

Drecom



(TSE Code: 3793 / Sector: Information and communication)

FY03/2024 First Quarter Result

GIR View

■ Highlights

Drecom announced Q1 FY03/2024 results and revised full-year FY03/2024 forecasts and dividend forecasts after the close of trading on July 27, 2023. Q1 results showed a significant decrease in sales and profit, and the company incurred an extraordinary loss due to the decision to terminate "*DACHIMEN DENSETSU G*", a new title provided by its subsidiary. Considering this, the company revised downward its full-year forecasts: net sales by 3.5 billion yen, operating income by 1.5 billion yen, recurring income by 1.45 billion yen, and net income attributable to owners of the parent (hereinafter "net income") by 1.1 billion yen. The net income forecast is now zero yen, and the dividend forecast has been changed from 5 yen per share to an undetermined amount.

The downward revision was necessitated by the weak performance of existing titles relative to expectations, the slow start of new titles released recently ("*GGGGG*" and "*DACHIMEN DENSETSU G*"), and a more cautious assumption for the next title in development, "*Wizardry Variants Daphne*".

In response to these changes in the environment, the company will focus on reinforcing its business structure this year. The company has decided to concentrate management resources, reduce costs, and seek business partners who collaborate on new titles to be released in the future (joint business), aiming for middle-risk/middle-return profile. This is a shift from the company's previous aggressive management stance, which aimed to maximize

earnings by distributing its own IPs through its own channel.

The new business in media segment is moving forward as had planned.

The poor performance of the most recently released titles and the withdrawal of the dividend forecast are disappointing news. That said, the company's downward revision of its earnings forecast and its declaration of a quick shift to a more defensive management approach are commendable. Going forward, investors need to watch the degree to which the company will be able to revitalize its existing titles and a release date for its next key title "*Wizardry Variants Daphne*", together with its details of the joint project.

■ Overview of the first quarter of the fiscal year ending March 31, 2024

In the first quarter (April-June), sales were 2.3 billion yen (-19.8% YoY), operating profit was 8 million yen (-99% YoY), recurring profit was 2 million yen (-99.7% YoY), and net loss was 440 million yen. Both sales and profits were down compared to the previous quarter.

This is due to lower sales of some existing titles, higher advertising costs associated with the release of new titles, and poor sales of new titles. Three of the 12 titles in operation are underperforming, but the unprofitability of new titles "*GGGGG*" and "*DACHIMEN DENSETSU G*" is particularly noticeable. The company is considering modifications to the former, such as converting it to a blockchain game, while it decided to terminate the latter



and recorded an extraordinary loss of 416 million yen due to impairment.

■ Revision of Corporate Forecast and Dividend Forecast for the Fiscal Year Ending March 31, 2024

Considering the weak Q1 progress, the company has revised its business plan in a prudent manner, particularly with regard to "*Wizardry Variants Daphne*", which is scheduled for release during this fiscal year. The company will conduct a second round of its user test around fall 2023 and evaluate the results before launching the game. The timing of the launch will also be pushed back from the previous plan.

As a result, the company revised its full-year sales forecast downward by 3.5 billion yen to 11.5 billion yen, mainly due to the revision of the contribution from new titles from the initial forecast of approximately 4.9 billion yen to approximately 1.8 billion yen. Partially offsetting the lower sales forecast were cost reductions in advertising and R&D (approx. 400 million yen each), resulting in an operating profit forecast of 500 million yen (revised downward by 1.5 billion yen), recurring profit forecast of 450 million yen (revised downward by 1.45 billion yen), and net income attributable to owners of the parent of zero yen (revised downward by 1.1 billion yen). The annual dividend forecast was changed from 5 yen per share to undecided.

"*Evil Prince and the Puppet*" will be released during this fiscal year, as previously planned. However, it will not contribute to earnings until the next fiscal year or later. In new business areas such as publishing, video, and Web3, the company plans to continue its main projects, including the launch of a comic/webtoon label and preparations for the release of "*Eternal Crypt - Wizardry*

BC-".

The company expects Q2 sales to be higher than in Q1, partly because one title distributed by another company will be changed to in-house distribution, and operating profit is expected to improve from Q1 due to cost reductions (according to the company's financial results briefing material).

■ A year of strengthening its business structure

The company continues to aim for annual sales growth of 20% or more and an operating margin of 15% in the next fiscal year and beyond. However, in light of the current challenging performance trends, the company intends to focus on strengthening its business structure during the current fiscal year.

This includes not only reviewing development and investment plans, reducing costs, and strengthening the profitability of existing businesses, but also selecting the most appropriate partners for each new title project and accepting investment in the form of joint venture. This is likely to improve the probability of success in launching new titles while reducing cost burden, resulting in a medium risk/medium return business profile. This is a shift from the company's previous policy of risk-taking by acquiring and distributing its own titles, but it is a swift and sensible decision given the current situation in which both two new in-house titles have fallen short of expectations. The company keeps aiming at acquiring and nurturing in-house IPs as much as appropriate over mid-term horizon.



■ Future Highlights

The first point to watch going forward will be the results of the leverage of existing titles and the early realization of the effects of cost reductions.

