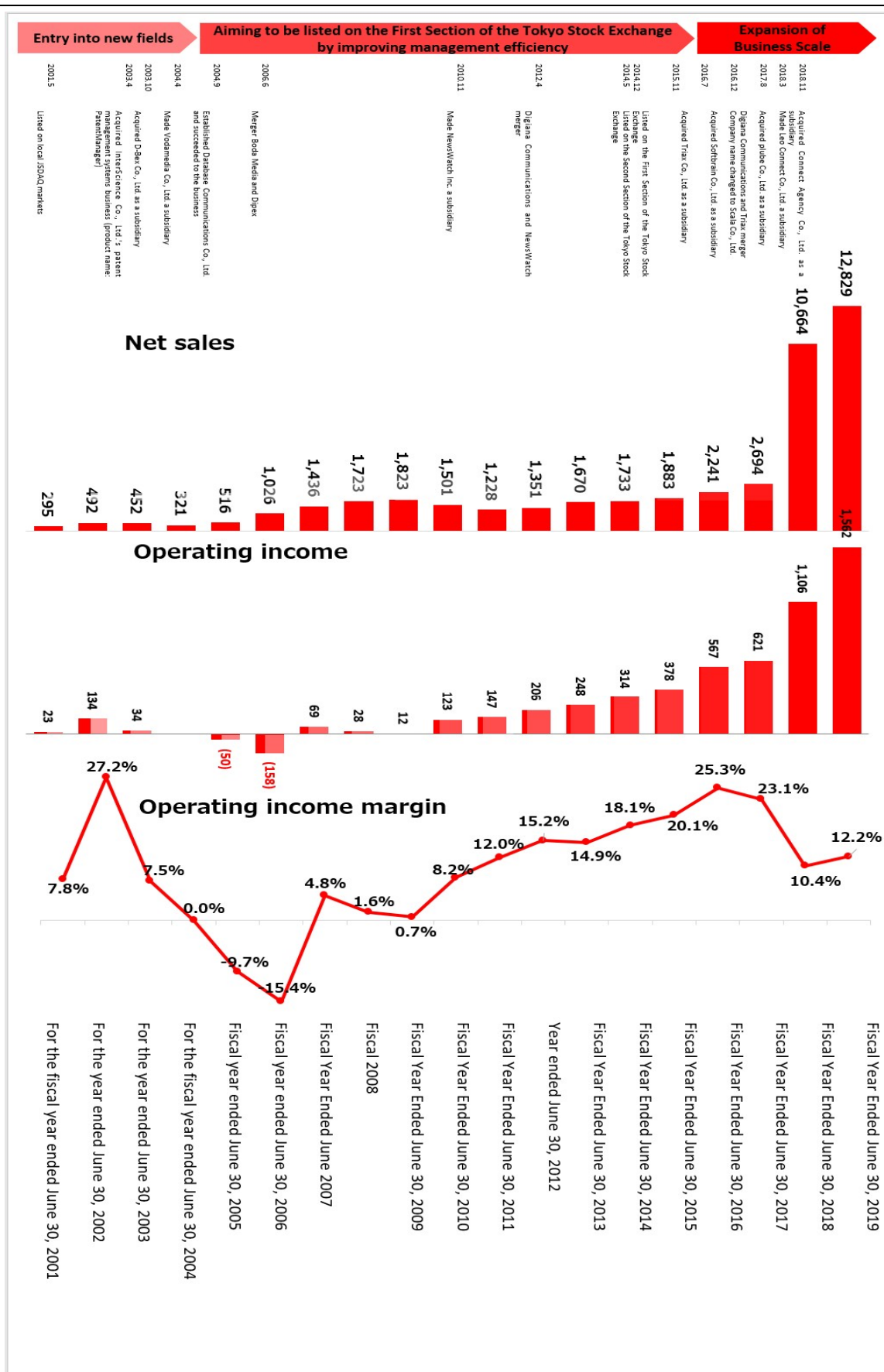
(Source) Prepared by J-Phoenix Research based on corporate materials

#### History

Dec. 1991	Kenzo Tamura and Hideki Shimazu founded Database Communications (now, Scala, Inc.)
Jan. 1999	Formed sales agency contracts for the Japanese market with US-based Computer Corporation of America and Sirius Software and started Model 204 support
May 2001	Listed on the Osaka Securities Exchange's NASDAQ Japan market (now, TSE JASDAQ (Standard))
Apr. 2003	Acquired the patent management software (product name; PatentManager) of Interscience Co., Ltd. with the aim of entering the patent management system field
Oct. 2003	Acquired Dbecs Co., Ltd. as a subsidiary to enter the CRM field
Apr. 2004	Acquired Vodamedia Inc. as a subsidiary with the aim of entering the IVR (interactive voice response) field)
Sep. 2004	Renamed as Fusion Partners, Co. in the transition to a holding company structure and established Database Communications (now, Scala Services Inc.) as a new company and transferred its business
June 2006	Merged subsidiaries Vodamedia and Dbecs and renamed it to Digi-Ana Communications Inc. (now, Scala Communications Inc.)
Nov. 2010	Acquired NewsWatch Inc. as a subsidiary
Apr. 2012	Merged subsidiaries Digi-Ana Communications and NewsWatch (now, Scala Communications Inc.)
Aug. 2013	Norikatsu Nagino was appointed as Representative Director and President
May 2014	Listing transferred to the TSE Second Section
Dec. 2014	Elevated to the TSE First Section
Nov. 2015	Acquired TriAx Corp. as a subsidiary
Jan. 2016	Renamed subsidiary Database Communications as PAREL, Inc. (now, Scala Services Inc.)
July 2016	Acquired Softbrain Co., Ltd. as a subsidiary
Dec. 2016	Changed the corporate name to Scala, Inc.
Dec. 2016	Merged subsidiaries Digi-Ana Communications and TriAx and renamed it to Scala Communications Inc.
Apr. 2017	Scala Services began operation
Aug. 2017	Acquired plube Co., Ltd. as a subsidiary
Mar. 2018	Acquired Leoconnect, Inc. as a subsidiary
Nov. 2018	Acquired Connect Agency Inc. as a subsidiary
Nov. 2018	Established Scala Next, Inc.
Dec. 2018	Established the Mandalay Branch (Myanmar) of Scala Next, Inc.

(Source) Prepared by J-Phoenix Research based on corporate materials

## Scala's long-term business results since its listing in 2001



(Source) Prepared by J-Phoenix Research based on the data from corporate materials, FactSet, Nikkei NEEDS, etc.

## History of growth driven by M&As

M&As of the last three years boosted revenue by about 5 times and operating profit by about 2.5 times

### Business development since foundation

**Transformed into a comprehensive IT service company, committed to satisfy customers' needs and requests**

Scala was founded in December 1991 as a sales distributor of database services. In 2000, as corporate information systems were migrated from mainframes to small-scale decentralized-processing servers, it determined that it needed to change its business structure and started to expand its business through M&As, utilizing funds procured by its stock listing in 2001. Since the early 2000's, Scala has acquired numerous businesses and companies and has become a sophisticated, comprehensive IT service company, committed to satisfy customers' needs and requests. Over the course of its growth, Scala has established a unique business model with recurring (stock-type) income and a service structure with customized products and services to be developed in a short term.

### Rapid expansion in business scale in the last three years, driven by large-scale acquisitions

**Increase of 5 times in sales revenue and 2.5 times in operating profit, from FY6/2016 to FY6/2018**

Since 2015, Scala has accelerated expansion of business lines through M&As. Sales revenue surged by about five times from ¥2.6 billion in FY6/2016 to ¥12.8 billion in FY6/2018, while operating profit increased by about 2.5 times from ¥0.6 billion in FY6/2016 to ¥1.5 billion in FY6/2018.

#### Acquisition of SB: Significant contribution in business scale

In particular, Scala's acquisition of SB in July 2016 had a significant impact in expanding its size. Scala acquired SB and made it a subsidiary within a short period through market transaction, without making any negotiated transaction which would have been subject to TOB regulations. As of December 2018, Scala owns a 47.7% stake of SB, which recorded sales of ¥9.1 billion and operating profit of ¥1.24 billion in FY12/2018.

#### Acquisition of plube: A strategic move to B-to-C

Scala has been engaged in B2B business, but in 2018, they acquired plube Co., which is engaged in managing an EC website for buying and selling trading cards, and started a B2C business. This was the first move for Scala to develop in the area of B2C business.

