Gamecard-Joyco Holdings / 6249

COVERAGE INITIATED ON: 2011.07.11
LAST UPDATE: 2019.08.08

Shared Research Inc. has produced this report by request from the company discussed in the report. The aim is to provide an “owner’s manual” to investors. We at Shared Research Inc. make every effort to provide an accurate, objective, and neutral analysis. In order to highlight any biases, we clearly attribute our data and findings. We will always present opinions from company management as such. Our views are ours where stated. We do not try to convince or influence, only inform. We appreciate your suggestions and feedback. Write to us at sr_inquiries@sharedresearch.jp or find us on Bloomberg.

Research Coverage Report by Shared Research Inc.

INDEX

How to read a Shared Research report: This report begins with the trends and outlook section, which discusses the company's most recent earnings. First-time readers should start at the business section later in the report.

Key financial data

Income statement (JPYmn)	FY03/10 Par.	FY03/11 Par.	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Est.
Sales	**32,834**	**37,005**	**43,575**	**39,545**	**34,192**	**25,741**	**23,885**	**20,405**	**16,928**	**17,375**	**15,000**
YoY	6.0%	12.7%	-	-9.2%	-13.5%	-24.7%	-7.2%	-14.6%	-17.0%	2.6%	-13.7%
Gross profit	**9,660**	**11,199**	**13,093**	**11,884**	**10,980**	**9,665**	**8,413**	**8,250**	**7,871**	**7,446**	
YoY	-6.4%	15.9%	-	-9.2%	-7.6%	-12.0%	-13.0%	-1.9%	-4.6%	-5.4%	
GPM	29.4%	30.3%	30.0%	30.1%	32.1%	37.5%	35.2%	40.4%	46.5%	42.9%	
Operating profit	**1,566**	**4,322**	**4,459**	**2,668**	**1,764**	**816**	**-1,440**	**1,919**	**3,596**	**2,423**	**900**
YoY	-41.4%	176.0%	-	-40.2%	-33.9%	-53.7%	-	-	87.4%	-32.6%	-62.9%
OPM	4.8%	11.7%	10.2%	6.7%	5.2%	3.2%	-6.0%	9.4%	21.2%	13.9%	6.0%
Recurring profit	**1,508**	**4,208**	**4,543**	**2,692**	**1,849**	**836**	**-1,383**	**1,945**	**3,594**	**2,419**	**900**
YoY	-44.4%	179.0%	-	-40.7%	-31.3%	54.7%	-	-	84.8%	-32.7%	-62.8%
RPM	4.6%	11.4%	10.4%	6.8%	5.4%	3.2%	-5.8%	9.5%	21.2%	13.9%	6.0%
Net income	**918**	**2,338**	**4,573**	**1,598**	**900**	**293**	**-2,117**	**27**	**2,318**	**1,429**	**500**
YoY	-59.3%	154.7%	-	-65.1%	-43.7%	-67.4%	-	-	-	-38.3%	-65.0%
Net margin	2.8%	6.3%	10.5%	4.0%	2.6%	1.1%	-8.9%	0.1%	13.7%	8.2%	3.3%
Per share data (split-adjusted)											
Shares issued (year-end; '000)	11,413	11,413	14,263	14,263	14,263	14,263	14,263	14,263	14,263	14,263	
EPS	80.4	204.9	320.6	112.1	63.2	20.5	-148.5	2.0	162.6	100.3	35.1
EPS (fully diluted)	-	-	-	-	-	-	-	-	-	-	
Dividend per share	50.0	50.0	60.0	60.0	60.0	60.0	60.0	30.0	35.0	35.0	35.0
Book value per share	2,838.8	2,991.8	2,881.7	2,930.5	2,933.2	2,893.7	2,684.3	2,654.0	2,771.4	2,836.2	
Balance sheet (JPYmn)											
Cash and cash equivalents	18,071	22,642	24,848	26,731	32,009	25,020	25,529	23,475	26,000	32,099	
Total current assets	**36,273**	**41,670**	**51,055**	**51,567**	**56,522**	**45,284**	**43,934**	**40,015**	**40,038**	**46,428**	
Tangible fixed assets	-2,190	2,005	2,369	2,120	2,193	1,486	776	469	373	333	
Intangible fixed assets	6,540	5,506	4,636	3,509	2,624	2,896	2,226	3,188	2,619	2,140	
Investments and other assets	7,628	6,991	7,921	8,313	3,315	9,413	7,844	6,975	6,480	1,295	
Total assets	**52,431**	**56,173**	**65,983**	**65,510**	**64,655**	**59,081**	**54,781**	**50,648**	**49,511**	**50,197**	
Accounts payable	3,320	3,453	4,423	3,675	3,040	2,211	2,402	2,019	1,334	1,598	
Short-term debt	-	-	-	-	-	-	-	-	-	-	
Unused card balance	4,323	3,578	3,308	2,770	2,660	2,591	2,530	2,335	2,143	1,968	
Total current liabilities	**11,927**	**12,237**	**13,905**	**13,183**	**13,448**	**10,107**	**10,363**	**7,932**	**6,188**	**6,425**	
Long-term debt	-	-	-	-	-	-	-	-	-	-	
Total fixed liabilities	**8,104**	**9,790**	**10,977**	**10,528**	**9,370**	**7,702**	**6,132**	**4,862**	**3,795**	**3,319**	
Total liabilities	**20,032**	**22,028**	**24,882**	**23,712**	**22,819**	**17,809**	**16,496**	**12,795**	**9,983**	**9,744**	
Net assets	**32,399**	**34,145**	**41,101**	**41,798**	**41,835**	**41,272**	**38,230**	**37,830**	**39,506**	**40,453**	
Total interest-bearing debt	-	-	-	-	-	-	-	-	-	-	
Statement of cash flows (JPYmn)											
Cash flows from operating activities	2,615	5,082	4,266	5,109	4,631	3,844	1,828	2,264	3,466	1,952	
Cash flows from investing activities	-4,319	77	-13,950	1,133	-1,146	-5,046	-841	1,381	-6,008	-240	
Cash flows from financing activities	-1,504	-1,639	-1,998	-2,360	-2,194	-1,799	-1,476	-699	-828	-654	
Financial ratios											
ROA (RP-based)	2.9%	7.7%	7.4%	4.1%	2.8%	1.4%	-2.4%	3.7%	7.2%	4.9%	
ROE	2.8%	7.0%	11.1%	3.9%	2.2%	0.7%	-5.3%	0.1%	6.0%	3.6%	
Equity ratio	61.8%	60.8%	62.3%	63.8%	64.7%	69.9%	69.8%	74.7%	79.8%	80.6%	

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.
Note: Figures prior to FY03/12 are for Nippon Game Card.

Recent updates

Highlights

On **August 8, 2019**, Gamecard-Joyco Holdings, Inc. announced earnings results for Q1 FY03/20; see the results section for details.

On **the same day**, the company announced the acquisition of treasury shares through the Off-Auction Own Share Repurchase Trading System (ToSTNeT-3).

Acquisition method

Consigned purchase at the closing price of JPY1,310 as of August 8, 2019 through the Off-Auction Own Share Repurchase Trading System (ToSTNeT-3) of the Tokyo Stock Exchange at 8:45am on August 9, 2019.

Details of acquisition

- Type of shares to be acquired: Common shares of the company
- Total number of shares to be acquired: 350,000 shares (2.45% of issued shares)
- Total acquisition price: JPY500mn (upper limit)

On **June 21, 2019**, Shared Research updated the report following interviews with the company.

On **May 9, 2019**, the company announced earnings results for full-year FY03/19.

For previous releases and developments, please refer to the News and topics section.

Trends and outlook

Quarterly trends and results

Cumulative performance		FY03/19				FY03/20			FY03/20	
(JPYmn)	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	% of FY	FY Est.
Sales	4,121	8,466	12,890	17,375	4,045				27.0%	15,000
YoY	-7.4%	-1.1%	-1.7%	2.6%	-1.8%					-13.7%
Gross profit	1,949	3,868	5,762	7,446	1,849					
YoY	-6.4%	-5.9%	-6.4%	-5.4%	-5.1%					
GPM	47.3%	45.7%	44.7%	42.9%	45.7%					
SG&A expenses	988	2,141	3,200	5,023	1,133					
YoY	-12.6%	-1.8%	-0.9%	17.5%	14.7%					
SG&A ratio	24.0%	25.3%	24.8%	28.9%	28.0%					
Operating profit	960	1,726	2,562	2,423	716				79.6%	900
YoY	1.1%	-10.6%	-12.6%	-32.6%	-25.4%					-62.9%
OPM	23.3%	20.4%	19.9%	13.9%	17.7%					6.0%
Recurring profit	963	1,727	2,564	2,419	728				80.9%	900
YoY	0.5%	-10.4%	-12.4%	-32.7%	-24.4%					-62.8%
RPM	23.4%	20.4%	19.9%	13.9%	18.0%					6.0%
Net income	693	1,177	1,690	1,429	399				79.8%	500
YoY	-0.1%	-15.9%	-15.1%	-38.3%	-42.4%					-65.0%
Net margin	16.8%	13.9%	13.1%	8.2%	9.9%					3.3%

Quarterly performance		FY03/19				FY03/20		
(JPYmn)	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Sales	4,121	4,345	4,423	4,486	4,045			
YoY	-7.4%	5.8%	-3.0%	17.7%	-1.8%			
Gross profit	1,949	1,919	1,894	1,684	1,849			
YoY	-6.4%	-5.5%	-7.5%	-1.6%	-5.1%			
GPM	47.3%	44.2%	42.8%	37.5%	45.7%			
SG&A expenses	988	1,153	1,059	1,823	1,133			
YoY	-12.6%	9.8%	1.1%	74.3%	14.7%			
SG&A ratio	24.0%	26.5%	23.9%	40.6%	28.0%			
Operating profit	960	765	835	-139	716			
YoY	1.1%	-22.0%	-16.5%	-	-25.4%			
OPM	23.3%	17.6%	18.9%	-	17.7%			
Recurring profit	963	763	837	-145	728			
YoY	0.5%	-21.3%	-16.3%	-	-24.4%			
RPM	23.4%	17.6%	18.9%	-	18.0%			
Net income	693	483	512	-261	399			
YoY	-0.1%	-31.5%	-13.4%	-	-42.4%			
Net margin	16.8%	11.1%	11.6%	-	9.9%			

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.
Note: Company forecasts are the most recent figures.

Performance by product type (cumulative)

Cumulative	FY03/18				FY03/19			
(JPYmn)	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Sales	**4,451**	**8,557**	**13,117**	**16,928**	**4,121**	**8,466**	**12,890**	**17,375**
YoY	-6.2%	-12.2%	-16.2%	-17.0%	-7.4%	-1.1%	-1.7%	2.6%
Equipment sales	1,564	2,862	4,634	5,732	1,478	3,186	5,006	6,949
YoY	-3.9%	-19.6%	-27.4%	-29.8%	-5.5%	11.3%	8.0%	21.2%
Card sales	820	1,609	2,403	3,170	730	1,485	2,230	2,963
YoY	-11.2%	-11.8%	-12.7%	-12.2%	-11.0%	-7.7%	-7.2%	-6.5%
System-usage fees	1,951	3,867	5,745	7,584	1,793	3,552	5,269	6,950
YoY	-6.2%	-6.4%	-6.7%	-6.9%	-8.1%	-8.1%	-8.3%	-8.4%
Others	115	218	333	440	118	241	383	514
YoY	0.9%	-4.0%	-11.2%	-8.1%	2.6%	10.6%	15.0%	16.8%
Gross profit	**2,082**	**4,112**	**6,159**	**7,871**	**1,949**	**3,868**	**5,762**	**7,446**
YoY	-4.6%	-5.3%	-6.9%	-4.6%	-6.4%	-5.9%	-6.4%	-5.4%
GPM	46.8%	48.1%	47.0%	46.5%	47.3%	45.7%	44.7%	42.9%
Equipment sales	239	457	725	703	235	443	666	737
YoY	-3.6%	-4.8%	-15.0%	4.5%	-1.7%	-3.1%	-8.1%	4.8%
GPM	15.3%	16.0%	15.6%	12.3%	15.9%	13.9%	13.3%	10.6%
Card sales	523	1,042	1,533	2,029	472	961	1,430	1,889
YoY	-13.4%	-13.6%	-12.4%	-10.3%	-9.8%	-7.8%	-6.7%	-6.9%
GPM	63.8%	64.8%	63.8%	64.0%	64.6%	64.7%	64.1%	63.8%
System-usage fees	1,289	2,560	3,815	5,022	1,200	2,378	3,530	4,648
YoY	-0.6%	-1.1%	-2.0%	-2.8%	-6.9%	-7.1%	-7.5%	-7.4%
GPM	66.1%	66.2%	66.4%	66.2%	66.9%	67.0%	67.0%	66.9%
Others	31	52	84	116	41	83	134	173
SG&A expenses	**1,131**	**2,181**	**3,228**	**4,274**	**988**	**2,141**	**3,200**	**5,023**
YoY	-24.7%	-29.1%	-35.5%	-32.5%	-12.6%	-1.8%	-0.9%	17.5%
SG&A ratio	25.4%	25.5%	24.6%	25.2%	24.0%	25.3%	24.8%	28.9%
Personnel expenses	416	852	1,230	1,611	362	789	1,175	1,578
R&D expenses	82	155	273	393	94	281	408	1,206
Operating profit	**950**	**1,931**	**2,931**	**3,596**	**960**	**1,726**	**2,562**	**2,423**
YoY	39.7%	52.8%	81.9%	87.4%	1.1%	-10.6%	-12.6%	-32.6%
OPM	21.3%	22.6%	22.3%	21.2%	23.3%	20.4%	19.9%	13.9%
Quarterly	**FY03/18**				**FY03/19**			
(JPYmn)	**Q1**	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**	**Q3**	**Q4**
Sales	**4,451**	**4,106**	**4,560**	**3,811**	**4,121**	**4,345**	**4,423**	**4,486**
YoY	-6.2%	-17.8%	-22.9%	-19.7%	-7.4%	5.8%	-3.0%	17.7%
Equipment sales	1,564	1,298	1,772	1,098	1,478	1,708	1,819	1,943
YoY	-3.9%	-32.9%	-37.1%	-38.6%	-5.5%	31.6%	2.7%	77.0%
Card sales	820	789	794	767	730	754	744	733
YoY	-11.2%	-12.5%	-14.3%	-10.5%	-11.0%	-4.4%	-6.3%	-4.4%
System-usage fees	1,951	1,916	1,878	1,839	1,793	1,759	1,717	1,681
YoY	-6.2%	-6.5%	-7.2%	-7.7%	-8.1%	-8.2%	-8.6%	-8.6%
Others	115	103	115	107	118	123	141	131
Gross profit	**2,082**	**2,030**	**2,047**	**1,712**	**1,949**	**1,919**	**1,894**	**1,684**
YoY	-4.6%	-5.9%	-10.1%	4.8%	-6.4%	-5.5%	-7.5%	-1.6%
GPM	46.8%	49.4%	44.9%	44.9%	47.3%	44.2%	42.8%	37.5%
Equipment sales	239	218	268	-22	235	208	222	71
YoY	-3.6%	-6.0%	-28.2%	-	-1.7%	-4.6%	-17.2%	-
GPM	15.3%	16.8%	15.1%	-	15.9%	12.2%	12.2%	3.7%
Card sales	523	519	491	496	472	489	468	459
YoY	-13.4%	-13.8%	-9.7%	-2.9%	-9.8%	-5.8%	-4.7%	-7.5%
GPM	63.8%	65.8%	61.8%	64.7%	64.6%	64.9%	62.9%	62.6%
System-Usage Fees	1,289	1,271	1,255	1,207	1,200	1,178	1,152	1,118
YoY	-0.6%	-1.5%	-3.7%	-5.6%	-6.9%	-7.3%	-8.2%	-7.4%
GPM	66.1%	66.3%	66.8%	65.6%	66.9%	67.0%	67.1%	66.5%
Others	31	21	32	32	41	42	50	39
SG&A expenses	**1,131**	**1,050**	**1,047**	**1,046**	**988**	**1,153**	**1,059**	**1,823**
YoY	-24.7%	-33.3%	-45.8%	-21.1%	-12.6%	9.8%	1.1%	74.3%
SG&A ratio	25.4%	25.6%	23.0%	27.4%	24.0%	26.5%	23.9%	40.6%
Personnel	416	436	378	381	362	426	386	403
R&D expenses	82	73	118	120	94	187	127	798
Operating profit	**950**	**981**	**1,000**	**665**	**960**	**765**	**835**	**-139**
YoY	39.7%	68.0%	188.2%	115.9%	1.1%	-22.0%	-16.5%	-
OPM	21.3%	23.9%	21.9%	17.4%	23.3%	17.6%	18.9%	-

