

This PDF document is an updated note on the company. A comprehensive version of the report on the company, including this latest update, is available on [our website](#) and various professional platforms.

On **August 9, 2018**, SOURCENEXT Corporation announced earnings results for Q1 FY03/19.

Quarterly performance (JPYmm)	FY03/17				FY03/18				FY03/19				FY03/19	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	% of 1H	1H Est.
Sales	1,988	2,233	2,795	2,325	1,579	2,341	2,813	2,761	2,436				37.9%	6,418
YoY	29.1%	27.2%	34.0%	41.3%	-20.6%	4.8%	0.6%	18.8%	54.3%					63.7%
Gross profit	1,452	1,532	1,758	1,568	989	1,579	1,933	1,779	1,355					
YoY	35.8%	16.8%	15.9%	35.3%	-31.9%	3.1%	10.0%	13.5%	37.0%					
GPM	73.0%	68.6%	62.9%	67.4%	62.6%	67.4%	68.7%	64.4%	55.6%					
SG&A expenses	1,008	1,057	1,295	1,177	1,172	1,637	1,009	1,295	1,408					
YoY	22.9%	26.0%	27.3%	28.4%	16.3%	54.8%	-22.1%	10.1%	20.1%					
SG&A ratio	50.7%	47.3%	46.3%	50.6%	74.3%	69.9%	35.9%	46.9%	57.8%					
Operating profit	486	380	476	231	63	376	398	402	85				17.8%	478
YoY	74.2%	-17.2%	-3.2%	7.3%	-87.1%	-1.2%	-16.4%	73.7%	35.8%					9.1%
OPM	24.4%	17.0%	17.0%	9.9%	4.0%	16.0%	14.2%	14.5%	3.5%					7.4%
Recurring profit	497	382	472	242	65	380	400	414	85				17.7%	480
YoY	76.5%	-17.4%	-4.4%	6.9%	-86.9%	-0.5%	-15.2%	70.9%	30.6%					7.9%
RPM	25.0%	17.1%	16.9%	10.4%	4.1%	16.2%	14.2%	15.0%	3.5%					7.5%
Net income	338	257	311	165	86	242	259	675	49				14.3%	345
YoY	81.2%	-19.3%	-5.6%	5.3%	-74.5%	-6.1%	-16.8%	309.8%	-42.8%					5.3%
Net margin	17.0%	11.5%	11.1%	7.1%	5.5%	10.3%	9.2%	24.4%	2.0%					5.4%
Cumulative	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	% of FY	FY Est.
Sales	1,988	4,221	7,016	9,341	1,579	3,920	6,733	9,495	2,436				14.5%	16,807
YoY	29.1%	28.1%	30.4%	33.0%	-20.6%	-7.1%	-4.0%	1.6%	54.3%					77.0%
Gross profit	1,452	2,984	4,741	6,309	989	2,568	4,501	6,280	1,355					
YoY	35.8%	25.3%	21.7%	24.8%	-31.9%	-13.9%	-5.1%	-0.5%	37.0%					
GPM	73.0%	70.7%	67.6%	67.5%	62.6%	65.5%	66.9%	66.1%	55.6%					
SG&A expenses	1,008	2,065	3,360	4,537	1,172	2,371	3,818	5,114	1,408					
YoY	22.9%	24.5%	25.6%	26.3%	16.3%	14.8%	13.6%	12.7%	20.1%					
SG&A ratio	50.7%	48.9%	47.9%	48.6%	74.3%	60.5%	56.7%	53.9%	57.8%					
Operating profit	486	866	1,342	1,573	63	438	836	1,238	85				3.4%	2,499
YoY	74.2%	17.3%	9.1%	8.8%	-87.1%	-49.4%	-37.7%	-21.3%	35.8%					101.9%
OPM	24.4%	20.5%	19.1%	16.8%	4.0%	11.2%	12.4%	13.0%	3.5%					14.9%
Recurring profit	497	879	1,351	1,593	65	445	845	1,259	85				3.4%	2,502
YoY	76.5%	18.2%	9.2%	8.8%	-86.9%	-49.4%	-37.5%	-21.0%	30.6%					98.8%
RPM	25.0%	20.8%	19.3%	17.1%	4.1%	11.4%	12.5%	13.3%	3.5%					14.9%
Net income	338	595	906	1,071	86	328	586	1,261	49				2.7%	1,818
Net margin	81.2%	17.8%	8.6%	8.1%	-74.5%	-45.0%	-35.3%	17.8%	-42.8%					44.1%