#### Acquisition of two strategic businesses of Hikari Tsushin (TSE First Section 9435)

In 2018, Scala acquired two subsidiaries of Hikari Tsushin, Inc. (TSE First Section 9435), which sells various types of products that collect charges on an ongoing basis for corporate customers. They are Leoconnect Inc., which provides consulting services to call centers, and Connect Agency Inc., which was created from Hikari Tsushin's one-stop IP telephone service department that provided a charging function by second and a recording function of all calls to the Hikari Tsushin Group companies. In addition to expecting to generate synergies with Scala, both acquired companies have Hikari Tsushin as their customer and will therefore benefit from high growth of Hikari Tsushin. Scala may also be allowed to access to Hikari Tsushin's corporate customers.



## ■ Major acquisition of the last three years

### Acquisition of Softbrain Co., Ltd.: July 2016

Sales growth	Sales growth by making this listed company a consolidated subsidiary. Softbrain has many blue-chip customers and stable business growth with little risk of sharp deterioration in business
Profitability	Efficient use of mutual business assets, including customer base, services, and know-how to raise organizational efficiency
Invested capital	Aim to combine Scala's strong technology in website action record analysis with SB's sales support software
Business risk	Possibility of unfavorable impact to the stock price, as it became Scala's subsidiary via a hostile takeover.

(Source) Prepared by J-Phoenix Research based on corporate materials and interviews

### Acquisition of plube Co., Ltd.: August 2017

Sales growth	The entry to the app. ¥100 billion trading card market means to bring in a source of cash, which is not sensitive to a single industry's economic condition.
Profitability	Anticipate synergy with shipping agency business and field marketing, and with existing services (i.e., customer support)
Invested capital	Aim to raise operational efficiency of its online card shop Yuyutei
Business risk	The trading card game market is at a matured stage (risk of the market to shrink)

(Source) Prepared by J-Phoenix Research based on corporate materials and interviews

### Acquisition of Leoconnect Inc.: March 2018

Sales growth	The unique know-how, accumulated through a vast number of projects and operations, can be sold to outside customers, in addition to the existing customers of Hikari Tsushin group companies
Profitability	Raise added value in services by evolving into an inbound center of a consulting proposal type, using Voice of Customer (VOC) big data
Invested capital	Leoconnect's customer support consulting services to collaborate with Scala's call center-related IT services, so as to improve quality of response at customer help desk.
Business risk	Decline of the call center operation (shift into alternative ways, such as the Chatbot)

(Source) Prepared by J-Phoenix Research based on corporate materials and interviews

### Acquisition of Connect Agency Inc.: November 2018

Sales growth	Established from the one-stop IP telephone service department. It has functions of billing by second and recording of all calls, which are provided to Hikari Tsushin group companies. Will benefit from high growth of the Hikari Tsushin Group
Profitability	Anticipate business synergy from cross selling of Scala's call center-related IT services and Connect Agency's IP telephone services
Invested capital	Expect business synergy to enable more efficient use of invested capital
Business risk	Technological obsolescence

(Source) Prepared by J-Phoenix Research based on corporate materials and interviews

## 4. A noteworthy pattern of success and a potential future growth scenario

A successful model of capturing a large project, a key to Scala's future

Strength in building a strong relationship and in solution-type sales to lead from a small business to a large project

### Noteworthy pattern of horizontally developing successful businesses with large corporate customers

#### Example of business with Sompo Japan Nipponkoa Insurance

Sompo Japan Nipponkoa Insurance Inc. has been a customer of Scala, initially for its main service i-search\*. Scala has since established a good relationship with the company, providing consultation as a part of sales efforts, introducing tens of its services, and asking more opportunities to offer services. It is during the time that Sompo Japan and Nipponkoa were in the midst of merger procedures and were planning to launch a new safe-driving assistance service, Smiling Road. As a background, transportation companies, in particular, had a high rate of accidents caused by their drivers and were in desperate need of a system for managing drivers. For developing and moving ahead of its competitors with a new service involving installation of a drive recorder and other devices to prevent accidents -- reduce insurance premiums -- the speedy development in the initial phase as well as continuous additions of functions were requisites. Receiving an inquiry from Sompo Japan Nipponkoa Insurance, Scala developed the customized service that precisely satisfied their needs. This business resulted in generating sales revenue of ¥400-500 million per year for Scala and making Sompo Japan Nipponkoa Insurance one of Scala's major customers. This is a successful business example, attributable to Scala's technology and response capacity in managing big data for a major company and to its strength in marketing and sales to uncover previously unrecognized needs.

Such needs in customization are expected to increase in the age of AI/IoT. At present Scala's average SaaS/ASP cloud service revenue per corporate customer is around ¥6-7 million but potential revenue is expected to expand significantly as their customers tend to be big companies and most are listed in the stock market.

\* i-search is a website search service within a corporate website to enable users find contents or web page on their own from a keyword.

■ **Successful scenario to expand business with a large company to generate ¥400-500 million in sales**



(Source) Prepared by J-Phoenix Research, based on corporate materials and interviews

## 4. Business segments

Five businesses that facilitates smooth communication between companies and consumer

Provision of companies' customized communication tool with their customers

### Summary of major businesses

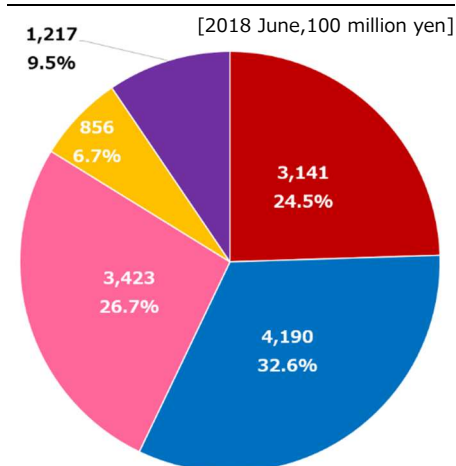
The Scala Group is engaged in the following five business segments.

#### Scala's business segments

Business segment	Description of business
SaaS/ASP business	Provision of SaaS/ASP-type services that use automated voice technologies of the browser, telephone, fax, etc. over the Internet or telephone lines
SFA business	Provision of services, such as the licensing of the sales support system, cloud services, customized development, marketing consulting, marketing skill training, and operation consulting and education by using iPad and other tools
Field marketing business	Provision of services related to field activities, marketing research, etc.
Customer support business	Provision of one-stop consulting services related to customer supports, such as call center operations and diverse BPOs
Other business	Provision of the EC website for buying and selling battle-type trading cards; contracted development of software; publishing of business-related books, etc.

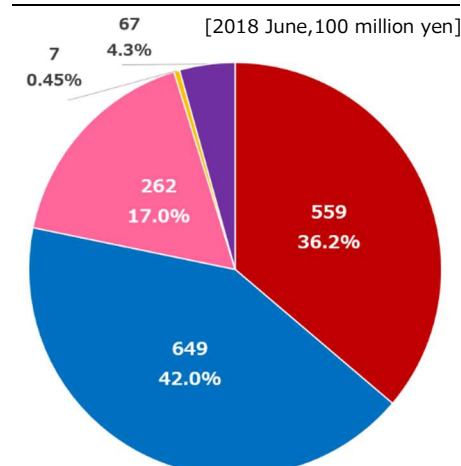
(Source) FY6/2018 Securities Report

#### Sales revenues by segment



■ SaaS/ASP ■ SFA ■ field marketing ■ support services ■ publishing marketing

#### Operating profit by segment



(Source) Prepared by J-Phoenix Research from FY6/2018 results briefings material

### SaaS/ASP business: Current status

#### Business outline and the trend of major services

This segment provides SaaS/ASP-type services that use automated voice technologies of the Web, telephone, fax machines, etc. over the Internet or telephone lines. The services enable customers to use applications via the Internet or telephone lines without making any large-scale capital investment.

Major products are the i-search website search engine that offers better visibility by displaying images in search results and provides effective guidance to users; the i-ask system that allows users to resolve issues on their own by listing frequently asked questions in advance within a corporate website; and the Interactive Voice Response (IVR) system for voice-based automated response at corporate phone help desks. As services are related to IoT and big data, the segment provides processing and management services of big data for Smiling Road, a safe-driving assistance service sold by Sompo Japan Nipponkoa Insurance.

## High growth in main services

The SaaS/ASP business segment's products and sales trend are shown below. In sum, the segment provides comprehensive services related to all kinds of communication tools of corporate customers.