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.

Earnings-related metrics (cumulative)

Cumulative	FY03/18				FY03/19			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
No. of equipment shipped ('000)	12.0	20.8	33.6	43.6	11.2	25.8	40.7	61.7
YoY	-5.3%	-29.2%	-38.3%	-38.3%	-6.7%	23.7%	21.2%	41.5%
No. of member stores	3,889	3,826	3,778	3,674	3,612	3,543	3,482	3,401
YoY change	-219	-240	-242	-283	-277	-283	-296	-273
YoY	-5.3%	-5.9%	-6.0%	-7.2%	-7.1%	-7.4%	-7.8%	-7.4%
QoQ change	-68	-63	-48	-104	-62	-69	-61	-81
QoQ	-1.7%	-1.6%	-1.3%	-2.8%	-1.7%	-1.9%	-1.7%	-2.3%
Quarterly	FY03/18				FY03/19			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
No. of equipment shipped ('000)	12.0	8.8	12.8	10.0	11.2	14.6	15.0	20.9
YoY	-5.3%	-47.3%	-49.0%	-38.6%	-6.7%	65.1%	17.2%	109.6%

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.

Q1 FY03/20 results

- Sales: JPY4.0bn (-1.8% YoY)
- Operating profit: JPY716mn (-25.4% YoY)
- Recurring profit: JPY728mn (-24.4% YoY)
- Net income*: JPY399mn (-42.4% YoY)

*Net income refers to net income attributable to parent company shareholders.

Even as pachinko hall operators that comprise the company's primary customer base continue to have an uncertain future due to ongoing study of gambling addiction countermeasures accompanying the Integrated Resort Promotion Act and the enforcement of a tighter regulatory environment reflecting the revised regulations (Regulations Partially Amending the Ordinance for Enforcement of the Act on Control and Improvement of Amusement Business, etc.), there are still some medium-sized and large chain operators looking to maintain or even improve their competitive position by opening up more pachinko halls in and around Japan's major cities, especially in the Kanto and Kinki regions.

The company group is actively undertaking a range of sales initiatives to maintain and improve its share of member halls. It has implemented measures to strengthen its relationships with distributors, actively rolled out machine replacement promotion measures, and carried out aggressive equipment sales leveraging its strong financial base. However, sales and profit declined, reflecting a decline in the number of member halls and intensifying competition as the overall market continues to contract.

For details on previous quarterly and annual results, please refer to the Historical earnings results section.

Full-year company forecasts

	FY03/18			FY03/19			FY03/20
(JPYmn)	1H Act.	2H Act.	FY Act.	1H Act.	2H Act.	FY Act.	FY Est.
Sales	**8,557**	**8,371**	**16,928**	**8,466**	**8,909**	**17,375**	**15,000**
YoY	-12.2%	-21.5%	-17.0%	-1.1%	6.4%	2.6%	-13.7%
Cost of sales	4,444	4,613	9,057	4,599	5,330	9,929	
Gross profit	**4,112**	**3,759**	**7,871**	**3,867**	**3,579**	**7,446**	**6,300**
YoY	-5.3%	-3.9%	-4.6%	-6.0%	-4.8%	-5.4%	
GPM	48.1%	44.9%	46.5%	45.7%	40.2%	42.9%	42.0%
SG&A expenses	2,181	2,093	4,274	2,140	2,883	5,023	5,400
SG&A ratio	25.5%	25.0%	25.2%	25.3%	32.4%	28.9%	
Operating profit	**1,931**	**1,665**	**3,596**	**1,726**	**697**	**2,423**	**900**
YoY	52.8%	154.2%	87.4%	-10.6%	-58.1%	-32.6%	-62.9%
OPM	22.6%	19.9%	21.2%	20.4%	7.8%	13.9%	6.0%
Recurring profit	**1,927**	**1,667**	**3,594**	**1,727**	**692**	**2,419**	**900**
YoY	50.9%	149.6%	84.8%	-10.4%	-58.5%	-32.7%	-62.8%
RPM	22.5%	19.9%	21.2%	20.4%	7.8%	13.9%	6.0%
Net income	**1,399**	**919**	**2,318**	**1,177**	**252**	**1,429**	**500**
YoY	76.9%	-	-	-15.9%	-72.6%	-38.3%	-65.0%

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.
Note: "-" indicates that the year-on-year ratio exceeds 1000%.

Details of company forecasts

	FY03/18	FY03/19	FY03/20
(JPYmn)	FY Act.	FY Act.	FY Est.
Equipment sales (units)	43,593	61,673	52,000
YoY	-38.3%	41.5%	-15.7%
No. of member stores	3,674	3,401	3,108
YoY	-7.2%	-7.4%	-8.6%
Sales	16,928	17,375	15,000
YoY	-17.0%	2.6%	-13.7%
Equipment sales	5,732	6,949	5,500
YoY	-29.8%	21.2%	-20.9%
Card sales	3,170	2,962	2,500
YoY	-12.2%	-6.6%	-15.6%
System-usage fees	7,584	6,950	6,000
YoY	-6.9%	-8.4%	-13.7%
Other	440	513	1,000
Gross profit	7,871	7,446	6,300
YoY	-4.6%	-5.4%	-15.4%
GPM	46.5%	42.9%	42.0%
SG&A expenses	4,274	5,023	5,400
YoY	-32.5%	17.5%	7.5%
SG&A ratio	25.2%	28.9%	36.0%
Personnel expenses	1,611	1,577	1,689
YoY	-24.7%	-2.1%	7.1%
R&D expenses	393	1,206	1,612
YoY	-56.6%	206.9%	33.7%
R&D ratio	2.3%	6.9%	10.7%
Other	2,269	2,239	2,140
YoY	-30.9%	-1.3%	-4.4%
Operating profit	3,596	2,423	900
YoY	87.4%	-32.6%	-62.9%
OPM	21.2%	13.9%	6.0%

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.

FY03/20 forecasts

- ▷ Sales: JPY15.0bn (-13.7% YoY)
- ▷ Operating profit: JPY900mn (-62.9% YoY)
- ▷ Recurring profit: JPY900mn (-62.8% YoY)
- ▷ Net income*: JPY500mn (-65.0% YoY)

*Net income refers to net income attributable to parent company shareholders.

Pachinko hall operators that comprise the company's primary customer base will continue to be impacted by a tighter regulatory environment accompanying the 2018 implementation of the Regulations Partially Amending the Ordinance for Enforcement of the Act on Control and Improvement of Amusement Business and others, and the Basic Bill on Gambling Addiction Countermeasures. The market is likely to continue shrinking.

Gamecard-Joyco expects this to impact its earnings, with system usage fee revenue declining as the number of member halls continues falling. In light of these circumstances, it considers maintaining existing member halls to be a priority issue and is therefore conducting initiatives including making proposals for system replacement to prepare for the consumption tax increase, developing products to prevent gambling addiction, and actively hiring personnel.

- ▷ The company forecasts equipment unit sales to fall 15.7% YoY to 52,000 units.
- ▷ Meanwhile, the number of member halls is expected to fall to 3,108 (-8.6% YoY). The number of member halls has declined at an annual average of 6.5% over the past five years, but the company predicts the decline to be even more rapid in FY03/20. Gamecard-Joyco forecasts pachinko hall closures will increase with the removal of old-format pachislot machines by December 2019.

The company expects lower sales in all categories, with equipment sales reflecting the largest drop.

- ▷ Equipment sales are forecasted at JPY5.5bn (-20.9% YoY). The decline in equipment sales is predicted to outstrip the decline in equipment unit sales. Shared Research thinks this means the company expects the selling price to go down.
- ▷ Card sales are forecasted at JPY2.5bn (-15.6% YoY) due to an expected decrease in the number of member halls and lower revenue from information management fees. The drop in information management fees is an expected result of lower card spending due to halls installing higher numbers of gaming machines with low-priced balls.
- ▷ System-usage fee revenue is forecasted to fall 13.7% YoY to JPY6.0bn due in part to decline in the number of member halls. The company expects the decrease in system-usage fee revenue to be greater than the forecasted 8.6% YoY decrease in the number member halls.

Gamecard-Joyco expects gross profit to fall 15.4% YoY to JPY6.3bn and GPM to fall 0.9pp to 42.0%. Little change from the sales breakdown in FY03/19 is expected, but the company forecasts lower GPM overall due mainly to the product mix change in FY03/20.

The company forecasts SG&A expenses at JPY5.4bn, an increase of 7.5% YoY. The company plans to spend especially heavily on R&D in FY03/20 for the development of new products and product development geared toward providing stable services, forecasting a 33.7% YoY increase in R&D expenses to JPY1.6bn.

Dividends

The company plans to pay an annual dividend of JPY35 per share (interim dividend of JPY17.5 and year-end dividend of JPY17.5; annual dividend of JPY35 per share in FY03/18).

Medium- to long-term Outlook

Gamecard-Joyco Holdings' medium-term financial performance is primarily driven by:

- ▷ Trends in installed pachinko and pachislot machine base;
- ▷ Trends in pachinko hall sales;
- ▷ Total number of pachinko halls (itself dependent on competition among halls and market contraction);
- ▷ Market share of halls using its systems;
- ▷ R&D expenses progress

In addition, Shared Research believes that regulatory amendment that took effect in February 2018 will pave the way for the introduction of "controlled machines", and accordingly see prospects of replacement demand for card-reading units (devices from which game balls are borrowed) over the medium term.

Installed pachinko and pachislot machine base, market size, and total pachinko hall count

Installed pachinko and pachislot machine base, market size (pachinko hall sales) and total number of pachinko halls are external factors that the company cannot directly control. All three have continued to show a trend of long-term decline, contributing to a continued harsh operating environment in FY03/19 (see the Market and value chain section for details).

Market share of member halls

Thanks to its merger with JOYCO SYSTEMS Corp. the company was able to capture a majority share of the market for prepaid cards used at pachinko and pachislot halls. The number of member halls is trending down due to new market entrant Daikoku Denki (TSE1: 6430) gaining market share.