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

Sales by channel (quarterly) (JPYmm)	FY03/17				FY03/18				FY03/19					
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4		
Smartphones and telecom carriers	388	401	391	384	364	290	282	270	238					
YoY	34.7%	36.4%	15.0%	17.1%	-6.4%	-27.7%	-27.9%	-29.7%	-34.6%					
SOURCENEXT online store	974	939	1,152	941	899	968	1,414	1,109	1,046					
YoY	30.0%	3.6%	10.6%	4.1%	-7.7%	3.1%	22.7%	17.9%	16.4%					
Elec. mass retailers, third-party websites	572	826	1,159	870	185	921	928	1,172	817					
YoY	31.3%	61.3%	74.8%	136.4%	-67.6%	11.5%	-19.9%	34.7%	341.6%					
Other	52	69	92	109	130	161	183	217	333					
Cumulative	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4		
Smartphones and telecom carriers	388	789	1,180	1,564	364	654	936	1,206	238					
YoY	34.7%	35.5%	27.9%	25.1%	-6.4%	-17.1%	-20.7%	-22.9%	-34.6%					
SOURCENEXT online store	974	1,913	3,065	4,006	899	1,867	3,281	4,390	1,046					
YoY	30.0%	15.5%	13.6%	11.3%	-7.7%	-2.4%	7.0%	9.6%	16.4%					
Elec. mass retailers, third-party websites	572	1,398	2,557	3,427	185	1,106	2,034	3,206	817					
YoY	31.3%	47.4%	58.7%	73.1%	-67.6%	-20.9%	-20.5%	-6.4%	341.6%					
Other	52	121	213	322	130	291	474	691	333					

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

Q1 FY03/19 results

Overview

- ▷ Sales: JPY2.4bn (+54.3% YoY)
- ▷ Operating profit: JPY85mn (+35.8% YoY)
- ▷ Recurring profit: JPY85mn (+30.6% YoY)
- ▷ Net income*: JPY49mn (-42.8% YoY)

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

Net profit attributable to parent company shareholders declined because the company had deferred income tax due to the tax losses carried forward at subsidiaries in Q1 FY03/18, but income tax rose in Q1 FY03/19 due to the absence of such tax losses.

Q1 FY03/19 sales reached 37.9% of the company's forecast for 1H FY03/19 (Q1 FY03/18 sales reached 57.2% of 1H FY03/18 results), operating profit 17.8% (15.6%), recurring profit 17.7% (15.7%), and net income attributable to parent company shareholders 14.3% (12.8%).

Q1 FY03/19 sales reached 14.5% of the company's forecast for full-year FY03/19 (Q1 FY03/18 sales reached 16.6% of full-year FY03/18 results), operating profit 3.4% (5.1%), recurring profit 3.4% (5.2%), and net income attributable to parent company shareholders 2.7% (6.8%).

In Q1 PC shipments were solid, increasing 6.6% YoY (based on data from JEITA, June 2018). Additionally, the number of foreign visitors to Japan in June 2018 increased 15.3% YoY to 2.7mn (based on data from the Japan National Tourism Organization, July 2018), a record high for June. The environment surrounding the travel market in Japan has been performing well against the backdrop of the 2020 Tokyo Olympic Games, the recent global situation, and diversification of travel destinations.

In such circumstances the company worked to acquire new users for smartphone apps, PC software and IoT products, and to enlarge its market.

In Q1 the company focused on expanding sales of its first IoT product POCKETALK, an automatic interpreting device. Its expansion into of major electronics mass retailers accelerated, and the company also conducted showroom sales at railway station stores and event venues in various regions, meeting with a favorable reception. The introduction to businesses of a corporate rental service progressed, and there were many enquiries from businesses that provide goods and services to regional tourism authorities and foreign visitors to Japan; the company expects demand to increase in future.