### List of services of the SaaS/ASP business segment

Type	Product name	Description
Site assistance service	i-search	Site internal search engine
	i-linkcheck	Broken link detection system
	i-print	Site print system
	i-linkplus	Related link display service
CMS service	i-ask	FAQ system
	i-catalog	Product site management system
	i-learning	e-learning system
	i-flow	Progress management/approval system
CRM service	LaCoon	Web system architecture platform
	i-entry	Comprehensive questionnaire CRM service
	Dbecs	High-performance web mailer
	i-assist	Virtual assistance
	i-livechat	Web chat system
Telephone system service	i-gift	Digital gift service
	SaaS-type IVR	24-hour, 365-day automated voice response service
News distribution service	Corporate news	Important business information checking
Data management	Patent Manager 6	Latest patent management system
	Grip Manager	Contracted work management system
Site management business	Fresheye	Search portal site
IoT and big data	Safe driving analysis	Handling and control of big data
SFA business	e-sales manager	Sales support system
Field marketing business	Field activities/research	Market research and shop field activities
EC business	Online card shop	Online sales and trading of trading cards and related products
Customer support business	Contact Center	Customer support consulting

(Source) Prepared by J-Phoenix Research from FY6/2018 results briefings material

### SaaS/ASP business: sales trend and highlights in FY6/2018

The sales breakdown of the SaaS/ASP business in FY6/2018 is as follows.

### SaaS/ASP business: sales composition

(100 million yen)	June 2017	June 2018	Growth	Growth rate	
i-search	409	457	+48	+11.8%	
i-ask	356	450	+94	+26.3%	
i-entry	104	101	-3	-2.8%	
Chatbot	426	467	+41	+9.5%	
Big data processing	337	487	+150	+44.5%	
Contact center	263	273	+10	+3.8%	
News distribution	421	430	+9	+2.2%	
EC site	488	473	-15	-3.1%	
Total	2,807	3,141	+334	+11.9%	

(Source) FY6/2018 results briefings material



**Growth potential in sales by increasing projects such as for Sampo Japan**

**Introduction of a minimum package to lower the barrier for initial adoption**

## **Differentiated business model**

**Customized service structure enabled by sticking to direct sales**

**Customer-first products, offered only by Scala**

**Development of customers with a small “hook” service**

**A small “hook” service is a ticket to enter and provide more products**

**Capturing of regular needs results in a high rate of long-term usage service**

Major services have rapidly grown in the last few years. This robust growth features an increase in sales related to IoT and big data of 44.5% year-on-year to around 500 million yen, although this service is provided only to Sampo Japan Nipponkoa Insurance. This shows that Scala’s sales per customer, which is less than ¥10 million on average at present, can be higher than ¥100 million if Scala successfully develops similar large-scale service to other companies.

### **Sales growth potential: customization to satisfy a range of needs**

Scala generates 80% of revenue from direct sales. Its salesperson identifies the needs of each customer and customizes the basic package to satisfy the customer’s needs. Through this customization, Scala can uncover potential needs on top of existing ones, and thereby propose new services.

### **Differentiated business model from competitors**

Scala provides customized services despite being in the SaaS/ASP business. This has been realized because Scala carefully listens to customers, ascertains their needs, and customizes its services. In contrast, conventional SaaS/ASP providers only offer standard services. This greatly differentiates Scala from its competitors. This business model has also been enabled by being committed to direct sales, which represent 80% of revenue. Scala’s basic policy is that its sales person visits a customer for direct sales and arranges a meeting for an actual user to directly talk with a Scala engineer, which results in accurately finding out the customer’s needs and providing right solutions.

### **Scala’s services not competing with other companies’ services**

Scala’s representative services include i-search and i-ask. The latter is a FAQ system and major companies, including Oracle and OKWAVE, offer similar services. At the time of creating a new service, a common practice might be to study functions offered by forerunners such as OKWAVE and Oracle and to try to excel them. This, however, would cost a significant amount for development and a new company cannot easily catch up with frontrunners who are committed to grow further. Scala’s approach is different: Scala starts customizing its service even with less functions initially than its forerunners, and prioritizes customers, rather than products. This allows Scala to be free of competing with other companies’ services and contain cost at a low level.

### **Expansion from a small “hook” service to a wide range of services**

Scala positions i-search and i-ask as broad-based introductory service to attract customers’ interest. While sales of these two services may be limited, customers using these products may find Scala’s offerings to be attractive, and be inclined to use Scala again when the next business opportunity emerges. A representative example is Sampo Japan Nipponkoa Insurance, which initially used i-search and is now using about 60 services of Scala, with its monthly billing amounting to several tens of millions of yen.

### **A high rate of long-term usage leads to realization of a stock-type business and stable profit**

Scala’s sales people make repeated visits to a customer even after the initial service development phase, and learn of and promptly respond to any dissatisfaction of the customer in each occasion, raising the level of customer satisfaction and resulting in the long use of Scala’s services by the customer.

### **Diversified services to raise customer satisfaction**

By responding to requests of many customers, Scala has accumulated know-how and has realized a diversity of service line-ups at low cost. The combination of multiple services and cross-selling enables Scala to raise both the average transaction per customer and customer satisfaction. In addition, Scala is aggressively striving for provision of unprecedented services in responding to difficult needs to be addressed by big companies with fragmented departments.

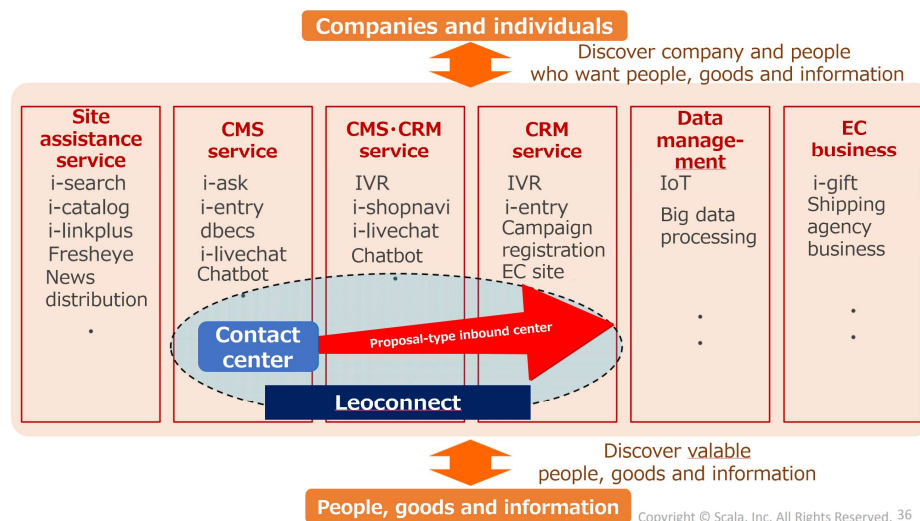
## Provision of services related to all communication tools of customers

## Ceaseless evolution and development

### SaaS/ASP business: Direction of strategy

#### Future direction

Scala will expand the SaaS/ASP business, aiming at timely providing information and goods needed based on IT services that help communications of companies and individuals



(Source) FY6/2018 results briefings material

### SaaS/ASP to further advance and develop

Scala is acquiring the industry's leading market share in website search (with i-search), website FAQ systems (with i-ask), and IVR automated voice response systems. With the aim of promoting active use of these important services for corporate marketing or as communication tools with users, Scala intends to further improve services and develop more and better services that satisfy needs of companies, with Customer Relationship Management (CRM) and Content Management System (CMS) as main service.