Number of member halls, market share

	Dec. 2009	Dec. 2010	Dec. 2011	Dec. 2012	Dec. 2013	Dec. 2014	Dec. 2015	Dec. 2016	Dec. 2017	Dec. 2018
Number of member halls	5,451	5,429	5,047	4,974	4,836	4,529	4,272	4,020	3,778	3,482
YoY	-3.1%	-0.4%	-7.0%	-1.4%	-2.8%	-6.3%	-5.7%	-5.9%	-6.0%	-7.8%
Market share	53.3%	53.3%	52.1%	51.7%	50.9%	48.7%	46.7%	45.1%	43.6%	42.0%

Source: Shared Research based on data from Prepaid System Association

R&D expenses

- ▷ In response to the ongoing decline in sales that began in FY03/13, the company increased R&D spending steadily through FY03/16, developing new features for its G∞WIN'Z series, next-generation systems, and attempting to create new business areas. One major R&D project was the "inter-industry cooperation service". The company had been hoping to establish the service, which was built around an electronic money service, but after a review of potential profitability and the return on investment, the company decided it would be difficult to continue and halted development in FY03/16. Due to the additional cost of cancelling this project, the company's R&D spending swelled to JPY3.9bn in FY03/16.
- ▷ R&D spending declined sharply to JPY906mn in FY03/17. The decline stemmed mainly from the dropout of expenditures related to the canceled project in FY03/16 and being more focused and selective in its R&D investments. In FY03/18, R&D expenses further dropped to JPY393mn. In FY03/19, R&D expenses rose to JPY1.2bn due to progress in the development of products equipped with addiction prevention features and compliant with new regulations, as well as product development and other measures geared toward providing stable services.
- ▷ The company plans to increase R&D spending to JPY1.6bn in FY03/20 for the development of new products and services, as well as product development and other measures geared toward providing stable services.

R&D expenses

(JPYmn)	FY03/10 Par.	FY03/11 Par.	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Est.
Sales	32,834	37,005	43,575	39,545	34,192	25,741	23,885	20,405	16,928	17,375	15,000
R&D expenses	1,733	672	1,820	2,724	2,978	3,146	3,931	906	393	1,206	1,612
R&D expenses as % of sales	5.3%	1.8%	4.2%	6.9%	8.7%	12.2%	16.5%	4.4%	2.3%	6.9%	10.7%

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.
Note: Figures prior to FY03/12 are for Nippon Game Card.

Replacement demand for card-reading units driven by “controlled machines”

Shared Research understands that the regulatory amendment in February 2018 will pave the way for the introduction of “controlled machines” (see the Market and value chain section for details). Because “controlled machines” differ from conventional machines, a new card-reading unit is necessary when introducing “controlled machines”. This requirement may drive replacement demand for card-reading units (devices from which game balls are borrowed) over the medium term.

Regulatory amendment in February 2018 to pave the way for introduction of “controlled machines”

In the partial amendment to the Ordinance for Enforcement of the Act on Control and Improvement of Amusement Businesses and the Regulations Concerning Authorization and Model Approval for Amusement Machines (promulgated in September 2017, slated to take effect in February 2018), a machine equipped with a device that displays the number of game balls (i.e., a “controlled machine”) is added as a new gaming machine standard. Shared Research believes the amendment will pave the way for the introduction of “controlled machines,” which in turn may drive replacement demand for card-reading units (devices from which game balls are borrowed).

Differences between conventional and “controlled machines”

When using conventional machines, players borrow game balls from a card-reader unit (physical game balls are dispensed externally), which are then loaded and shot in the machine by operating a handle. If a game ball enters the prize-winning chucker (scoring hole), prize balls are dispensed externally from the machine. “Controlled machines,” on the other hand, adopt a structure in which there is no physical interaction between the players and the game balls. Our understanding at Shared Research is that instead of dispensing the game balls externally, game balls are managed through an electromagnetic system. In other words, the process of borrowing game balls via a card-reading unit is the same as for conventional machines, but game balls are no longer dispensed externally and the number of borrowed game balls corresponding to the purchased amount is indicated using an electromagnetic system. If the player wins prize balls, these are displayed as an increase in the total number of game balls.

Advantages of “controlled machines” over conventional machines

Shared Research understands that “controlled machines” offer several advantages over conventional machines such as a reduction in gambling addiction, prevention of fraud, enhanced freedom in machine layout, and cost reductions for pachinko halls.

- management of information on game balls released should curb the gambling nature of pachinko machines and contribute to a reduction in gambling addiction
- The adoption of a structure that removes physical interaction between the players and the game balls should support fraud prevention
- Compared with the conventional mechanism that re-uses game balls across a number of machines using a supply device, “controlled machines” re-use game balls in a single machine, eliminating the need for a supply device. This allows pachinko halls to have greater freedom in machine layout and lower costs

Although details are not yet clear, the company is seeing similar demand for controlled machines for pachinko slot machines, just as it did for pachinko machines.

Business

Business description

Gamecard-Joyco Holdings Inc., a holding company founded in April 2011, operates a prepaid-card system business for pachinko machines and it is the market leader in terms of number of members (pachinko halls). Nippon Game Card and JOYCO SYSTEMS Corp. are both 100% subsidiaries.

Business model

Nippon Game Card provides third-party issuer prepaid-card systems to pachinko halls (hereafter halls). JOYCO SYSTEMS provides house-issuer card payment systems for halls. As of the end of March 2019, there were 3,401 halls using JOYCO SYSTEMS's card payment systems (market share of 41.6%).

Prepaid-card system and pachinko and pachislot machines

Most pachinko machines are card reader (CR) models. CR models rely on prepaid cards, and players obtain pachinko balls directly from the pachinko machine using their card.

There are two ways to play a CR model pachinko machine.

- The first is when players purchase a prepaid card from a card-vending terminal.
- The second, and predominant, way is to insert money directly into a card-reading unit attached to a pachinko machine, which issues a prepaid IC card on the spot with the monetary information recorded on the IC chip, and balls are then dispensed based on that information.
- Customers can play on any machine with a card-reading unit installed.
- When done playing, a refund can be obtained using the same card from a separate card-balance refund terminal. The company supplies all components of both systems, including equipment and cards themselves.

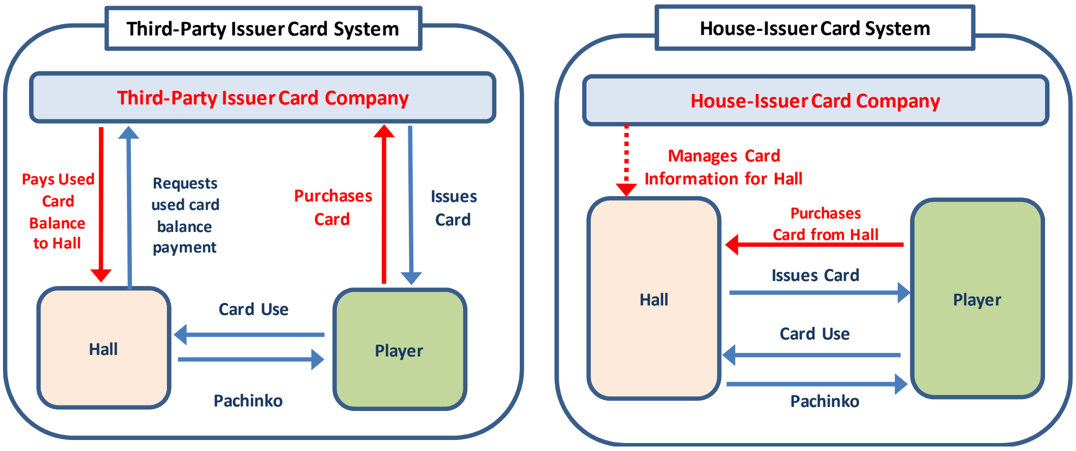
While CR model pachislot machines do not exist, there are a growing number of halls who install token-dispensing units for pachislot machines that allow use of the same prepaid-card system (and therefore the same card by individual players) for both pachinko and pachislot machines in the same hall.

Third-party issued card system vs. house-issued card system

There are two types of prepaid-card systems:

- **Third-party issuer system**: here the card company (i.e., the "third party"), is responsible for payment settlement between the hall and player.
- **House-issuer system (proprietary issuance)**: the company offering the card system merely manages the information stored on cards. The hall operator issues cards and settles payments with players directly.

As of May 2019, Nippon Game Card was the only company in the industry operating a third-party issuer system. On the other hand, JOYCO offers a house-issuer system.



Source: Shared Research based on company data

The advantages of the third-party issuer system compared to the house-issuer system are as follows:

- ▷ **Complete accounting transparency**: all payments to the hall are made through the card company.
- ▷ **Superior consumer protection**: even if a hall goes out of business, the card company will pay the remaining balance to card holders (However, when done playing, most players turn remaining balance in their cards into cash at a card-balance refund terminal installed at pachinko halls within the same day).

The disadvantage of a third-party issuer system is higher development and running costs of the system. This is due to card companies being responsible for settlements so it has to ensure the security and reliability of the system, which increases the costs compared to house-issuer systems. Shared Research estimates the costs for third-party issuer systems are about 30% to 40% higher than house-issuer systems. Apart from this, Shared Research understands that functionally both types of systems are similar.

Relevant regulations

While the pachinko prepaid-card industry itself is not directly subject to any laws or regulations the company’s clients, halls, are governed by numerous regulations (Law on Control and Improvement of Amusement Businesses, National Public Safety Commission's Rules, Prefectural Ordinances). In order to actually use a card-reading unit it is necessary to acquire permission from and notify the authorities. Consequently, in the event that any of the various laws and regulations governing pachinko halls are revised, the company’s business may be affected when selling and installing card units to halls.

Finally, in accordance with the Settlement of Funds Act (enacted on April 1, 2010; previously known as Act on Regulation, etc. of Advanced Payment Certificates) Nippon Game Card is registered with the Kanto Regional Financial Bureau as a “third-party issuer”. This regulation requires the company to deposit over 50% of the unused face value on its cards for card balance insurance purposes.

Main product

B∞LEX

Released in November 2009, B∞LEX had become the company’s mainstay product. The device can be easily attached to existing company products, additional functionality (e.g. ball-counting systems) can be added at any time, and similarly, ball-counting systems to each pachinko machine can be easily removed. It is a full-color display.

Ball-counting systems

Ball-counting systems are devices installed onto card-reading units connected to individual pachinko machines that measure the number of dispensed balls. In the past, players put dispensed balls into boxes at the end of play, and pachinko hall staff carried these boxes to and poured into an automated counting machine (known as a Jet Counter). However, a box full of balls is heavy and the staff needs to carry it for counting, particularly difficult and time consuming task when large winnings are involved. Winning players also need new empty boxes, further increasing burden on personnel and driving up labor costs.

Amidst the challenging market environment, halls have taken to cost cutting as a means to boost profits, such as through reducing staff headcount and paring back on installation costs. This means that to sell well, prepaid-card systems too must contribute to reducing operating costs and enhancing customer satisfaction. The company claims it is possible to reduce pachinko hall staff to approximately one-half to one-third of their present amount by the introduction of ball-counting systems. Moreover, these systems would contribute to an improved working environment by eliminating the need for employees to carry heavy boxes of pachinko balls.

With the propagation of operations with low-priced balls such as one-yen pachinko, there have been calls for measures to prevent customers from taking balls won at one-yen machines and using them to play at four-yen machines (effectively borrowing low-price balls to play at machines delivering regular-price payouts) in pachinko halls that house both types of machine. Ball-counting systems also serve as a preventative measure against this kind of diversion.

The company was late in developing such a system compared to competitors, but the arrival in November 2009 of the B∞LEX line allowed its card-reading units to be equipped with ball-counting systems. B∞LEX's ease of use as well as its functional flexibility allowing installation of the ball-counting units at any time, received high user acclaim.

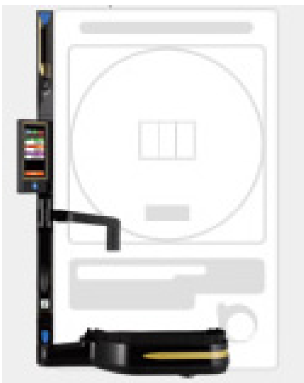
G∞WIN'Z

In March 2015, Gamecard-Joyco launched G∞WIN'Z, the successor to B∞LEX. It is the company's mainstay product as of May 2019. In addition to the features of B∞LEX, pachinko hall operators can select whether to use G∞WIN'Z with card subtraction or ball subtraction system machines (different methods of passing on consumption tax to customers). G∞WIN'Z also features a full-color 5-inch LC screen that can display and transmit original movies and still images, and transmit promotional movies for amusement machines. It also has a removable nozzle for dispensing balls into the trays of the amusement machines.

Two methods of collecting consumption tax: Shared Research understands that thus far ball and token lending charges included tax, with hall operators shouldering the tax burden. But new and renovated stores are increasingly installing equipment with systems designed to handle the consumption tax hike of April 2014. The **card subtraction system** maintains the same quantity of balls and tokens and subtracts the cost—plus the consumption tax—from the amount loaded on the user's prepaid card. By contrast, the **ball subtraction system** keeps the cost the same, but reduces the amount of balls or tokens to compensate for consumption tax. The disadvantage of the card subtraction system is that prepaid card balances become too granular (units of a single yen) for the player to use the entire balance.