Gross profit (for GPM adjusted for additions to and reversals from provisions for product returns) was JPY1.5bn (+20.9% YoY), and GPM before adjustment for additions to and reversals from provisions for product returns decreased 7.0pp to 55.6%. CoGS rose as sales for POCKETALK (which carries a higher CoGS-to-sales ratio than other software products that the company has sold) increased, and provisions for the adjustment of product returns increased as shipments increased substantially YoY. SG&A expenses were JPY1.4bn (+20.1% YoY), but the SG&A-to-sales ratio improved to 57.8%, falling 16.4pp. Although advertising and promotional expenses decreased YoY, personnel expenses relating to employee salaries along with increases to personnel, promotional expenses in order to push sales of POCKETALK, shipping expenses for e-commerce (SOURCENEXT online store), and outsourcing costs with system upgrades all increased YoY.

By sales channel

Smartphones and telecommunications carriers

Sales: JPY238mn (-34.6% YoY)

This channel focuses on apps offered and sold through the fixed-rate, all-you-can-use app subscription service offered by Japan's three leading telecommunications carriers. SOURCENEXT increased the number of applications offered through KDDI's au Smart Pass to 34 (versus 39 in Q1 FY03/18), with a focus on popular overseas apps. The number of apps offered on SoftBank's App Pass

was 33 (versus 27 in Q1 FY03/18). In Q1 the company launched new software Trigger and Rosetta Stone (English, Chinese, and Korean). The number of apps offered through NTT DoCoMo's Sugotoku Contents service was 24 apps from five sites (versus 23 apps from five sites in Q1 FY03/18). The company launched Rosetta Stone 6 Language Edition.

E-commerce (SOURCENEXT online store)

Sales: JPY1.0bn (+16.4% YoY)

The company operates the SOURCENEXT eSHOP as part of its own website. The eSHOP sells software and PC-related hardware.

SOURCENEXT opened a dedicated website for POCKETALK, focusing on explaining the functions and lineup in an easily understood way. Additionally, the company developed and released a cloud-service multiplatform version of the language learning software Rosetta Stone so that lessons can be delivered easily to Windows, Mac, smartphones or tablets, rather than only PCs.

Electronics mass retailers and third-party websites

Sales: JPY817mn (+341.6% YoY)

This sales channel consists primarily of major electronics retailer chains and third-party websites that sell PC software and other products to individual users.

The company worked to increase sales of POCKETALK, in particular at electronics mass retailers. The company actively carried out demonstrations and sales events at large station stores, extending the product onto other floors, for example putting it into electronic dictionary corners and travel corners (which the company had not done for previous software), planning to raise awareness among store visitors.

Other channels

Sales: JPY333mn (+156.9% YoY)

Sales through other channels consist primarily of POCKETALK rental to corporations, PC software and unlimited-use smartphone app services.

The all-you-can-use smartphone app service for Android apps for low-price smartphone and SIM providers and Smart Answering Machine app released in FY03/18 (with which one can read answering machine messages as text), contributed to profit by increasing mobile phone and smartphone users.

The company has progressed steadily with its offering of the POCKETALK rental service businesses, in particular to transportation companies (airport or rail), and outsourcing businesses that deal with foreigners or foreign visitors to Japan (such as retail or temporary staffing companies). Additionally, subsidiary sales also contributed to increased sales.

This note is the most recent addition to the [full report](#).

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>.

Disclaimer

This document is provided for informational purposes only. No investment opinion or advice is provided, intended, or solicited. Shared Research Inc. offers no warranty, either expressed or implied, regarding the veracity of data or interpretations of data included in this report. We shall not be held responsible for any damage caused by the use of this report.

The copyright of this report and the rights regarding the creation and exploitation of the derivative work of this and other Shared Research Reports belong to Shared Research. This report may be reproduced or modified for personal use; distribution, transfer, or other uses of this report are strictly prohibited and a violation of the copyright of this report. Our officers and employees may currently, or in the future, have a position in securities of the companies mentioned in this report, which may affect this report's objectivity.

Japanese Financial Instruments and Exchange Law (FIEL) Disclaimer

The report has been prepared by Shared Research under a contract with the company described in this report ("the company"). Opinions and views presented are ours where so stated. Such opinions and views attributed to the company are interpretations made by Shared Research. We represent that if this report is deemed to include an opinion by us that could influence investment decisions in the company, such opinion may be in exchange for consideration or promise of consideration from the company to Shared Research.

Contact Details

Shared Research Inc.

3-31-12 Sendagi Bunkyo-ku Tokyo, Japan

<https://sharedresearch.jp>

Phone: +81 (0)3 5834-8787

Email: info@sharedresearch.jp