**Provides  
services  
that make  
use of  
cutting-  
edge**

**No. 1 in  
comprehensive  
customer  
satisfaction in  
CRM/SFA**

## SFA business: Current status

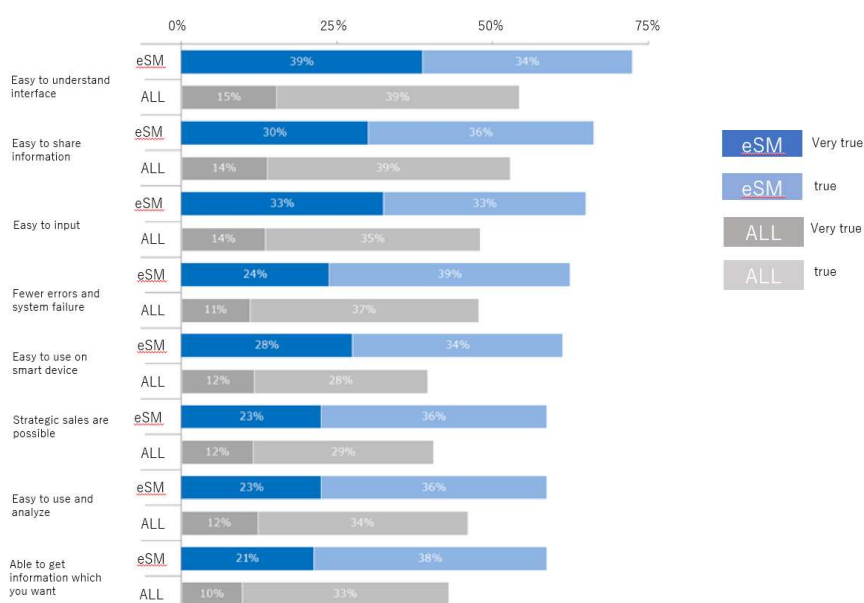
### Sales growth potential: No. 1 in comprehensive customer satisfaction in CRM/SFA

Scala provides services that always make use of cutting-edge devices under the development concept of “No. 1 CRM/SFA<sup>1</sup> in terms of usability.” As a result, Scala won the No. 1 in usability, operational improvement, effect of introduction, service satisfaction, and system satisfaction in the most recent CRM/SFA user survey. It was awarded No. 1<sup>2</sup> CRM/SFA in terms of the comprehensive satisfaction level.

1: Sales Force Automation (SFA)

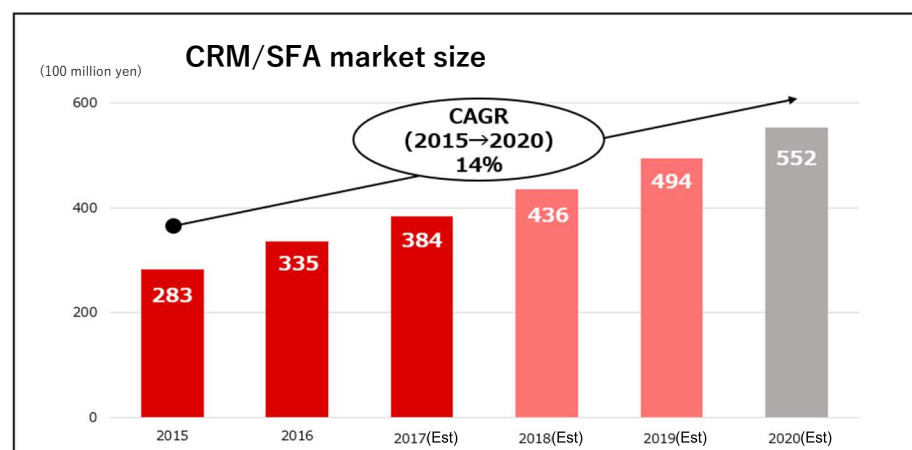
2: Surveyed by ESP Research Institute, Inc. in May 2018, targeting men and women of the 20's – 60's brackets; corporate owners, executives of companies and organizations, and employees of companies and organizations (including dispatched and contracted workers); 300 users of CRM/SFA; web-based questionnaire

### No. 1 in comprehensive customer satisfaction in CRM/SFA



(Source) Scala's medium-term business plan presentation material, 1/30/2018

### Japan's SFA market size



(Source) Scala's medium-term business plan presentation material, 1/30/2018

More than 5,000 corporate customers in a diverse range of scale, industry, and business categories

The CRM/SFA market is expected to grow by 14% per year. At present, only about 15% of targeted large companies and major medium-sized companies has so far adopted CRM and SFA.

### No.1\* Japanese vendor

Scala has more than 5,000 corporate customers in a diverse range of scale, industry, and business categories. Based on the solid knowhow accumulated from many of those services, Scala is able to provide appropriate solutions to customers' sales issues.

\* SB's estimate, based on IDC "Market shares of Japan's CRM application market, 2017"

### Major customers in the SFA business



Company names and logos are registered trademarks or trademarks of their respective companies. Only some of the customers who kindly agreed are listed.

(Source) Scala's website



**Flexible  
employment style  
and data  
collection  
to respond  
to the  
changing  
business  
environment**

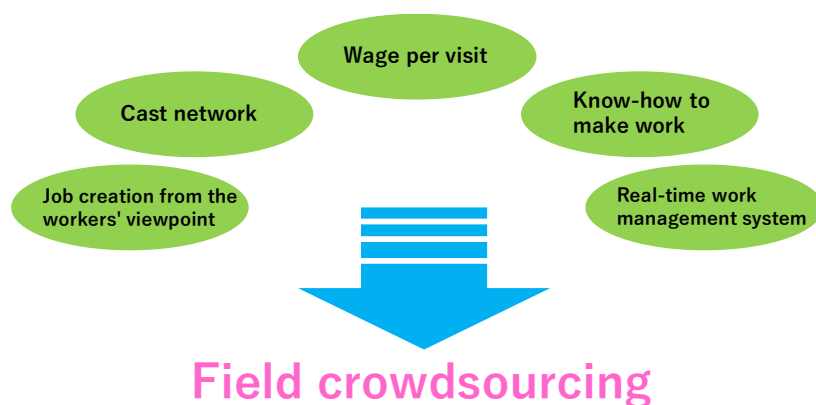
**256,567 “casts” who  
like Softbrain Field’s  
consumer-friendly  
workstyle conduct  
sales support and  
market research**

## Field marketing business: Current status

### Focus on the “fields,” in response to the changing business environment

This segment is mainly operated by Softbrain Field Co., Ltd. and uses registered staff nationwide in sales support and market research. Based on the data accumulated from various parts of Japan by use of mystery shoppers, in-store surveys, and other means, Scala is in fact engaged in sales promotion and proxy sales services in addition to assisting in sales and personnel hiring, so that its corporate customers can respond to ever-changing business environment.

#### What is the Field Crowdsourcing?



**The know-how and cast network of Softbrain Field are in need in all "fields" (meaning "points of contact with consumers")**

(Source) Softbrain Field's website

### Unique business model with a flexible employment system

The field marketing business considers its staff as consumers and creates jobs that are remarkable for facilitating a friendly workstyle. This workstyle can be said to embody the concept of doing work you like, as much as you like, wherever you like, and whenever you like. The total of 256,567 “casts” across Japan (as of 2018), who have empathized with the concept, comprise the cast network, forming a unique business model, “Field Crowdsourcing.”

What is particularly unique, is to use housewives, who are conventionally regarded as consumers, as competent human resources with shrewd consumer know-how, which is valuable to service providers. Housewives in Japan are also receiving more attention as a segment of the workforce to fill in labor shortage.

#### Characteristics of “casts”

**Hiring of  
housewives to  
connect companies  
with consumers**

**Collaboration  
with a  
subsidiary to  
provide one-  
stop solution  
for call  
center  
operation**

**Collaboration with a  
subsidiary to  
develop proposal-  
type inbound call  
centers**



Key person of consumer activities

Casts have a daily life as a consumer with shrewd consumer views on products and services



Core of the local community

Casts socialize with diverse people in the community and understand unique issues and needs of the community



Work experience

Casts have a corporate work experience, good business manner and common sense, and are eager to accomplish their assigned work.

(Source) Softbrain Field's website

## Field marketing business: Direction of strategy

**A bridge between companies and consumers, contributing to a more active community**

Softbrain Field creates jobs for housewives, as main registered staff of its Cast Network, in their daily living area, which results in establishing a network mainly of consumers in the local community. Subsequently, this will energize local businesses and connect the Cast Network with local companies that provide products and services to consumers. Such a chain of development aligns well with Scala's direction of timely providing information and services needed based on information accumulated, allowing Scala an overview extending to the end of a supply chain.

## Customer support business: Current status

**One-stop solutions provided by specialists and Scala's tools**

This segment is operated by Leoconnect, a subsidiary of Scala, under contracted business from the Hikari Tsushin Group companies. The main business is the inbound call center operation for the products of the Hikari Tsushin Group companies, providing solutions on various issues of call center operations, from accepting inquiries through to the follow-ups after the responses. By combining Leoconnect's knowhow with Scala's tools, the service cost of both companies can be halved, leading to higher profitability. In addition, there are chances that Scala's SaaS/ASP services can be accepted and adopted by the Hikari Tsushin Group companies.