G∞WIN'Z

(Pachinko) unit installation



(Pachislot) token dispenser installation

Source: Company data

Earnings structure

Earnings structure

(JPYmn)	FY03/10 Par.	FY03/11 Par.	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.
Sales	**32,834**	**37,005**	**43,575**	**39,545**	**34,192**	**25,741**	**23,885**	**20,405**	**16,928**	**17,375**
YoY	6.0%	12.7%	-	-9.2%	-13.5%	-24.7%	-7.2%	-14.6%	-17.0%	2.6%
Equipment sales	16,650	21,336	25,978	22,295	18,506	11,395	10,654	8,167	5,732	6,949
YoY	22.2%	28.1%	-	-14.2%	-17.0%	-38.4%	-6.5%	-23.3%	-29.8%	21.2%
% of sales	50.7%	57.7%	59.6%	56.4%	54.1%	44.3%	44.6%	40.0%	33.9%	40.0%
Card sales	4,865	4,797	5,530	5,587	4,854	4,229	3,957	3,609	3,170	2,963
YoY	-7.4%	-1.4%	-	1.0%	-13.1%	-12.9%	-6.4%	-8.8%	-12.2%	-6.5%
% of sales	14.8%	13.0%	12.7%	14.1%	14.2%	16.4%	16.6%	17.7%	18.7%	17.1%
System-usage fees	10,793	10,421	11,581	11,230	10,409	9,612	8,808	8,148	7,584	6,950
YoY	-6.4%	-3.4%	-	-3.0%	-7.3%	-7.7%	-8.4%	-7.5%	-6.9%	-8.4%
% of sales	32.9%	28.2%	26.6%	28.4%	30.4%	37.3%	36.9%	39.9%	44.8%	40.0%
Others	524	450	485	432	422	503	465	479	440	514
Gross profit	**9,660**	**11,199**	**13,093**	**11,884**	**10,980**	**9,665**	**8,413**	**8,250**	**7,871**	**7,446**
YoY	-6.4%	15.9%	-	-9.2%	-7.6%	-12.0%	-13.0%	-1.9%	-4.6%	-5.4%
GPM	29.4%	30.3%	30.0%	30.1%	32.1%	37.5%	35.2%	40.4%	46.5%	42.9%
Equipment sales	1,904	3,333	3,757	2,569	2,356	1,187	554	673	703	737
YoY	16.5%	75.1%	-	-31.6%	-8.3%	-49.6%	-53.3%	21.5%	4.5%	4.8%
YoY	11.4%	15.6%	14.5%	11.5%	12.7%	10.4%	5.2%	8.2%	12.3%	10.6%
% of gross profit	19.7%	29.8%	28.7%	21.6%	21.5%	12.3%	6.6%	8.2%	8.9%	9.9%
Card sales	2,971	2,828	3,199	3,285	2,952	2,811	2,468	2,261	2,029	1,889
YoY	-13.3%	-4.8%	-	2.7%	-10.1%	-4.8%	-12.2%	-8.4%	-10.3%	-6.9%
YoY	61.1%	59.0%	57.8%	58.8%	60.8%	66.5%	62.4%	62.6%	64.0%	63.8%
% of gross profit	30.8%	25.3%	24.4%	27.6%	26.9%	29.1%	29.3%	27.4%	25.8%	25.4%
System-usage fees	5,044	5,213	6,261	6,028	5,600	5,523	5,340	5,169	5,022	4,648
YoY	-7.8%	3.4%	-	-3.7%	-7.1%	-1.4%	-3.3%	-3.2%	-2.8%	-7.4%
YoY	46.7%	50.0%	54.1%	53.7%	53.8%	57.5%	60.6%	63.4%	66.2%	66.9%
% of gross profit	52.2%	46.5%	47.8%	50.7%	51.0%	57.1%	63.5%	62.7%	63.8%	62.4%
Others	-259	-175	-125	0	71	143	50	145	116	173
SG&A expenses	**8,093**	**6,877**	**8,633**	**9,216**	**9,216**	**8,848**	**9,854**	**6,331**	**4,274**	**5,023**
SG&A-to-sales ratio	24.6%	18.6%	19.8%	23.3%	27.0%	34.4%	41.3%	31.0%	25.2%	28.9%
Personnel expenses	1,749	1,818	2,206	2,228	2,278	2,164	2,163	2,139	1,611	1,578
R&D expenses	1,733	672	1,820	2,724	2,978	3,146	3,931	906	393	1,206
Others	4,611	3,493	4,607	4,264	3,960	3,538	3,760	3,286	2,270	2,239
Operating profit	**1,566**	**4,322**	**4,459**	**2,668**	**1,764**	**816**	**-1,440**	**1,919**	**3,596**	**2,423**
YoY	-41.4%	176.0%	-	-40.2%	-33.9%	-53.7%	-	-	87.4%	-32.6%
OPM	4.8%	11.7%	10.2%	6.7%	5.2%	3.2%	-6.0%	9.4%	21.2%	13.9%

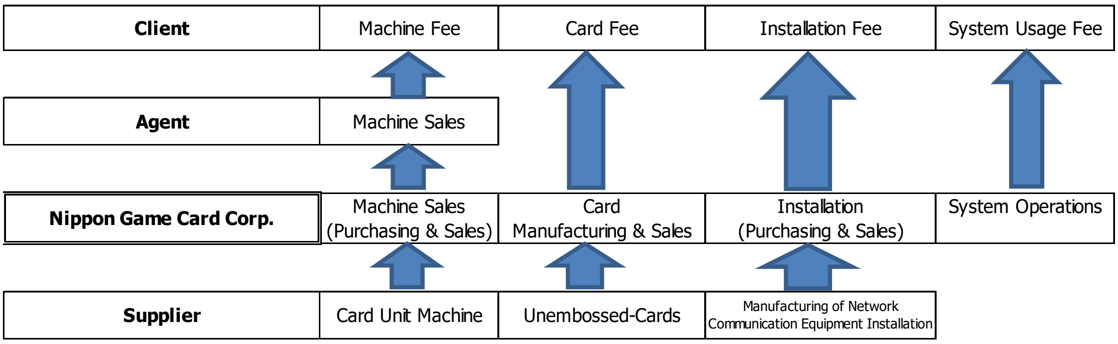
Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.

Sales

The company's revenues comprise of four main components:

- Equipment sales
- Card sales
- System-usage fee revenue
- Other revenues (such as, equipment installation and maintenance)

Shared Research thinks the company's business resembles that of a mobile network operator. The company's equipment sales roughly correspond to handset sales by mobile network operators while card sales are comparable to network operators' usage-based tariffs, such as call rates and packet usage fees, while system-usage fees mirror network operators' basic monthly fees.



Source: Shared Research based on company data

Note: Unembossed-cards refer to prepaid cards yet to be encoded with the required information.

Equipment sales (40.0% of total sales, 9.9% of total gross profit in FY03/19)

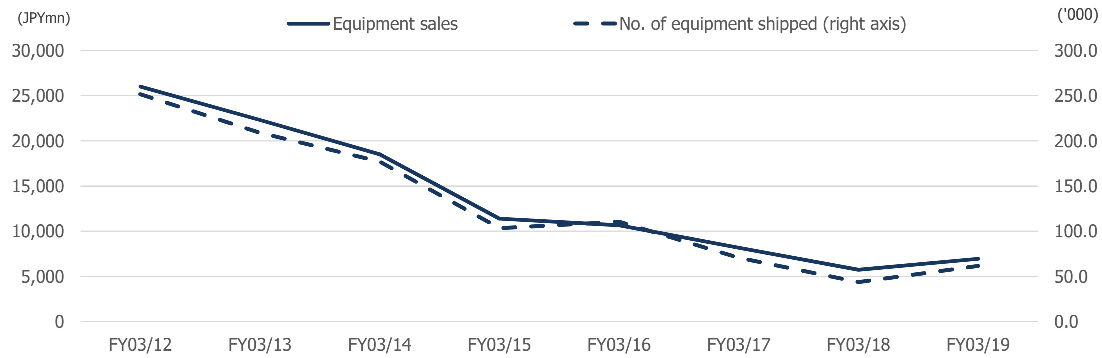
The company sells via distributors, card systems, token dispensers, and card-balance refund terminals to halls. Equipment sales are calculated by multiplying the amount of equipment units sold in each category by the prices for each type of equipment. The number of equipment units sold changes based on openings and closures of pachinko halls, equipment replacement demand, and market competition. The selling price fluctuates according to the company's sales strategy.

Card systems: Devices located between (CR model) pachinko machines. They dispense balls and are necessary to calculate card cash balances.
Token dispensers: Devices that dispense pachislot tokens.
Card-balance refund terminals: Devices that calculate card balances after play is finished and refund any remaining balances to players.

Card systems and token dispensers, which are the company's main product, are procured from Mamiya-OP Co. (TSE1: 7991), International Card System Co. (a subsidiary of Sankyo Co. [TSE1: 6417]) and other companies.

According to the company, the standard replacement cycle for equipment in pachinko halls is roughly five to ten years, with additional capex beyond the replacement cycle driven by equipment upgrades as new functionality comes into the market (e.g., new ball-counting systems etc.).

Equipment sales and number of equipment shipped



Note: Equipment sales are represented by the solid line (in units of JPY1mn) and the number of equipment shipped is represented by the dotted line (in units of 1,000 equipment units delivered)

	FY03/12	FY03/13	FY03/14	FY03/15	FY03/16	FY03/17	FY03/18	FY03/19
No. of equipment shipped ('000)	251.7	209.0	177.1	103.4	110.5	70.7	43.6	61.7
YoY	-	-17.0%	-15.3%	-41.6%	6.9%	-36.0%	-38.3%	41.5%
Equipment sales (JPYmn)	25,978	22,295	18,506	11,395	10,654	8,167	5,732	6,949
YoY	-	-14.2%	-17.0%	-38.4%	-6.5%	-23.3%	-29.8%	21.2%

Source: Shared Research based on company data

Card sales (17.1% of total sales, 25.4% of total gross profit in FY03/19)

Card sales are comprised of the sale of actual cards, information management fees, and booking of unredeemed card balances.

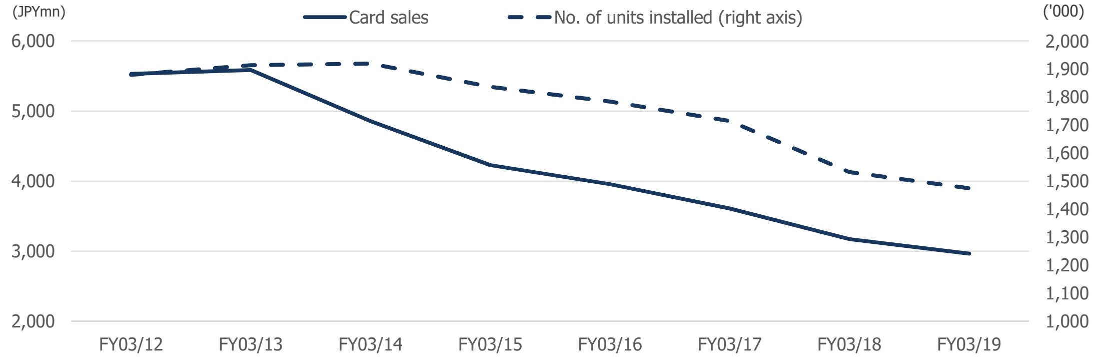
▷ Card sales denote the purchase of prepaid cards at pachinko halls and mainly moves according to the number of prepaid cards sold.

- Information management fees denote the fees the company receives from pachinko halls when a card settlement occurs after a customer plays pachinko. These fees are determined by the amount spent by players on their cards. The majority of card sales come from information management fees.

Prepaid cards are information recording media used to manage pachinko hall sales (ball and token fees). Since 2000 contactless IC cards have superseded one-time use magnetic cards as the industry standard.

- Booking of unredeemed card balances denotes a practice in accordance with The Corporation Tax Act, which stipulates that after four years any unused balances on issued cards purchased by players should be booked as income. Both unused balances and corresponding income have been declining as the industry moved from magnetic card to IC card use. This is because more players using IC cards tend to cash out their unused balances compared to players using magnetic cards.

Card sales and number of units installed



Note: Card sales are represented by the solid line (in units of JPY1mn) and the number of units installed is represented by the dotted line (in units of 1,000 systems installed)

	FY03/12	FY03/13	FY03/14	FY03/15	FY03/16	FY03/17	FY03/18	FY03/19
No. of units installed ('000)	1,879	1,914	1,919	1,836	1,784	1,715	1,532	1,474
YoY	0.0%	1.9%	0.3%	-4.3%	-2.8%	-3.9%	-10.6%	-3.8%
Card sales (JPYmn)	5,530	5,587	4,854	4,229	3,957	3,609	3,170	2,963
YoY	-	1.0%	-13.1%	-12.9%	-6.4%	-8.8%	-12.2%	-6.5%

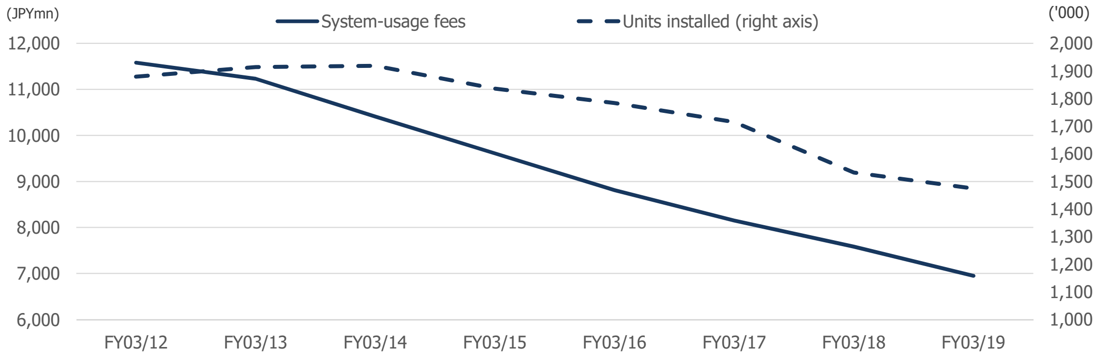
Source: Shared Research based on company data

System-usage fees (40.0% of total sales, 62.4% of total gross profit in FY03/19)

The company collects a recurring system-usage fee from member halls based on the number of prepaid card systems installed.

The company's prepaid-card system is based on a design by NTT Data Corp. (TSE1: 9613) and system modifications, such as improvements and addition of new functions, are outsourced to NTT Data. NTT Data also handles the collection of card usage information and data processing.