The more important point this fiscal year is the release of "*Wizardry Variants Daphne*". It is time to take a hard look at whether the second user test will yield satisfactory results and set a definite release date. Partners of its joint venture and the associated economic conditions are also critical.

Financial Data (Consolidated: Quarterly)

Figure 1 Statements of Income

(Millions of yen)

Accounting period	FY 03/20	FY 03/21	FY 03/22	FY03/23					FY03/24				
	Q1-Q4	Q1-Q4	Q1-Q4	Q1	Q2	Q3	Q4	Q1-Q4	Q1	Q2	Q3	Q4	CE
Sales	10,150	11,841	10,528	2,927	2,873	2,579	2,420	10,800	2,346				11,500
YoY	-5%	17%	-11%	10%	14%	-11%	-1%	3%	-20%				6%
Net sales	2,192	3,997	3,797	1,308	1,321	1,058	871	4,558	684				
YoY	53%	82%	-5%	26%	38%	3%	12%	20%	-48%				
Net sales margin	21.6%	33.8%	36.1%	44.7%	46.0%	41.0%	36.0%	42.2%	29.1%				
SG&A	1,575	1,944	2,205	491	530	566	690	2,277	675				
YoY	-22%	23%	13%	-8%	7%	-1%	14%	3%	37%				
Operating income	617	2,053	1,591	817	790	492	180	2,281	8				500
YoY	-	233%	-22%	62%	71%	9%	5%	43%	-99%				-78%
Operating income margin	6.1%	17.3%	15.1%	27.9%	27.5%	19.1%	7.5%	21.1%	0.4%				4.3%
Ordinary income	636	2,019	1,541	810	737	477	167	2,192	2				450
YoY	-	218%	-24%	64%	65%	9%	4%	42%	-100%				-79%
Net income	711	1,625	807	521	534	110	-7	1,159	-442				0
YoY	-	128%	-50%	74%	72%	-54%		44%					
Net Income Ratio	7.0%	13.7%	7.7%	17.8%	18.6%	4.3%	-0.3%	10.7%	-18.8%				0.0%

Source: Prepared by Global IR, Inc. based on company securities reports and company IR materials.

Note: CE=Company Estimate. Rounded to the nearest million yen, rounded to one decimal place *Calculated by Global IR, Inc.

Figure 2 Per Share Data

(Consolidated)

Accounting period	FY 03/17	FY 03/18	FY 03/19	FY 03/20	FY 03/21	FY 03/22	FY03/23
Total number of shares issued and outstanding (thousand shares)	14,371	28,742	28,819	28,894	28,976	29,073	29,130
EPS	29.7	-7.2	-60.5	25.0	57.0	28.3	40.7
EPS Adjusted	29.7	-	-	25.0	56.9	28.3	40.6
BPS	113.2	106.7	47.9	74.2	132.9	159.1	195.7
DPS	0.0	0.0	0.0	0.0	0.0	5.0	5.0

Source: Prepared by Global IR, Inc. based on company securities reports and company IR materials.

Note: Rounded to the nearest million yen, rounded to one decimal place *Calculated by Global IR, Inc.

Figure 3 Cash flows

(Millions of yen)

Accounting period	FY 03/17	FY 03/18	FY 03/19	FY 03/20	FY 03/21	FY 03/22	FY03/23
Depreciation and amortization	214	299	462	382	627	537	269
Cash flows from operating activities	846	-79	78	691	3196	1603	2666
Cash flows from investing activities	-456	-1,958	-123	-101	-1140	-1766	-2017
Cash flows from financing activities	1,345	2,288	-271	-1,188	969	-388	659

Source: Prepared by Global IR, Inc. based on company securities reports and company IR materials.

Note: Rounded to the nearest million yen, rounded to one decimal place *Calculated by Global IR, Inc.

Figure 4 Financial Data

(%)

Accounting period	FY 03/17	FY 03/18	FY 03/19	FY 03/20	FY 03/21	FY 03/22	FY03/23
Return on Assets (ROA)	16.7	-0.4	-16.8	9.5	25.2	16.0	20.0
Return on Equity (ROE)	35.5	-6.6	-78.3	41.0	55.0	19.4	22.9
Capital adequacy ratio	47.0	33.2	19.6	32.9	39.5	46.9	45.6

Source: Prepared by Global IR, Inc. based on company securities reports and company IR materials.

Note: Rounded to the nearest million yen, rounded to one decimal place *Calculated by Global IR, Inc.

Disclaimer

This report has been prepared by Global IR, Inc. (GIR) under a contractual arrangement with the company described in this report (“the company”). The report is provided for informational purposes only. It is not intended to solicit or recommend investment in the company’s securities. While the information and views contained in this report have been obtained from sources that GIR believes to be reliable, or created on the basis of publicly available information, no guarantee is offered with regard to their accuracy or completeness. Our analysis is in any case provided with an emphasis on accuracy and objectivity and pays the utmost attention to neutrality and independence. In addition, based on discussions with the relevant business owners, and others, and original on research, perspectives that we consider important to investors have been provided, on the basis that they are GIR's own opinions. GIR is not responsible for any loss or damage resulting from the use of this report. Investment decisions in the relevant corporate stock are at the reader's own judgment and responsibility.