## Customer support business: Direction of strategy

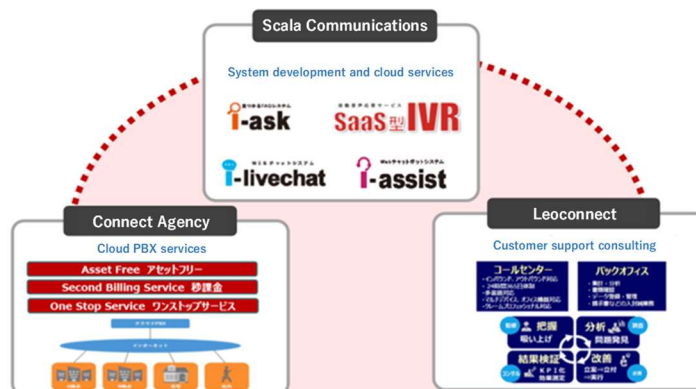
**Advanced combination of knowhow and tools**

This segment will accelerate combining customer support consulting services with IT services related to call centers and improve quality of response at customer help desks. Moreover, it intends to further develop proposal-type inbound call centers, which include promotion of product purchase and restraining of cancellation of service in their service menu.

Providing measures for inbound tourism to municipalities and companies that cannot fill the needs

Collaboration with a subsidiary to provide best practices to the troubled software developers

## Creating synergies with consolidated subsidiaries



(Source) FY6/2018 results briefings material

## Enhanced support to measures for inbound tourism

The customer support segment aims to strengthen a multi-language call center function and to provide high-grade concierge service, in order to support measures for inbound tourism of companies and municipalities, which are in need to respond to an increasing number of foreign visitors to Japan ahead of the Rugby World Cup in 2019 and the 2020 Tokyo Olympic Games. At present, many companies and municipalities do not have sufficient measures for inbound tourism and companies may be losing some business opportunities. Scala Communications and Leoconnect will therefore launch services, including translation of the FAQ website page of a municipality or a company, assistance via video chat with a multi-language operator, and response by a concierge in case the FAQ page does not help solve an issue.

## Other business: Current status

### System development business

This business is conducted by Softbrain Offshore Co., Ltd. By having know-how accumulated from many years of offshore development, the company emphasizes elimination of dependency on individual skills and thorough project management, avoiding mistakes typically made in offshore development. It also provides best practices by flexibly combining other methods, including use of domestic partners.

### Publishing business

This business is originated in the editorial department that published “Diamond Sales” magazines at Diamond, Inc., Japan’s prominent business-related publisher. The department was spun off and in 2005 SB took an equity stake and made it a merged company jointly with Diamond, Inc. It is now engaged primarily in publishing a diverse range of business books on management, marketing, sales and other themes, but also in consulting services to enhance IR, branding, and marketing for corporate clients. It also does joint publishing with those clients.

### EC business

This business is operated by plube, which manages Yuyutei, an EC website for buying and selling battle-type trading cards. Its strength lies in internal sourcing of logistics, systems, sales, purchasing, marketing, and other functions.

## Other business: Direction of strategy

### System development business: Direction of strategy

The software development landscape is becoming increasingly harsh due to:

- (1) delay in development work due to chronic engineer shortage;
- (2) inability to handle an increasing number of small-scale development projects; and
- (3) increase in management cost.

Scala thereby intends to provide best practices by combining the following:

- (1) use of abundant overseas engineers (offshore development);

**Publishing business plans to use Diamond's strong sales network**

**Aiming to expand into EC website management for individuals in the TCG field**

- (2) use of domestic partners (near-shore development); and
- (3) overseas outsourcing of maintenance operation (O&M) or services by overseas staff.

### **Publishing business: Direction of strategy**

The business line-up will be expanded by using accumulated know-how in conventional business publishing to production of corporate history books. These books can also be distributed to bookstores nationwide by using the strong sales channel of Diamond, Inc. There are some examples of corporate history book production for overseas clients.

### **EC business: Direction of strategy**

As the No. 1 website shop in trading card games (TCG), plube began development of software application for smartphones so as to offer the best trading experience to TCG users. As such, plube continuously improves its system and services and has aggressively increased its game titles. It also timely provides hints and tips for games with deep insights, creating a place to gather for TCG users and growing business. Scala is accumulating experience and know-how in inventory management, nationwide distribution, product pricing, etc., which will be useful for its future expansion into EC website management for individuals.



## 5. Potential synergy with Softbrain

**Collaboration with SB to become a leading company in the CRM/CMS field**

**The business alliance enables cross-selling and joint development of products**

**SB plans to reform its profit structure and to enhance consulting sales to achieve its targets**

### Details of the acquisition

#### Intention behind acquisition

Scala acquired Softbrain Co., Ltd. (SB) with the aim of raising the added value of its services by collaborating with SB. There is some commonality in business strategy between Scala's cloud service that comprehensively supports communication of companies and customers and SB's SFA products that support raising operational efficiency of non-managerial departments. Through their business alliance, both companies strive to propose better customized services to corporate customers and to improve convenience and satisfaction. They also consider to enter into new services and new domains by using strengths of both companies, in addition to expanding their existing businesses. The ultimate aim of Scala's acquisition of SB is to establish a leading position in the CRM/CMS field.

#### Details of the business alliance

This alliance should enable cross-selling and joint development of products and services. Cross-selling includes research on potential needs, drafting of marketing plans, and making proposals of individual or joint services in order to mutually sell services of the other. Scala and SB also jointly develop more value-added services, leveraging on both companies' technology, achievement and experiences.

#### Timeline of acquisition of SB in 2016

Mar. 30	Issued new shares, disposed treasury shares, and publicly offered shares
May 25	Decided share issuance amount via third-party allotment/secondary offering
May 16	Began purchase of shares of SB
May 23	Suspended purchase of shares of SB
June 20	Sold shares of Asia Co., Ltd. (Approximately ¥1.3 billion)
June 22	Scala's President met with SB's President
June 27	Resumed purchase of shares of SB
June 30	Borrowed ¥3.3 billion from Chiba Bank, Mizuho Bank, etc.
July 4	Acquired 40% of SB's shares outstanding; made it an equity-owned affiliate
July 14	Acquired 45.57% of SB's shares outstanding; made it a consolidated subsidiary
Aug. 15	Began talks on business alliance
Nov. 2	First cross-sale by selling SB's e-Sales Manager to Scala's customers

(Source) Extracted from disclosed information

### Evaluation of SB from the viewpoint of GCC management®

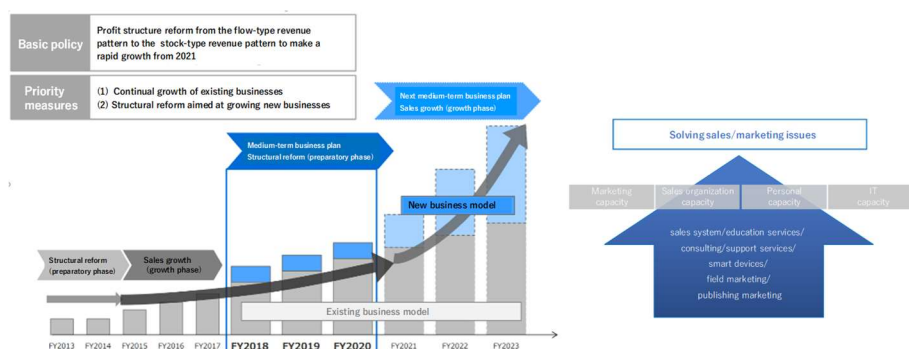
#### Numerical targets and measures toward achieving them

With regard to SB's two core businesses, targets for FY2020 are sales of 11.3 billion yen and operating profit of 1.5 billion yen (operating margin: 14%) in its sales innovation business and sales of 3.9 billion yen and operating profit of 0.34 billion yen (operating margin: 9%) in its field marketing business. In order to achieve these targets, SB has developed a medium- to long-term growth strategy with a focus on structural reform to shift from the flow-type revenue pattern to the stock-type revenue pattern, and on the enhancement of consulting sales to existing customers.

**Expecting  
high  
shareholder  
value by  
collaboratio  
n with SB**

**Corporate value  
evaluation from the  
three viewpoints of  
the GCC  
management®**

## Summary of SB's strategy



(Source) Extracted from SB's 2H FY12/2018 results briefings material

## Analysis of the GCC management®: Employees' viewpoint

Based on SB's strategy, potential synergy with Scala is analyzed using the concept of the GCC management®. As mentioned above, the GCC management® is to organize a corporate value growth story from the three perspectives: Growth (in sales), Connection (of people and businesses, leading to improve Return on Invested Capital), and Confidence. Based on the analysis, SB is expected to achieve both the effect of raising its shareholders' value and the enhancement of happiness of SB's employees at the same time.