System-usage fees and number of units installed



Note: System-usage fees are represented by the solid line (in units of JPY1mn) and the number of units installed is represented by the dotted line (in units of 1,000 systems installed)

	FY03/12	FY03/13	FY03/14	FY03/15	FY03/16	FY03/17	FY03/18	FY03/19
Units installed ('000)	1,879	1,914	1,919	1,836	1,784	1,715	1,532	1,474
YoY	-	1.9%	0.3%	-4.3%	-2.8%	-3.9%	-10.6%	-3.8%
System-usage fees (JPYmn)	11,581	11,230	10,409	9,612	8,808	8,148	7,584	6,950
YoY	-	-3.0%	-7.3%	-7.7%	-8.4%	-7.5%	-6.9%	-8.4%

Source: Shared Research based on company data

Others (equipment installation and maintenance)

Equipment installation (card-reading units etc.) and maintenance is conducted by the company's distributors, such as SANKYO, based on contracts with halls. Installation of network communication equipment for prepaid-card systems (known as a "T-BOX") is outsourced to separate contractors, and the company then invoices halls for the installation cost.

A T-BOX (Terminal Box) is a data-collection unit used in the prepaid-card systems the company provides to halls. The T-BOX collates sales information and other data from the installed card-reading units and token-dispensing units within a hall. This information is then transmitted to a data center, which consolidates all the data for management of halls.

Gross profit

Gamecard-Joyco's GPM fluctuates in the range of 30–50%, changing based on the sales breakdown. Card sales and system-usage fees command higher GPMs than the other categories.

- In card sales, the majority of gross profit comes from information management fees (handling commissions for account settlements of card balances). The gross profit margin for card sales generally exceeds 60%. Given that for information management fees the gross profit margin is 100%, it is possible to further infer that sales of prepaid cards (booked as a "media fee") are relatively unprofitable for the company.
- Gross profit margin for system-usage fees tends to exceed 60%, with this part of the business contributing over 60% to the overall gross profit.
- In contrast, in FY03/19 the GPM for equipment sales was only 10.6%, lower than other income sources. Even though equipment sales comprise 40.0% of the company's overall sales they accounted for only 9.9% of gross profit. Shared Research believes that the impact on profits of a decline in equipment unit sales will be limited and the company is likely to generate a steady stream of income from information management and system-usage fees.

SG&A expenses

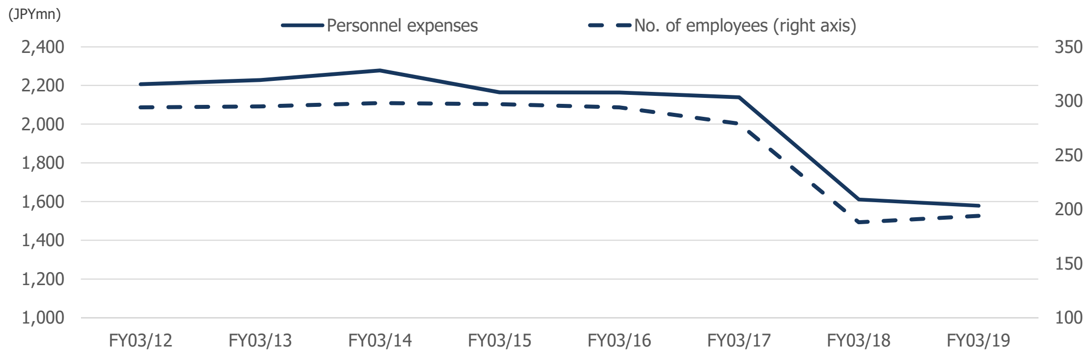
The company's SG&A expenses are mainly personnel expenses (31.4% of SG&A expenses in FY03/19) and R&D expenses (24.0%), but also include rent, depreciation, commission expenses, etc.

Expenses fell overall during the ten-year period from FY03/10 through FY03/19, peaking in FY03/2016 and falling substantially through FY03/18.

Personnel expenses

Personnel expenses decreased significantly in FY03/18, falling 32.6% YoY due to implementation of a voluntary retirement program in April 2017.

Personnel expenses and number of employees



Note: Personnel expenses are represented by the solid line (in units of JPY1mn) and the number of employees is represented by the dotted line (in units of 1 employee)

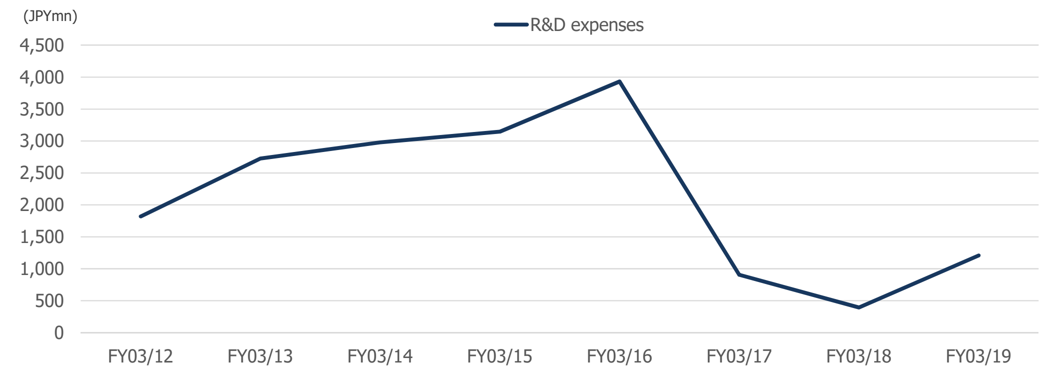
	FY03/12	FY03/13	FY03/14	FY03/15	FY03/16	FY03/17	FY03/18	FY03/19
No. of employees	294	295	298	297	294	279	188	194
YoY	-	0.3%	1.0%	-0.3%	-1.0%	-5.1%	-32.6%	3.2%
Personnel expenses (JPYmn)	2,206	2,228	2,278	2,164	2,163	2,139	1,611	1,578
YoY	-	1.0%	2.2%	-5.0%	0.0%	-1.1%	-24.7%	-2.0%

Source: Shared Research based on company data

R&D expenses

R&D expenses grew through FY03/16, but sharply decreased in FY03/17 and FY03/18 as the company reviewed its product development system and refined its development projects.

R&D expenses



(JPYmn)	FY03/12	FY03/13	FY03/14	FY03/15	FY03/16	FY03/17	FY03/18	FY03/19
R&D expenses	1,820	2,724	2,978	3,146	3,931	906	393	1,206
YoY	-	49.7%	9.3%	5.6%	25.0%	-77.0%	-56.6%	206.9%

Source: Shared Research based on company data

Strengths and weaknesses

Strengths

- **Leading company within the industry.** The company has the largest market share both in terms of number of halls using its systems and the overall card settlement value. Shared Research thinks this gives the company an advantage in identifying customer needs and factoring these needs into new product development ahead of the competition.
- **Pachinko/pachislot manufacturers as major shareholders.** The company's major shareholders are leading pachinko/pachislot machine manufacturers, such as SANKYO Co. (TSE1: 6417), Sammy Inc. (a subsidiary of Sega Sammy Holdings Inc. (TSE1: 6460)), and Heiwa Corp. (TSE1: 6412). For a company that develops critical ancillary features for pachinko machine manufacturers, such as prepaid-card systems and card-reading units, these capital ties provide it with an advantageous position in co-operating with pachinko/pachislot machine manufacturers
- **Specialization in prepaid-card systems.** Unlike its competitors, who also deal with other peripheral devices (such as prize exchange systems, membership systems and call lights) for both pachinko and pachislot machines, the company specializes purely in prepaid-card systems. This means it can collaborate with other leading companies in other areas who produce different types of peripheral devices. If new halls were opening up systematically, this could allow companies offering a one-stop shop model bundling a variety of peripheral pachinko devices together plenty of scope to increase market share, however, this is not the case. Instead, demand is currently driven by upgrades of existing facilities and even then equipment tends to be upgraded in piece-meal fashion. Nippon Game Card's cross-compatibility with other peripheral device makers' products in this environment may be thus seen as advantageous.

Weaknesses

- **Shrinking market.** The pachinko market is continuing to shrink. As the dominant player within the industry the company is easily affected by market trends.
- **Single source of income.** The company's core market is shrinking and while the company could theoretically move into other businesses to grow, it is currently focused on the core business making its earnings highly susceptible to the vagaries of the pachinko market.
- **Regulated industry.** The company's client base of halls is strictly regulated by laws such as the Law on Control and Improvement of Amusement Businesses. By extension, the company's financial performance is also affected by such regulations.

Market and value chain

Market overview

As for the company's earnings, trends in the installed pachinko machine base affect its Equipment Sales segment; revenues for card sales (essentially, information management fees or handling commissions for account settlements of card balances) are affected by halls' sales trends; while hall numbers are the swing factor for system-usage fees. Therefore, when looking at the company's earnings structure it is necessary to focus on the earnings environment and competitive pressure among halls, in addition to trends in the overall size of the pachinko market.

The Japan Productivity Center estimated the total domestic leisure market at JPY69.9tn (+0.2% YoY) in fiscal 2017 (source: White Paper on Leisure 2018). Pachinko/pachislot market (total lending charge of pachinko balls) was estimated at JPY19.5tn (-4.3% YoY). The pachinko/pachislot market has created a large presence to account for around 28% of the overall leisure market.

Industry trend

Shared Research focuses on the following indicators to gauge the state of the pachinko/pachislot industry.

Key indicators for pachinko/pachislot industry

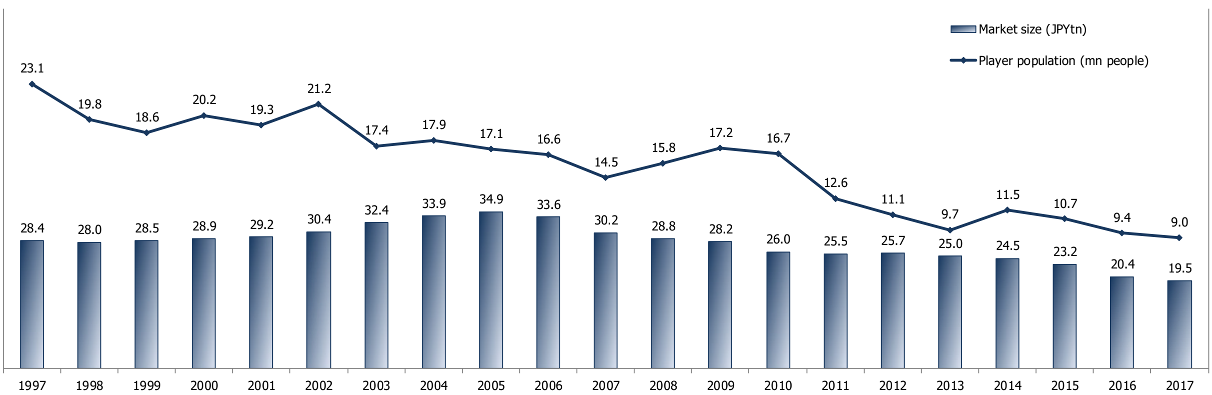
Indicator	Key figures	CAGR	Reference
Number of players	9.0mn (2017)	-4.7% (past 10 years)	In a long-term downtrend
Pachinko/pachislot market size	JPY19.5tn (2017)	-4.3% (past 10 years)	Declining since 2005 along with game-playing population
Number of pachinko halls	10,596 (2017)	-2.5% (past 10 years)	Shrinking with pachinko/pachislot market Average number of machines installed per hall rising
Number of machines installed	4.43mn (2017)	-0.4% (past 10 years)	In a mild downtrend

Source: Shared Research based on various sources
Note: replacement rate = number of machines sold ÷ number of machines installed

Downward trend in player population and declining number of pachinko halls

- ▷ The pachinko industry has been experiencing a gradual long-term decline in the player base and market size. The player base fell to 9.0mn in 2017 compared to 29.0mn in 1995.
- ▷ Until 2005, the market size grew despite a shrinking player population as average annual spend per player was growing. The market size (total lending charge of pachinko balls) peaked in 2005 at JPY34.9tn, and fell to JPY19.5tn in 2017.

Pachinko players and market size



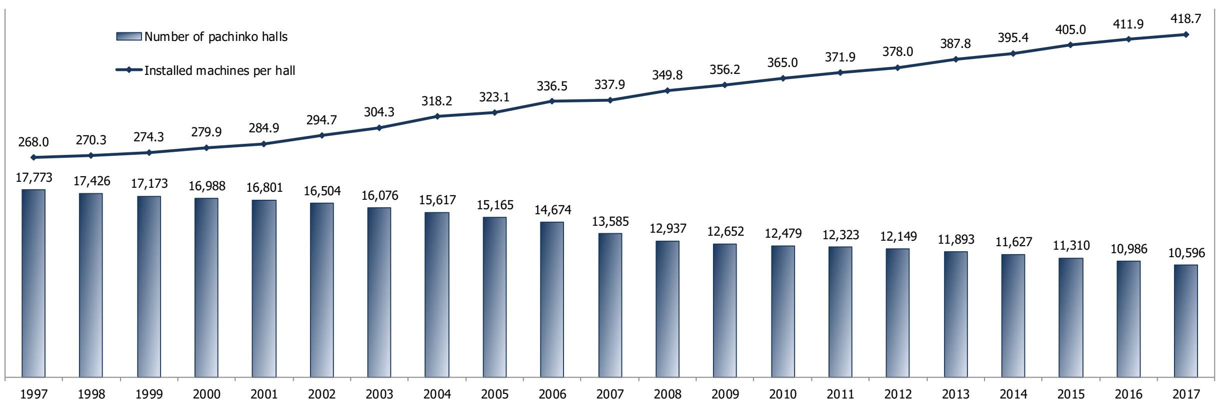
	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Player population (mn people)	23.1	19.8	18.6	20.2	19.3	21.2	17.4	17.9	17.1	16.6	14.5	15.8	17.2	16.7	12.6	11.1	9.7	11.5	10.7	9.4	9.0
Market size (JPYtn)	28.4	28.0	28.5	28.9	29.2	30.4	32.4	33.9	34.9	33.6	30.2	28.8	28.2	26.0	25.5	25.7	25.0	24.5	23.2	20.4	19.5

Source: Shared Research based on White Paper on Leisure

Diverging trends among halls

- The number of pachinko halls declined to 10,596 in 2017 from 17,773 in 1997 (source: National Police Agency).
- However, despite the growing downward trend in the number of pachinko halls, the number of installed machines has remained generally unchanged at 4.43mn in 2017 and 4.73mn in 1997. On the other hand, hall sizes have become larger, increasing to an average of 419 installed machines per hall in 2017 from 268 machines in 1997.
- A decrease in the amount of cash flow available for new investments has forced some smaller operators to sell or shut operations, while larger chains appear to be gaining scale, highlighting continued polarization of the market.