### Growth: Increased expectation for SB's growth and contribution in the solution providing business, due to the customized strategy and higher growth potential of AI/IoT

SB's employees can meet with corporate customers' top executives and managers of a sales department and learn their thoughts and views on various issues, from current challenges to future business development, which helps them deepen knowledge, enhance personal growth and satisfaction, and meet their self-actualization needs. These employees ultimately contribute to SB's sales growth.

### Connection: Enhancing connection with customers

Jointly with those in the technical department, SB's employees work and solve corporate customers' issues found through consulting sales. With their strong customized services with self-developed software packages and their thorough follow-ups, SB has achieved the No. 1 ranking in customer comprehensive satisfaction and 96% in the retention rate in CRM/SFA, highly popular sales support tools. On top of SB's robust sales infrastructure, Scala's services are added, to more precisely satisfy customer needs, strengthen connections with customers, and ultimately satisfy employees' needs for dignity, as well as social needs.

### Confidence: Reducing business risks by expanding a stock-type revenue

SB is expected to generate more synergy with Scala and augment its growth potential in the AI/IoT field. Moreover, the stock-type business model will be enhanced, business risks will be reduced, and financial compensation to employees will become stable, thereby satisfying employees' physiological needs and needs for safety.

## Analysis of the GCC management®: Shareholders' viewpoint

### Growth: sales growth driven by cross sales

Scala and SB can expand fields to satisfy customer needs by incorporating services of both companies. In addition, acquisition of new customers by using Scala's strong strategy of using a "hook" service as well as provision of new services to existing customers of both companies will contribute to sales growth. They will have a more powerful customer base with 4,000 plus customers in SB's sales support cloud services and Scala's over 1,000 customers, of which over 400 are listed companies. This is

because Scala's and SB's B-to-B cloud services have a high degree of business affinity.

**Connection: Joint development of new services to improve ROIC**

Scala's strong technology in website action record analysis history will be tied with SB's sales support software to create a new service. This can be a foothold from the existing SaaS/ASP business domain to entering new domains, including AI, robotics, and EC. Both Scala and SB have important technologies and an ample salesforce in the cloud service business. They will collaborate in services and also aim to develop more value-added services and improve profitability through interaction. Scale merit is also a contributing factor to improve ROIC.

**Confidence: Enhancing a stock-type business model**

Customer retention and strong customer relationships are important to a stock-type business model. The service retention rate can be raised by responding to customers' needs with solutions derived from a wide range of the service line-up. Scala has already developed i-series of services, including i-search and i-ask, and can enhance the relationship with customers thanks to the alliance with SB, a market leader in the CRM/SFA field. Scala and SB will comprehensively support communication and business activities of corporate customers and deepen the relationships with them in order to raise the service retention rate and reduce business risks.

## 6. Review of FY6/2019, up to the third quarter

**Robust business segments led to an increase in sales and profit**

**CAGR of over 30% in main services**

**Up 14.4% in sales revenue of SFA business**

### SaaS/ASP business

In the SaaS/ASP business segment, sales revenue increased 28.1% y-o-y to ¥3,010 million and segment profit increased 36.4% to ¥609 million. There was some progress seen in the business to provide multiple services for solution, an area of strength in the segment. Sanyo Denki Co., Ltd. adopted Scala's Product Information Management (PIM) software that enables centralized management of product information, in addition to i-search and i-ask services. By making joint proposal with Leoconnect, i-ask was adopted by Max Support CO., Ltd. and i-ask and i-assist, by Last One Mile Corporation. Moreover, Connect Agency, Inc., which became a subsidiary of Scala in FY6/2018, adopted i-ask and is expected to reduce cost and contribute to sales revenue of the Scala Group.

### SFA business

On the sales side, the SFA business segment promoted development of new customers by continuing to host seminars and enhanced the group training for users, in addition to conventional software usage support services, in order to promote further usage by existing customers. On the development side, the focus continued to be to improve user-friendliness of e-Sales Manager, the main CRM/SFA software, and to develop a self-serve type of e-Sales Manager named RemixMS. Sales of e-Sales Manager were robust, particularly of the Cloud version. As a result, sales revenue increased 14.4% y-o-y to 3,592 million yen. As for profit, an increase in advanced expenses for growth, including development cost and personnel expenses, was more than offset by growth in sales revenue, resulting to an increase of 29.8% in segment profit to 703 million yen.

### Field marketing business

In the field marketing business segment, sales revenue increased 17.5% y-o-y to 2,912 million yen and segment profit increased 22.8% to 228 million yen. Under the concept of field crowdsourcing, this segment is working on measures aimed for new market development. Main services of the regular field business and the worker dispatch business continued to be strong.

### Customer support business

The customer support business segment recorded sales revenue of 2,073 million yen and segment profit of 43 million yen. Leoconnect, which became a subsidiary of Scala in FY6/2018, received outsourced customer support consulting operation for various companies in the Hikari Tsushin Group. In addition, Scala Communications was engaged in proposals, orders received, and introduction of the SaaS/ASP services and in new system development based on new needs.

### Summary of financial results

Reflecting high growth in main businesses, Scala's overall sales revenue increased 30-40% y-o-y while profit increased even at higher rates of 40-60% as profitability has improved in the first nine months of FY6/2019.



# Quarterly business results and forecasts

[Unit: one million yen]

Jun-19

		1Q	2Q	3Q	Full-year (pre)
SaaS/ASP business	Sales revenue	843	1,001	1,179	-
	YOY	3.3%	27.4%	57.8%	-
	Operating income	136	181	292	-
	YoY	-16.0%	33.1%	98.6%	-
SFA business	Operating profit margin	16.1%	18.1%	24.8%	-
	Sales revenue	1,124	1,299	1,179	-
	YoY	13.9%	23.4%	7.3%	-
	Operating income	196	320	187	-
field marketing business	YoY	16.7%	76.8%	-2.6%	-
	Operating profit margin	17.4%	24.6%	15.9%	-
	Sales revenue	940	1,016	957	-
	YoY	18.2%	22.3%	12.3%	-
customer support business	Operating income	72	69	86	-
	YoY	30.9%	9.5%	28.4%	-
	Operating profit margin	7.7%	6.8%	9.0%	-
	Sales revenue	656	685	737	-
others	Operating income	11	15	18	-
	Operating profit margin	1.7%	2.2%	2.4%	-
	Sales revenue	394	446	361	-
	Operating income	59	74	-15	-
Linked	Operating profit margin	15.0%	16.6%	-	-
	Sales revenue	3,959	4,446	4,376	16,600
	YoY	39.6%	47.3%	36.8%	29.4%
	Operating income	476	659	567	2,000
	YoY	24.6%	50.1%	40.7%	29.4%
	Operating profit margin	12.0%	14.8%	13.0%	12.0%
	Quarterly profit	329	427	382	1,340
	YoY	16.3%	52.0%	36.9%	26.3%
	Quarterly profit attributable to owner of parent company	204	254	296	890
	YoY	18.6%	27.0%	61.7%	25.9%

(Source) Prepared by J-Phoenix Research from financial statements

## 7. Financial strategy, shareholder return policy, and ESG

**Concurrently realizing high growth, aggressive M&As, and a 50% payout ratio**

**Planning the 10<sup>th</sup> consecutive fiscal year of dividend increase**

**Close to 50% in dividend payout ratio What is excess return?**

### Financial strategy

With the aim of raising corporate value over the medium- to long-term, Scala looks at sales revenue and earnings per share (non-GAAP indicators) as objective indicators. It aims at raising corporate value by promoting its existing business to achieve sustainable growth and by expanding business through M&As and developing business into other fields to further accelerate growth.

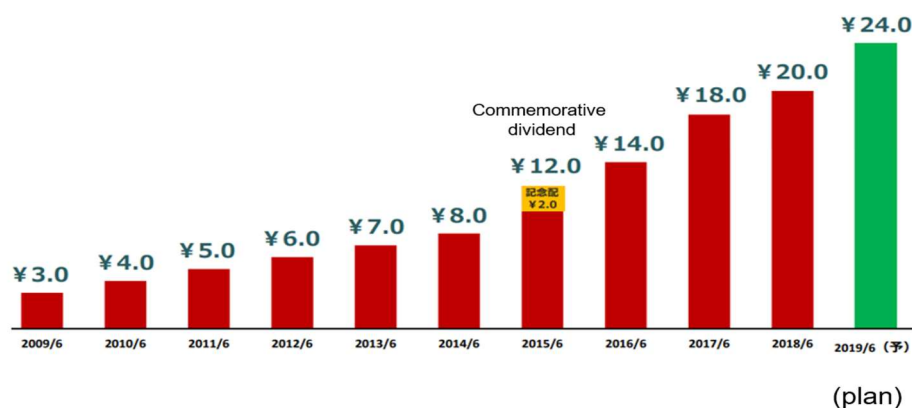
### Fund procurement

Scala mainly need to fund continuous execution of the shareholder return policy, as well as M&As and growth investment for business expansion and enhancement of corporate value. Scala's basic policy is to fund these activities by using cash on hand, and to procure funds by borrowing from financial institutions or issuing corporate bonds, as needed.

### Dividend policy

Scala places appropriate return of profits to shareholders as one of its management priority issues and continues to pay a stable dividend while it retains sufficient internal reserves to strengthen its financial position and develop business. Scala pays dividends of surplus twice a year as interim dividend and year-end dividend. In FY6/2019, Scala plans to increase the dividend per share by 4 yen from the previous fiscal year to 24 yen. This will be the tenth consecutive fiscal year of increase in dividends. The dividend payout ratio will be high at around 50% for FY6/2019. As Scala's business generates stable cash flow, it has achieved high growth and high dividend payout ratio.

### Shareholder return policy



(Summary) Extracted from FY6/2018 business presentation material

### ESG

#### Environment

Scala aims at contributing to problem-solving in Japan and globally, and to advancement and evolution of mankind.

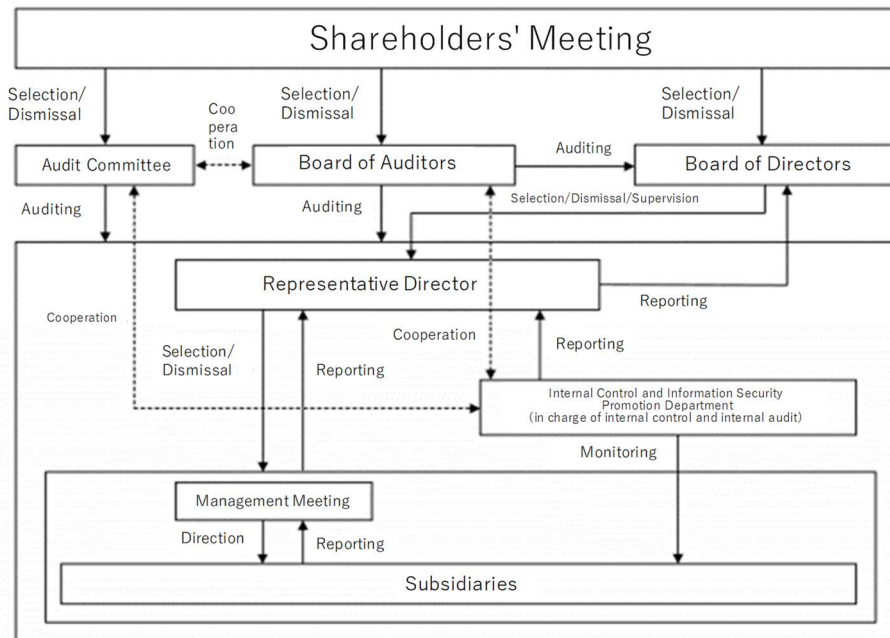
#### Social

Ethical values and social responsibility are taken up in Scala's corporate values statement. Scala will contribute to the maintenance and development of society by making social justice a criterion of its judgment and by responding to requests of employees and other stakeholders.

## Governance

Scala copes with changes in the management environment and enhances corporate governance by adopting a management supervising structure that consists of the Board of Directors (including one outside director) and the Board of Auditors (including two outside auditors).

### Scala's corporate governance structure



(Source) Extracted from Scala's 32<sup>nd</sup> Securities Report

## Compliance

Scala has its own compliance rules. Concerning legal violation or compliance issues of executives and employees, a contact desk is available and there is a scheme to prevent whistle blowers and others seeking for advice be disadvantaged.

## Audit

### Internal audit

The Internal Control and Information Security Promoting Department is positioned directly under the Representative Director and is engaged in business operation audit according to the internal audit rules and annual plan.

### External audit

Two outside auditors who have no personal or capital relationship or other interest with Scala perform audits from the expert viewpoint concerning financial, accounting, and legal matters.

## Risk management

Measures to prevent risk occurrence are undertaken by the Internal Control and Information Security Promoting Department, spearheading efforts to comprehensively manage potential risks and performing an audit upon reflecting priority issues stated on the internal audit plan. Concerning the prevention of leakage of confidential information and the handling of information security, the Information Security Committee, which is comprised of directors and employees, is established and employee training is conducted twice a year.

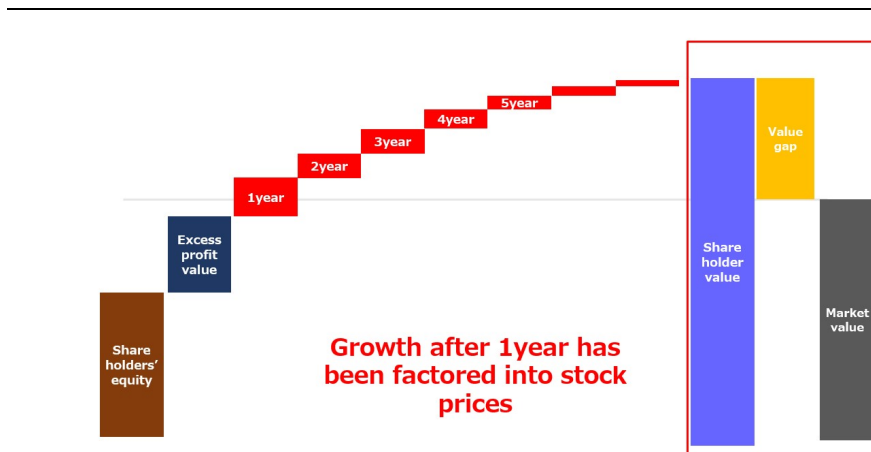
## 8. Reference material: Another way to estimate corporate value by use of ROIC and excess return

### What is excess profit?

### Excess return analysis framework

Excess profit or economic value added is widely used worldwide as an indicator to estimate corporate value, evidenced by being adopted by Kao Corporation, a Grand Prix winner of the Tokyo Stock Exchange Fifth Corporate Value Improvement Award (FY2016). In the calculation of excess return, corporate value can be broken down to four elements: invested capital, excess return value, growth value, and non-business assets. This facilitates better understanding of a structure to create corporate value. A company might be overvalued when its market cap is higher than its theoretical corporate value, and undervalued when the market cap is lower. Contribution of each year's corporate value can be visualized in the following figure, in which shareholders' equity is simply represented as a sum of invested capital and non-business asset, subtracting interest-bearing debts. The figure below allows us to estimate how many years of growth might be incorporated in the stock price.

### Breakdown of corporate value using excess return



(Source) J-Phoenix Research

Estimated excess is profit that exceeds investors' return expectations against invested capital. Its present value is "excess return value" while a potentially growing portion of excess return is "growth value." Moreover, assets which are not used in business are added as non-business asset value in estimating a theoretical corporate value. Theoretically, the estimated corporate value using excess return should be the same as the value estimated by using the discount cash flow (DCF) model. This report calculates excess return by using the following figures in the simplified way.