Number of pachinko halls and installed pachinko machines per hall



	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Number of pachinko halls	17,773	17,426	17,173	16,988	16,801	16,504	16,076	15,617	15,165	14,674	13,585	12,937	12,652	12,479	12,323	12,149	11,893	11,627	11,310	10,986	10,596
Installed machines per hall	268.0	270.3	274.3	279.9	284.9	294.7	304.3	318.2	323.1	336.5	337.9	349.8	356.2	365.0	371.9	378.0	387.8	395.4	405.0	411.9	418.7

Source: Shared Research based on National Police Agency

Industry regulations

Current gaming machine regulations that may affect the company’s earnings are as follows. To curb excessive gambling nature, voluntary regulations and a regulatory amendment for pachinko and pachislot machines have been implemented since 2015.

- The industry association implemented voluntary regulations for pachinko machines in November 2015 and on pachislot machines in December 2015. Further voluntary regulations were introduced for pachislot machines in October 2017.
- In February 2018, following the passage of the Bill for the Promotion of Integrated Resort Facilities as a measure to curb gambling addiction, a partial amendment to the Ordinance for Enforcement of the Act on Control and Improvement of Amusement Businesses and the Regulations Concerning Authorization and Model Approval for Amusement Machines was enforced. The proposed amendment includes a change in the number of pachinko balls released per play.

Effect of measures to curb the gambling nature of pachinko machines

In an effort to reduce the attraction of pachinko as a form of gambling and restore it as a form of entertainment, the pachinko machine manufacturers association (the Japan Game Machine Industry Association) agreed to change the lower limit of the pachinko machine jackpot probability range (the chance of “winning big”) to 1/320 (from 1/400 as of May 2015). Effective November 2015, this self-imposed regulatory change meant that game machine manufacturers would no longer be able to sell and newly install extremely competitive “max-type” machines (jackpot probability of 1/370–1/399 but with bigger winnings) that were the mainstay at pachinko halls prior to October 2015.

From May 2016, the Game Machine Industry Association also voluntarily introduced a lower maximum occurrence of a game feature called “probability fluctuation” (the jackpot rate after a successful jackpot) from around 80% to 65% (yet the rules for pachinko machines were changed again in November 2018 and the 65% limit to maximum occurrence of probability fluctuation was removed.)

This latest self-regulatory move was precipitated by pachinko halls increasingly installing “max-type” machines (reached more than 40% of all machines in pachinko halls at one point) to meet demand from hard-core pachinko players. As max-machines pushed up the average cost of playing pachinko, the number of players declined. The industry sought to tighten standards to reduce the addictive gambling aspect of pachinko, with the hope of bringing back more players into pachinko halls.

Impact of voluntary industry restrictions on pachislot machines

Voluntary industry restrictions on pachislot machines (Regulation 5.5)

In September 2014, the Security Communication Association changed its testing methodology for pachislot machines. Previously, pachislot machines had to register a minimum payout rate of 55% (at least 11 out of 20 tokens inserted) during a random test run. The new standard called for the same minimum payout rate while testing under a play mode set for the lowest possible payout rate. That same month, the pachislot machine manufacturers association (the Japan Game Machine Industry Association) adopted a new standard that would prohibit penalty features from irregular pressing of machines and also mandated that machine makers switch to motherboards with AT/ART functionality.

Prior to this change, pachislot machines incorporated a main circuit board and a sub board, both of which controlled the payout rate of game tokens. Effective December 2015, the new industry standard requires the sub-board program that controls game token discharge to be incorporated into the main circuit board.

AT Machine: An abbreviation of Assist Time, an AT Machine is a type of pachislot machine. During regular play, even if the user selects the winning icons, they do not match up on the screen because of the push-order rule. However, when the AT function is installed, if the machine selects the AT mode, a display screen on the pachislot machine will indicate the order of the buttons to press to match up the icons on the screen, allowing the user to increase their coins.

ART Machine: An abbreviation of Assist Replay Time, an ART Machine is a type of pachislot machine. When this function is installed, if the machine enters ART mode, the odds of a replay increase, allowing the user to continue playing without using up coins.

Voluntary industry restrictions on pachislot machines (Regulation 5.9)

In June 2016, Liaison Conference of Pachislot Machine Manufacturers explained that they would implement voluntary regulations, which limit ART functions for pachislot machines installed after October 2017, and classified pachislot machines that comply with these voluntary regulations as 5.9 models. New units of the current 5.5 machine models can only be installed up to the end of September 2017.

Shared Research understands that for 5.9 models there will be two sections related to the indicated navigation function (such as the push-order): a regular section, which will prohibit the ART mode, and a section in which the ART mode is allowed. Machines randomly select the transition from the regular to the ART mode, and the ART mode section will limit the total amount of tokens released to 3,000 by ending the game after a maximum of 1,500 games. The chance of the ART mode being selected is limited to under 70%.

Partial amendment to the Ordinance for Enforcement of the Act on Control and Improvement of Amusement Businesses and the Regulations Concerning Authorization and Model Approval for Amusement Machines

In September 2017, the NPA promulgated a partial amendment to the Ordinance for Enforcement of the Act on Control and Improvement of Amusement Businesses and the Regulations Concerning Authorization and Model Approval for Amusement Machines, which was brought into effect in February 2018.

The proposed amendment, which aims to reduce the addiction of pachinko as a form of gambling, limits the game ball-releasing capacity of amusement machines as well as the maximum number of game balls released per jackpot. It also introduces a “settings” feature for pachinko machines.

Tightening regulations on the number of balls released

The amendment newly stipulates a rule which curbs the ball-releasing capacity of amusement machines over a set playing span of four hours.

- ▷ Under this rule, the total number of game balls released during a four-hour play must be less than 1.5 times the total number of game balls shot by the player.

> A pachinko machine releases 100 balls in one minute, therefore it will release 24,000 in four hours (100 balls x 240 minutes). As this new rule stipulates that the amount of balls won must be no greater than 150% the number of balls released, in this example the maximum balls won is 36,000 (24,000 x 1.5). Subtracting 12,000 balls, that would be roughly a JPY50,000 payout (assuming one ball is 4 yen).

- ▷ Existing technical specifications and standards for one hour and 10 hours were also tightened to the same degree so that the total number of game balls released was reduced to about 2/3 of the current level.
- ▷ For pachislot machines, a new regulation similar to that of pachinko machines also for a four-hour playing span (1,600 shots in the case of pachislot machines) was put in place.

Regulations on the number of game balls released per jackpot

- ▷ For pachinko machines, the maximum number of game balls released per jackpot was reduced from the current upper limit of 2,400 to 1,500.
- ▷ For pachislot machines, the maximum number of game tokens was reduced from 480 to 300.

Addition of gaming machine specifications that allow easy access to information on game balls released

Gaming machine specifications that allow easy access to information on game balls released will be set with an aim to prevent excessively heightened addiction.

> The Definitions of Terms Used in Technical Standards section of Appended Table 2 of the Regulations Concerning the Certification of Gaming Machines and Model Inspections, Etc., included in the partial amendment to the Ordinance for Enforcement of the Act on Control and Improvement of Amusement Businesses and the Regulations Concerning Authorization and Model Approval for Amusement Machines (promulgated in September 2017), added the definition for Game Ball Number Display Device as "a device installed in gaming machines that adopt a structure that removes physical interaction between players and game balls, and in which the total number of balls that can be shot by a player is recorded using an electromagnetic system and can be displayed accordingly." This definition refers to "controlled machines".

Addition of managers' operations

Pachinko hall managers will be required to provide information to customers and take other necessary measures to prevent customers' excessive game playing.

Regulatory change schedule

Pachislot machines that passed model tests prior to January 2018 (pachislot 5.9) will be legally marketable until January 2021. Pachislot machines (pachislot 6.0) which meet the new regulations that went into effect in February 2017 were introduced to the market in October 2018.

Pachinko machines formatted on the old rules (those releasing 2,400 balls) that passed model tests prior to January 2018 will also be legally marketable until January 2021. Pachinko machines fit to the new regulations were introduced to the market in August 2018.

Barriers to entry

Barriers to entry are extremely high given that the company operates in an oligopolistic market and its client base of pachinko halls is subject to strict regulations, such as the Law on Control and Improvement of Amusement Businesses.

Competitive environment

Number of member halls using prepaid-card systems and market share

As of end March 2019, 8,168 halls (8,491 halls as of end March 2018) used prepaid-card systems, representing approximately 80% of the total 10,060 halls in Japan (as of end December 2018; 10,596 halls at end December 2017). The penetration rate for prepaid-card systems among halls has not changed much.

Halls using prepaid-card systems and market share

	FY03/16	FY03/17	FY03/18	FY03/19
Halls using prepaid-card systems	9,044	8,830	8,491	8,168
Nippon Game Card and JOYCO SYSTEMS	4,184	3,957	3,674	3,401
Market share	46.3%	44.8%	43.3%	41.6%
Glory Nasca	2,098	2,076	2,044	2,006
Market share	23.2%	23.5%	24.1%	24.6%
Mars Engineering	2,051	2,011	1,948	1,891
Market share	22.7%	22.8%	22.9%	23.2%
Daikoku Denki	527	616	679	743
Market share	5.8%	7.0%	8.0%	9.1%
Total number of halls	11,310	10,986	10,596	10,060

Source: Shared Research based on data from the National Police Agency's Community Safety Bureau and the Prepaid System Association.
Note: Total number of halls represent the number at end December of each year.

The pachinko prepaid-card industry is an oligopoly dominated by three companies: Gamecard-Joyco Holdings, GLORY NASCA Ltd. (a subsidiary of Glory Ltd. (TSE1: 6457) created from an April 2011 merger with Creation Card Co.), and Mars Engineering Corp. (TSE1: 6419).

Based on sales as of the end of March 2019, the company had 41.6% market share of halls using its prepaid-card system, making it easily the largest company in the space. GLORY NASCA followed with 24.6%, and Mars Engineering had 23.2%.

The main difference between Nippon Game Card and its competitors is the company's business model is based on a third-party issuer card system, while the other two provide predominantly house-issuer card systems. (JOYCO SYSTEMS actually sells house-issuer card system but for the company as a whole third-party issuer card systems are the dominant system). Additionally, the other two companies sell equipment used outside of the pachinko and pachislot space, whereas Nippon Game Card specializes purely in providing pachinko pre-paid card systems.

Please refer to the Business section for a detailed explanation on the differences between third-party issuer and house-issuer card systems. It is hard to judge whether Nippon Game Card's strategy of solely focusing on prepaid-card systems and collaborating with other companies for peripheral devices (for example, Daikoku Denki Co. [TSE1: 6430]) is superior to providing clients with other peripheral devices, as GLORY NASCA Ltd. and Mars Engineering do. Some halls, such as top-tier hall DYNAM (operates 450 halls nationwide as of March 2019), exclusively use Mars Engineering's systems, leaving no room for Nippon Game Card or other peripheral device manufacturers. Nonetheless, not all halls rely solely on one equipment maker, as DYNAM does. Moreover, GLORY NASCA and Mars Engineering's market shares for peripheral devices are not particularly dominant. Thus, focusing on its core business and partnering with other dominant specialist companies does have its advantages.

After 2012, Daikoku Denki, which has a high market share in computer systems used in pachinko and pachislot halls, entered the prepaid-card systems market. Despite being a latecomer to the market, Daikoku Denki has steadily built up its following, and as of the end of FY03/19, had 743 member halls for a 9.1% market share. Daikoku Denki, like Mars Engineering, appears to be retaining clients by providing them with other peripheral devices.

Historical earnings results

Full-year FY03/19 results

- ▷ Sales: JPY17.4bn (+2.6% YoY)
- ▷ Operating profit: JPY2.4bn (-32.6% YoY)
- ▷ Recurring profit: JPY2.4bn (-32.7% YoY)
- ▷ Net income*: JPY1.4bn (-38.3% YoY)

*Net income refers to net income attributable to parent company shareholders.

Business environment and the company's initiatives

Even as pachinko hall operators that comprise the company's primary customer base continue to have an uncertain future due to ongoing study of gambling addiction countermeasures accompanying the Integrated Resort Promotion Act and a tighter regulatory environment reflecting the revised regulations enforced in February 2018 (Regulations Partially Amending the Ordinance for Enforcement of the Act on Control and Improvement of Amusement Business, etc.), there are still some medium-sized and large chain operators looking to maintain or even improve their competitive position by opening up more pachinko halls in and around Japan's major cities, especially in the Kanto and Kinki regions.

However, the number of pachinko halls continues to decline as operators remain under pressure from tighter regulations on machines offering high potential payouts; loss of players to other forms of entertainment following the spread of smartphones and mobile gaming; and lower average spend stemming from an increase in the number of hall operators offering low-priced balls.

Gamecard-Joyco has focused on maintaining or improving its ability to provide proposals for a transition to and expandability of its mainstay product G∞WIN'Z. Turning mounting need for measures to prepare for the consumption tax increase into an opportunity, the company increased the number of units it sold and temporarily halted the decline in its overall sales.