- Excess return = NOPAT – Invested capital X WACC
- Net Operating Profit After Tax (NOPAT) = Operating profit X (1- Effective tax rate)
- Invested capital = Total assets – Non-business assets – Current liabilities excluding Interest bearing debt
- Non-business assets = Cash and deposits that exceed 10% of sales + Short-term investment securities + Investment securities + Deferred gains or losses on hedges + Land revaluation difference + Foreign currency translation adjustments
- Weighted average cost of capital (WACC)= After-tax interest rate of interest-bearing debt X (D/(E+D)+ Cost of shareholders' equity X (E/D+E)
- Cost of shareholders' equity= 0.5% + 5% X  $\beta$
- $\beta$  = Slope of a linear regression line of five-year daily returns of TOPIX and the stock price of the target company
- E = Market cap at the time of calculation
- D = Short-term interest-bearing debt + Long-term liabilities + Minority interests in the latest financial statements at the time of calculation



## 9. Helpful viewpoint: Use of Management Design Sheet

**Review of  
optimal  
customized  
cloud  
business  
develop-  
ment**

**Intensified  
competition in the  
media advertisement  
market forced Scala  
to sell its initial main  
business and to  
form business from  
needs of customers**

**Having to start from  
scratch led to  
creation of  
consulting sales and  
advanced  
engineering  
capacity, Scala's  
strengths at present**

### Corporation Management Design Sheet

#### What is the Corporation Management Design Sheet?

The Corporation Management Design Sheet is produced and publicly released in June 2018 by Japan's Cabinet Office Intellectual Property Strategy Headquarters as a tool to design management by appropriately evaluating a role of intellectual properties (IPs) in the corporate value creating mechanism\*. It was developed based on the knowledge and insights of experts and business people from various industries in order to visualize an increasing role of IPs as management driving source at the time of transition of the social, economic environment from the 20<sup>th</sup> century type, in which the market was driven by stable supply of products, to the 21<sup>st</sup> century type, in which the market was driven by diverse values of users who seek experiences and empathy. The Design Sheet can be described as a condensed framework of cutting-edge knowledge and insights in designing corporate management. This is intended to visualize value creation mechanism which can work as a future management base for sustainable corporate growth. There is an increase in use by companies. The design sheet facilitates obtaining a big picture of time-conscious corporate management and to make people aware of the relationship among resources, business model, and value.

In order to appeal to diverse values of users, companies are anticipated to be innovative in flexibly and continuously designing its value creating mechanism and, for that purpose, to appropriately evaluate the role of IPs in the value creating mechanism. Companies that can well organize their management strategy in keeping with the concept of the Management Design Sheet can be viewed as having their strategy being built according to a 21<sup>st</sup> century type of logic. For reference, Scala's Management Design Sheet is shown on the next page.

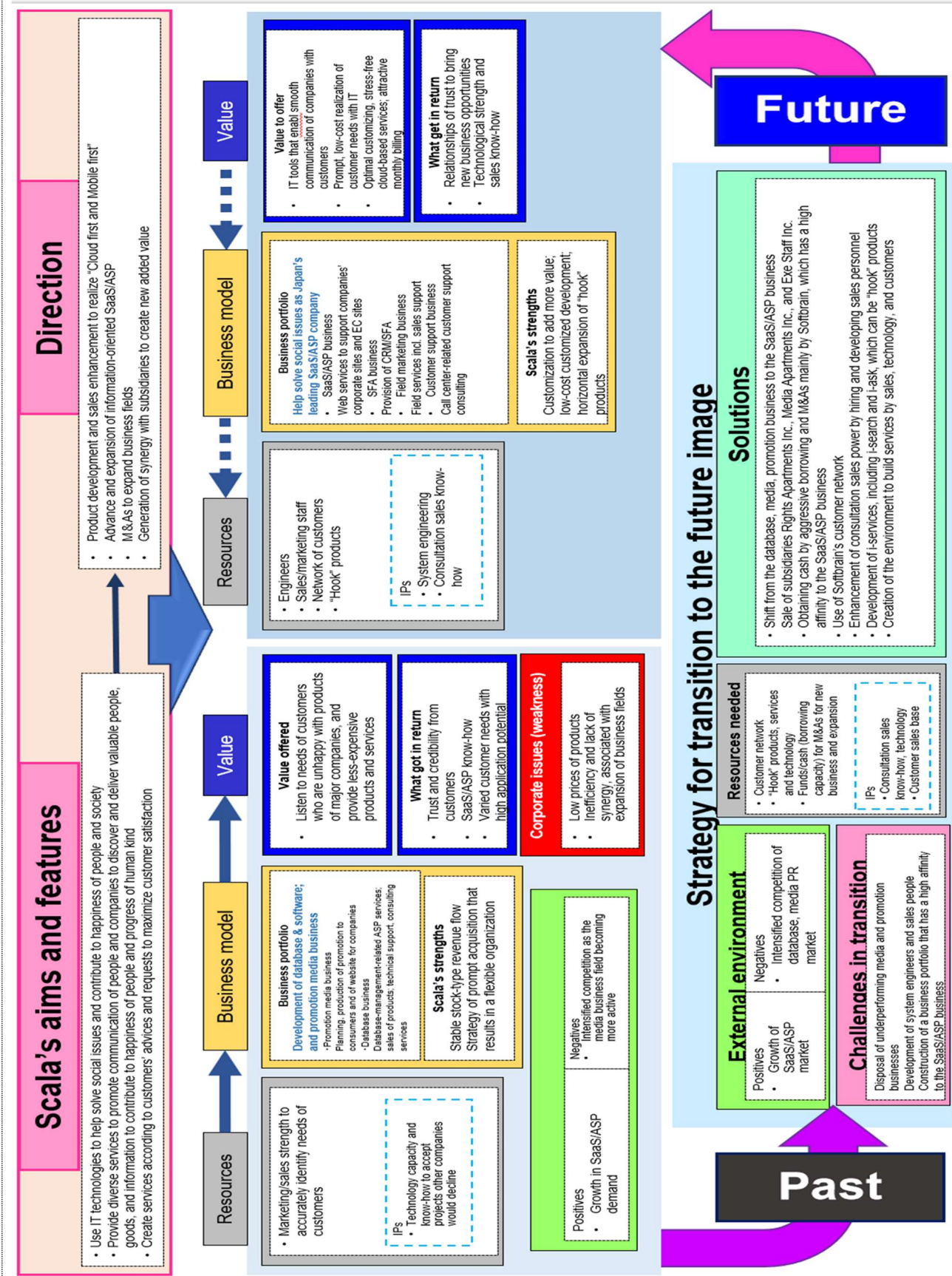
\* For reference: [https://www.kantei.go.jp/jp/singi/titeki2/keiei\\_design/index.html](https://www.kantei.go.jp/jp/singi/titeki2/keiei_design/index.html)

#### Scala's strategy development summary in the Management Design Sheet

Scala's original main business is the promotion media business of planning, production, and website production for corporate promotion activities targeted to consumers. However, due to the intensified competition in the media CM market, the business deteriorated and became loss making. Scala then boldly decided to sell the promotion media business and to shift into the SaaS/ASP business. Initially, without having any packaged software for sale, Scala developed services that satisfied needs of customers and expanded a line of services. Precisely by having to start from scratch, Scala was able to create capability in consultation sales and in engineering to develop products, which has now become Scala's advantages.

Such transition is organized in the Management Design Sheet on the next page. Reviewing the past, it is clear that Scala has necessary items in place, demonstrating its consistent, logical business strategy evolving around the provision of value to customers.

## Scala's Management Design Sheet



(Source) Prepared by J-Phoenix Research based on the Cabinet Office's material

**Disclaimer**

This report is issued by Toward the Infinite World, Inc. and IFIS JAPAN LTD. (hereafter “issuers”) under the brand name of "ANALYST NET" (a registered trademark) and written by external partners and analysts as its main authors.

- In the report issued under the brand name of "ANALYST NET", we are aiming to provide information and explanations about the target companies using a different approach from the traditional method. In principle, issuers do not seek a review or authorization against the contents herein. (However, we point out to the authors only if there are errors or incorrect wording.)
- Issuers may receive compensation directly or indirectly from the target companies in the project proposal and infrastructure offering to issue this report.
- External partners and analysts may receive compensation directly or indirectly from the target companies for additional work apart from writing this report. The external partners and analysts may have already been involved or may be involved in some trading of securities of target companies in the future.
- This report is created for the purpose of providing information for investors to refer to when they are making decisions about investments, and not for soliciting trading of securities or other financial products. Investors are responsible for their final decisions on trading of securities or other financial products.
- Although authors collected information during interviews with the target companies in order to create this report, the hypothesis and opinions in this report do not reflect the views of such companies, and are from the authors' own analysis and evaluation.
- Although this report is based on information that the authors believed to be reliable, we do not guarantee the accuracy, completeness and/or timeliness of the contents. The opinions and forecasts in this report are conducted at the time of publication and may be changed without notice.
- In any event, issuers and authors are not liable for any direct, indirect, incidental, or special damages that the investors may receive by relying on the information and analysis contained in this report.
- All contents of this report are the copyright of issues unless otherwise stated. No part of such information shall be reproduced, sold, displayed, distributed, published, amended, or used for commercial purposes without ISSURES's consent.