Overview of full-year FY03/19 results

Sales fell as the company was unable to halt the decline in system usage fee revenue from a decline in the number of member halls accompanying market contraction. In terms of profits, GPM fell to 42.9% (-3.6pp YoY) due to a fall in the relatively profitable system usage fee revenue. In addition, due to development aimed at producing a stable, ongoing product supply, SG&A expenses increased and profit lines from operating profit on down declined YoY.

Sales breakdown

- ▷ Equipment sales rose 21.2% YoY to JPY6.9bn on an increase in equipment unit sales to 61,637 units (+41.5% YoY). The company actively strengthened its relationships with distributors to maintain or increase its member hall share and actively rolled out machine replacement promotion measures at member halls. Equipment unit sales also increased in Q4 FY03/19 thanks to replacement demand encouraged by the upcoming consumption tax hike.
- ▷ Card sales were JPY3.0bn (-6.5% YoY), reflecting lower information management fees accompanying a drop in the total value of cards issued, and a drop in the number of cards sold. The fall in the total value of cards issued was attributable to a decline in the number of member halls to 3,401 (-273 or -7.4% YoY). Cancellations of member hall agreements due to closures outnumbered acquisitions of new member halls. In addition to the decline in the number of member halls, a drop in average spend due to the spread of operations with low-priced balls resulted in a drop in the total value of cards issued.
- ▷ System-usage fees fell 8.4% YoY to JPY7.0bn. The number of card-reading units fell 3.8% YoY to 1,474,000 due to the drop in the number of member halls noted above. As a result, system-usage fees the company collects from member halls based on the number of card-reading units installed also fell.
- ▷ Others (equipment installation and maintenance) posted sales of JPY514mn (+16.8% YoY).

Gross profit by product type

Gross profit declined 5.4% YoY to JPY7.4bn. GPM also fell 3.6pp YoY to 42.9%. Gross profit for equipment sales increased YoY while those for in card sales and system-usage fees decreased. GPM dropped because equipment sales, which have a relatively low GPM, took up a larger share of overall sales. However, GPMs from card sales and system-usage fees remained flat YoY.

- Gross profit for equipment sales was JPY737mn (+4.8% YoY), and GPM was 10.6% (-1.7pp YoY). Higher gross profit reflected an increase in equipment sales, despite lower GPM.
- Gross profit for card sales was JPY1.9bn (-6.9% YoY), and GPM was 63.8% (-0.3pp YoY).
- Gross profit for system-usage fees was JPY4.6bn (-7.4% YoY), and GPM was 66.9% (+0.7pp YoY). The company strove to ensure profitability by reducing costs.

SG&A expenses

SG&A expenses totaled JPY5.0bn (+17.5% YoY), of which personnel expenses were JPY1.6bn (-2.0% YoY) and R&D expenses were JPY1.2bn (+206.5% YoY). R&D expenses increased due to progress in the development of products equipped with addiction prevention features and compliant with new regulations, as well as product development and other measures geared toward providing stable services.

As a result, operating profit, recurring profit, and net income attributable to parent company shareholders fell YoY.

Q3 FY03/19 results

- Sales: JPY12.9bn (-1.7% YoY)
- Operating profit: JPY2.6bn (-12.6% YoY)
- Recurring profit: JPY2.6bn (-12.4% YoY)
- Net income*: JPY1.7bn (-15.1% YoY)

*Net income refers to net income attributable to parent company shareholders.

Business environment and the company's initiatives

Pachinko hall operators that comprise the company's primary customer base were impacted by a tighter regulatory environment reflecting the revised regulations enforced in February 2018 (Regulations Partially Amending the Ordinance for Enforcement of the Act on Control and Improvement of Amusement Business, etc.) and the implementation of the Basic Bill on Gambling Addiction Countermeasures in July 2018. The occurrence of several natural disasters also had a negative impact.

The company is maintaining and growing its share of member halls through aggressive marketing activities, as well as strengthening its relationships with distributors, actively promoting equipment replacements, and carrying out aggressive equipment sales leveraging its strong financial base.

Overview of cumulative Q3 FY03/19 results

Sales declined due to a decrease in the number of member halls and intensified competition as the market continued to contract. In terms of profits, in addition to the decline in sales, the GPM declined to 44.7% (-2.3pp YoY). All profit lines below gross profit declined.

Progress vs. full-year FY03/19 forecasts

Versus full-year FY03/19 company forecasts, sales reached 85.9% (77.5% of full-year results in Q3 FY03/18), operating profit 128.1% (81.5%), recurring profit 128.2% (81.4%), and net income attributable to parent company shareholders 120.7% (85.8%). In cumulative Q3 FY03/19, all profit categories below operating profit exceeded forecasts, and had greater progress rates than in Q3 FY03/18. In addition to the greater-than-expected number of equipment units sold, card sales and system-usage fees surpassed forecasts. However, in Q4 (January to March 2019), due to an increase in R&D expenses, the company expects

SG&A expenses to be higher than in any of the previous quarters in FY03/19, causing loss at all profit categories below operating profit.

Sales breakdown

- Equipment sales rose 8.0% YoY to JPY5.0bn on an increase in equipment unit sales to 40,739 units (+21.2% YoY). According to the company, demand for conversion to more efficient machines, such as ball-counting systems, also increased due to labor shortages. In addition, the company actively strengthened its relationships with distributors to maintain or increase its member hall share and actively rolled out machine replacement promotion measures at member halls. These efforts resulted in higher equipment unit sales.
- Card sales were JPY2.2bn (-7.2% YoY), reflecting lower information management fees accompanying a drop in the total value of cards issued, and lower media fees caused by a drop in the number of cards sold. The fall in the total value of cards issued was attributable to a decline in the number of member halls to 3,482 (-296 or -7.8% YoY). Cancellations of member hall agreements due to closures outnumbered acquisitions of new member halls. In addition to the decline in the number of member halls, a drop in average spend due to the spread of operations with low-priced balls resulted in a drop in the total value of cards issued.
- System-usage fee revenue fell 8.3% YoY to JPY5.3bn due to the drop in the number of member halls noted above. System-usage fees the company collects from member halls based on the number of card-reading units installed fell
- Others (equipment installation and maintenance) posted sales of JPY383mn (+15.0% YoY)

Gross profit per sales item

Gross profit declined 6.4% YoY to JPY5.8bn. GPM also fell 2.3pp YoY to 44.7%. Gross profit dropped for all product types, excluding those in others (equipment installation and maintenance), and GPM also decreased because equipment sales, which have a relatively low GPM took up a larger share of overall sales. However, GPMs from card sales and system-usage fees remained flat YoY.

- Gross profit for equipment sales was JPY666mn (-8.1% YoY), and GPM was 13.3% (-2.3pp YoY). Equipment sales rose owing to an increase in the number of equipment units sold, but gross profit fell on lower GPM
- Gross profit for card sales was JPY1.4bn (-6.7% YoY), and GPM was 64.1% (+0.3pp YoY)
- Gross profit for system-usage fees was JPY3.5bn (-7.5% YoY), and GPM was 67.0% (+0.6pp YoY)

SG&A expenses

SG&A expenses totaled JPY3.2bn (-0.9% YoY), of which personnel expenses were JPY1.2bn (-4.5% YoY) and R&D expenses were JPY408mn (+49.5% YoY). R&D expenses increased due to progress in the development of products equipped with addiction prevention features and compliant with new regulations, as well as product development and other measures geared toward providing stable services.

As a result, operating profit, recurring profit, and net income attributable to parent company shareholders fell YoY.

1H FY03/19 results

Consolidated results for 1H FY03/19 were as follows:

- Sales: JPY8.5bn (-1.1% YoY)
- Operating profit: JPY1.7bn (-10.6% YoY)
- Recurring profit: JPY1.7bn (-10.4% YoY)
- Net income*: JPY1.2bn (-15.9% YoY)

*Net income refers to net income attributable to parent company shareholders.

Pachinko hall operators that comprise the company's primary customer base, were impacted by the revised regulations (Regulations Partially Amending the Ordinance for Enforcement of the Act on Control and Improvement of Amusement Business, etc.) enforced in February 2018 and development of the Basic Bill on Gambling Addiction Countermeasures. The number of people playing pachinko continued to decline as sources of entertainment diversified with the proliferation of the internet and smartphones, causing the operating environment to remain difficult. Meanwhile, measures responding to the social need to curb gambling addiction are expected, with the establishment of operations with low-priced balls and the spread of machines that suppress the gambling element in order to conform to revised regulations (Regulations Partially Amending the Ordinance for Enforcement of the Act on Control and Improvement of Amusement Business, etc.).

Gamecard-Joyco group strove to streamline its operation with the theme of “completion of structural reform and maximization of its effects” as a core policy. The company promoted marketing activity, planned to maintain and grow the share of member halls, strengthened relationships with distributors, and promoted replacements at existing member halls. In terms of R&D, in order to revitalize the industry, the company simultaneously proceeded with development of products to conform to new regulations and curb gambling addiction, and with planning and development to offer a continuous and stable service. As a result, although the operating environment was difficult, sales remained similar to the level of FY03/18. Profit declined due to a fall in GPM to 45.7% (-2.4pp YoY).

Versus full-year FY03/19 company forecasts, 1H sales reached 56.4% (1H FY03/18 sales reached 50.5% of full-year FY03/18 results), operating profit 86.3% (53.7%), recurring profit 86.3% (53.6%), and net income attributable to parent company shareholders 84.0% (60.4%). The company announced an upward revision to its FY03/19 full-year forecast in November 2018 but 1H performance in profit was high compared to revised projections. For 2H, Gamecard-Joyco Holdings Inc. predicts an overall drop in sales, particularly in equipment sales, as well as concentrated recording of R&D expenses.

Sales breakdown

- Equipment sales rose 11.3% YoY to JPY3.2bn on an increase in equipment unit sales to 25,786 units (+23.7% YoY). According to the company, investment demand for peripheral devices in pachinko halls rose in 1H due to growing expectations for gaming machines compliant with new regulations. Demand for conversion to more efficient machines, such as ball-counting systems, also increased due to labor shortages. In addition, the company actively strengthened its relationships with distributors to maintain or increase its member hall share and actively rolled out machine replacement promotion measures at member halls. These efforts resulted in higher equipment unit sales.
- Card sales were JPY1.5bn (-7.7% YoY), reflecting lower information management fees accompanying a drop in the total value of cards issued, and lower media fees caused by a drop in the number of cards sold. The fall in the total value of cards issued was attributable to a decline in the number of member halls to 3,543 (-283 or -7.4% YoY). The share of member halls also fell to 42.5% (43.3% at end FY03/18). Acquisition of new member halls outpaced member hall loss due to closings or other reasons. In addition to the decline in the number of member halls, a drop in average spend due to the spread of operations with low-priced balls resulted in a drop in the total value of cards issued.
- System-usage fee revenue fell 8.1% YoY to JPY3.6bn due to the drop in the number of member halls noted above.
- Others (equipment installation and maintenance) posted sales of JPY241mn (+10.6% YoY).

Gross profit declined 5.9% YoY to JPY3.9bn. GPM also fell 2.4pp YoY to 45.7%. Gross profit dropped for all product types, excluding those in others (equipment installation and maintenance), and GPM also decreased because equipment sales, which have a relatively low GPM took up a larger share of overall sales.

- Gross profit for equipment sales was JPY443mn (-3.1% YoY), and GPM was 13.9% (-2.1pp YoY).
- Gross profit for card sales was JPY961mn (-7.8% YoY), and GPM was 64.7% (even YoY).
- Gross profit for system-usage fees was JPY2.4bn (-7.1% YoY), and GPM was 66.9% (+0.7pp YoY).

SG&A expenses totaled JPY2.1bn (-1.9% YoY), of which personnel expenses were JPY789mn (-7.4% YoY) and R&D expenses were JPY281mn (+81.3% YoY). R&D expenses increased due to progress in the development of products equipped with addiction prevention features and compliant with new regulations, as well as product development and other measures geared toward providing stable services.

As a result, operating profit, recurring profit, and net income attributable to parent company shareholders fell YoY.

Q1 FY03/19 results

- Sales: JPY4.1bn (-7.4% YoY)
- Operating profit: JPY960mn (+1.1% YoY)
- Recurring profit: JPY963mn (+0.5% YoY)
- Net income*: JPY693mn (-0.1% YoY)

*Net income refers to net income attributable to parent company shareholders.

For pachinko hall operators that comprise the company's primary customer base, the operating environment remained difficult. Fewer people are playing pachinko since the sources of entertainment are diversifying and operations with low-priced balls are becoming the norm. Additionally, there is uncertainty over the impact of the revised regulations (Regulations Partially Amending the Ordinance for Enforcement of the Act on Control and Improvement of Amusement Business, etc.) enforced in February 2018 and development of the Basic Bill on Gambling Addiction Countermeasures.

Gamecard-Joyco group continued to provide ideas useful to revitalize the industry and to operate pachinko halls, swiftly and precisely understanding the social needs as well as the needs of pachinko hall operators and pachinko fans. The company continuously strove to streamline its operation with the theme of “completion of structural reform and maximization of its effects” as a core policy. As a result, sales declined on lower number of equipment unit sales and member halls, but all profit items under operating profit remained flat YoY owing to a drop in SG&A expenses.

Versus full-year FY03/19 company forecasts, Q1 sales reached 29.0% (Q1 FY03/18 sales reached 26.3% of full-year FY03/18 results), operating profit 80.0% (26.4%), recurring profit 80.3% (26.7%), and net income attributable to parent company shareholders 86.6% (29.9%). Q1 results had high progress rates versus plan as unit prices of equipment were in line with expectations and majority of R&D expenses were expected to be booked in 2H.

Sales breakdown

- Equipment sales declined 5.5% YoY to JPY1.5bn on a drop in equipment unit sales to 11,208 units (-6.7% YoY). Amid uncertainties accompanying the revised regulations involving amusement business enacted in February 2018, investment interests in peripheral equipment of pachinko halls have dwindled, leading to a limited number of hall openings. As only a few new pachinko halls opened, equipment unit sales primarily came from replacement demand at existing member stores.
- Card sales were JPY730mn (-11.0% YoY), reflecting lower information management fees accompanying a drop in the total value of cards issued, and lower media fees caused by a drop in the number of cards sold. The fall in the total value of cards issued was attributable to a decline in the number of member halls to 3,612 (-277 or -7.1% YoY). In addition to the decline in the number of member halls, a drop in average spend due to the spread of operations with low-priced balls resulted in a drop in the total value of cards issued.
- System-usage fee revenue fell 8.1% YoY to JPY1.8bn due to the drop in the number of member halls noted above.
- Others (equipment installation and maintenance) posted sales of JPY118mn (+2.6% YoY).

Gross profit declined 6.4% YoY to JPY1.9bn. However, GPM improved 0.5pp YoY to 47.3%. Gross profit fell for all products except for others, but GPM rose.

- Gross profit for equipment sales was JPY235mn (-1.7% YoY), and GPM was 15.9% (+0.6pp YoY). Equipment sales mainly came from replacement demands at existing member halls.

- Gross profit for card sales was JPY472mn (-9.8% YoY), and GPM was 64.7% (+0.9pp YoY).
- Gross profit for system-usage fees was JPY1.2bn (-6.9% YoY), and GPM was 66.9% (+0.9pp YoY). The GPM rose as usage of equipment for updates and booking of expenses was postponed.

SG&A expenses totaled JPY988mn (-12.6% YoY), of which personnel expenses were JPY362 (-13.0% YoY) and R&D expenses were JPY94mn (+14.6% YoY).

As a result, operating profit, recurring profit, and net income attributable to parent company shareholders were flat YoY.

Other information

History

Nippon Game Card

Early period (1989 to 1994)

At the time of Nippon Game Card's establishment in Osaka in August, 1989, pachinko halls were under the spotlight for tax evasion, fraud and other issues. As part of a drive to clean up the pachinko industry's image the industry regulator, the National Police Agency, decided to introduce prepaid-card systems which enabled card companies to monitor pachinko hall sales in order to increase hall operator transparency.

Based on this, three main companies—all with capital ties to Japan's leading trading houses—were established to develop and implement the prepaid-card initiative:

- Nihon Leisure Card System K.K.: Established in 1988, largest initial shareholder was Mitsubishi Corp. (TSE1: 8058)
- Nippon Game Card: Established in 1989, largest initial shareholder was Sumitomo Corp. (TSE1: 8053)
- Nihon Advanced Card System K.K.: Established in 1995, largest initial shareholder was Mitsui & Co. (TSE1: 8031)

From 1993 onward the company grew rapidly as CR model (prepaid-card system) pachinko machines proliferated.

Turmoil (1995 to 2001)

By 1996 the pachinko industry had become plagued by card counterfeiting. The company had to focus on prevention of counterfeiting while combating the growing fallout from it. At the same time, numerous new market entrants had appeared, offering house-issuer card systems with lower running costs—Mars Engineering Corp. (entering the market in 1999), JOYCO SYSTEMS Corp. (see section below), Seta Corp. (which entered the market in 2000 and is now known as Universal Entertainment Corp. (JASDAQ: 6425)), as well as Nasca Corp. and Creation Card Information System Co. (both of whom entered the market in 1998), which have since merged to form Glory Nasca Ltd.

Rebuilding (2001 onward)

In 2001, pachinko/pachislot machine manufacturer SANKYO Co. replaced Sumitomo Corp. as the company's largest shareholder. The company used this change as an opportunity to refocus its business on meeting pachinko halls' business needs. The company also merged with former third-party card issuer competitors Nihon Advanced Card System in October 2003, and with Nihon Leisure Card System in April 2008. In April 2006, the company listed on the JASDAQ Securities Exchange (now merged with the Tokyo Stock Exchange).

JOYCO SYSTEMS Corp.

JOYCO SYSTEMS Corp. was established in March 2001. Unlike Nippon Game Card, it provides house-issuer prepaid-card systems. Relatively cheap maintenance costs of its system initially allowed it to grow market share among halls in the prepaid-card market. However, as a late industry entrant the company faced a shrinking market early on, slowing its momentum. It then fell behind competitors in launching new products resulting in a decline in the number of halls using its system.

Gamecard-Joyco Holdings, Inc.

On April 1, 2011, Nippon Game Card and JOYCO SYSTEMS merged and established a joint holding company "Gamecard-Joyco Holdings, Inc." through a share transfer.

News and topics

November 2018

On **November 8, 2018**, the company announced revisions to its earnings forecasts.

Revised forecast for FY03/19

- Sales: JPY15.0bn (versus previous forecast of JPY14.2bn)
- Operating profit: JPY2.0bn (JPY1.2bn)
- Recurring profit: JPY2.0bn (JPY1.2bn)
- Net income*: JPY1.4bn (JPY800mn)
- EPS: JPY98.16 (JPY56.09)

*Net income refers to net income attributable to parent company shareholders.

Reason for revision

The company has continuously striven to streamline its operation with the theme of “completion of structural reform and maximization of its effects” as a core policy since FY03/18, and promoted aggressive sales activities. As a result, sales are expected to exceed initial forecasts.

At the same time, operating profit, recurring profit, and net income attributable to parent company shareholders are expected to exceed initial forecasts as a result of some development plans relating to the development of products in line with revised regulations (Regulations Partially Amending the Ordinance for Enforcement of the Act on Control and Improvement of Amusement Business, etc.) shifting to the next financial year or later.

Major shareholders

Top shareholders	Shares held ('000)	Shareholding ratio
SANKYO CO., LTD.	2,131	14.94%
DATA-ART, Inc.	632	4.43%
Heiwa Corporation	612	4.29%
Kyoraku Sangyo Co., Ltd.	611	4.29%
Sammy Inc.	611	4.29%
Daiichi Co., Ltd.	611	4.29%
Newgin Group	611	4.29%
Fujishoji Co., Ltd.	611	4.29%
SAXA, Inc.	510	3.57%
Sansei R&D Co., Ltd.	463	3.24%
SANYO BUSSAN K.K.	463	3.24%
Daito Giken, Inc.	463	3.24%
Takao Co., Ltd.	463	3.24%
Takeya Co., Ltd.	463	3.24%
Toyomaru Industy Co., Ltd.	463	3.24%
SUM	9,723	68.17%

Source: Shared Research based on company data
As of March 31, 2019

Company profile

Company Name	Head Office
Gamecard-Joyco Holdings, Inc.	Orix Ueno 1-Chome Building 1-1-10 Ueno Taito-ku Tokyo, Japan 110-0005
Phone	**Listed On**
+81-3-6803-0301	JASDAQ Standard
Established	**Exchange Listing**
April 1, 2011	April 1, 2011
Website	**Financial Year-End**
http://www.gamecard-joyco.co.jp/index.html	March
IR Contact	**IR Web**
Investor Relations & General Affairs Division	http://www.gamecard-joyco.co.jp/ir/
IR Mail	**IR Phone**
-	+81-3-5812-7595

About Shared Research Inc.

We offer corporate clients comprehensive report coverage, a service that allows them to better inform investors and other stakeholders by presenting a continuously updated third-party view of business fundamentals, independent of investment biases. Shared Research can be found on the web at http://www.sharedresearch.jp.

Current Client Coverage of Shared Research Inc.

Accordia Golf Trust
ADJUVANT COSME JAPAN CO., LTD.
Aeon Delight Co., Ltd.
Aeon Fantasy Co., Ltd.
Ai Holdings Corporation
and factory, inc.
ANEST IWATA Corporation
AnGes Inc.
Anicom Holdings, Inc.
Anritsu Corporation
Apaman Co., Ltd.
ARATA CORPORATION
Arealink Co.,Ltd.
Artspark Holdings Inc.
AS ONE CORPORATION
Ateam Inc.
Aucfan Co., Ltd.
AVANT CORPORATION
Axell Corporation
Azbil Corporation
AZIA CO., LTD.
AZoom, Co., Ltd.
BEENOS Inc.
Bell-Park Co., Ltd.
Benefit One Inc.
B-lot Co.,Ltd.
Broadleaf Co., Ltd.
Canon Marketing Japan Inc.
Career Design Center Co., Ltd.
Carna Biosciences, Inc.
CARTA HOLDINGS, INC
CERES INC.
Chiyoda Co., Ltd.
Chugoku Marine Paints, Ltd.
cocokara fine Inc.
COMSYS Holdings Corporation
CRE, Inc.
CREEK & RIVER Co., Ltd.
Daiichi Kigenso Kagaku Kogyo Co., Ltd.
Daiseki Co., Ltd.
DIC Corporation
Digital Arts Inc.
Digital Garage Inc.
Dream Incubator Inc.
Earth Corporation
Elecom Co., Ltd.
en-Japan Inc.
euglena Co., Ltd.
Evolable Asia Corp.
FaithNetwork Co., Ltd.
Ferrotec Holdings Corporation
FIELDS CORPORATION
Financial Products Group Co., Ltd.
FreeBit Co., Ltd.
FRONTEO, Inc.
Fujita Kanko Inc.
Gamecard-Joyco Holdings, Inc.
GCA Corporation
Good Com Asset Co., Ltd.
Grandy House Corporation
Hakuto Co., Ltd.
Hamee Corp.
Happinet Corporation
Harmonic Drive Systems Inc.
HOUSEDO Co., Ltd.
IDOM Inc.
IGNIS LTD.
i-mobile Co.,Ltd.
Inabata & Co., Ltd.
Infocom Corporation
Infomart Corporation
Intelligent Wave, Inc.
ipet Insurance CO., Ltd.
istyle Inc.
Itochu Enex Co., Ltd.
JSB Co., Ltd.
JTEC Corporation
J Trust Co., Ltd
Japan Best Rescue System Co., Ltd.
JINS HOLDINGS Inc.
JP-HOLDINGS, INC.
KAMEDA SEIKA CO., LTD.
Kenedix, Inc.
KFC Holdings Japan, Ltd.
KI-Star Real Estate Co., Ltd.
Kondotec Inc.
Kumiai Chemical Industry Co., Ltd.
Lasertec Corporation
LUCKLAND CO., LTD.
MATSUI SECURITIES CO., LTD.
Medical System Network Co., Ltd.
MEDINET Co., Ltd.
MedPeer,Inc.
Mercuria Investment Co., Ltd.
Micronics Japan Co., Ltd.
Milbon Co., Ltd.
MIRAIT Holdings Corporation
Monex Goup Inc.
MORINAGA MILK INDUSTRY CO., LTD.
NAGASE & CO., LTD
NAIGAI TRANS LINE LTD.
NanoCarrier Co., Ltd.
Net One Systems Co.,Ltd.
Nichi-Iko Pharmaceutical Co., Ltd.
Nihon Denkei Co., Ltd.
Nippon Koei Co., Ltd.
NIPPON PARKING DEVELOPMENT Co., Ltd.
NIPRO CORPORATION
Nisshinbo Holdings Inc.
NS TOOL CO., LTD.
OHIZUMI MFG. CO., LTD.
Oisix ra daichi Inc.
Oki Electric Industry Co., Ltd
ONO SOKKI Co., Ltd.
ONWARD HOLDINGS CO.,LTD.
Pan Pacific International Holdings Corporation
PARIS MIKI HOLDINGS Inc.
PIGEON CORPORATION
QB Net Holdings Co., Ltd.
RACCOON HOLDINGS, Inc.
Raysum Co., Ltd.
RESORTTRUST, INC.
ROUND ONE Corporation
RVH Inc.
RYOHIN KEIKAKU CO., LTD.
SanBio Company Limited
SANIX INCORPORATED
Sanrio Company, Ltd.
SATO HOLDINGS CORPORATION
SBS Holdings, Inc.
Seikagaku Corporation
Seria Co.,Ltd.
SHIFT Inc.
SHIP HEALTHCARE HOLDINGS, INC.
SIGMAXYZ Inc.
SMS Co., Ltd.
Snow Peak, Inc.
Solasia Pharma K.K.
SOURCENEXT Corporation
Star Mica Holdings Co., Ltd.
Strike Co., Ltd.
SymBio Pharmaceuticals Limited
Synchro Food Co., Ltd.
TAIYO HOLDINGS CO., LTD.
Takashimaya Company, Limited
Take and Give Needs Co., Ltd.
Takihyo Co., Ltd.
TEAR Corporation
Tenpo Innovation Inc.
3-D Matrix, Ltd.
TKC Corporation
TOKAI Holdings Corporation
TOYOBO CO., LTD.
Toyo Ink SC Holdings Co., Ltd
Toyo Tanso Co., Ltd.
Tri-Stage Inc.
VISION INC.
VISIONARY HOLDINGS CO., LTD.
WirelessGate, Inc.
YELLOW HAT LTD.
YOSHINOYA HOLDINGS CO., LTD.
YUMESHIN HOLDINGS CO., LTD.
Yume no Machi Souzou Iinkai Co., Ltd.
Yushiro Chemical Industry Co., Ltd.
ZAPPALLAS, INC.

Attention: If you would like to see companies you invest in on this list, ask them to become our client, or sponsor a report yourself.

Contact Details

Shared Research Inc.
3-31-12 Sendagi Bunkyo-ku Tokyo, Japan
URL: https://sharedresearch.jp
Phone: +81 (0)3 5834-8787
Email: info@sharedresearch.jp