Analysis of Operating Results and Financial Position

[Review of Operations]

In the fiscal year ended November 30, 2018, the Japanese economy saw corporate earnings follow a recovery trend, supported by the Japanese government's economic policies together with monetary policies. On the other hand, the economic outlook still remains uncertain, based partly on unstable political trends overseas and concerns about the impact of geopolitical risk.

The Japanese government has incorporated the concept of the Fourth Industrial Revolution into its growth strategy. In the Fourth Industrial Revolution, physical things of all kinds, including automobiles and home electric appliances, will be connected to the Internet, making Cyber-Physical Systems a reality. A Cyber-Physical System is a system that quantifies various states of the Physical Part of the real world that are subject to control, and quantitatively analyzes this data in the Cyber Part to derive new insights and knowledge, which are then fed back and used to control the Physical Part of the real world. The general belief is that the ability to collect and retain big data from the Physical Part of the real world through IoT technology and the ability to manage and analyze this data through AI and blockchain technologies in the Cyber Part will be crucial to success.

The Company's main focus is the CPS/IoT market, which grew in 2016 to a scale of ¥194.0 trillion globally and ¥11.1 trillion in Japan. By 2030, the global market scale is projected to grow to ¥404.4 trillion, and the Japanese market scale to ¥19.7 trillion. Furthermore, the agriculture field, which has exhibited remarkable growth in Japan, saw annualized growth of 20.2%. (Source: Japan Electronics and Information Technology Industries Association "Survey of Trends Related to Focus Field 2017")

In this operating environment, in January 2018, the Company entered into a business tie-up with Fisco Cryptocurrency Exchange ("FCCE") with regard to the development of an AI trading system for cryptocurrencies to be undertaken with Company's subsidiary e frontier, Inc. ("e frontier"). Furthermore, e frontier conducted multiple trials of software under development, started investing in bitcoin, and succeeded in delivering a certain level of results. Moreover, also in January 2018, e frontier's then-equity method affiliate NCXX Solutions Inc. ("NCXX Solutions") conducted a share exchange with another then-equity method affiliate, CAICA Inc. ("CAICA") to make NCXX Solutions a wholly owned subsidiary of CAICA. By making NCXX Solutions a wholly owned subsidiary, CAICA aimed to further increase operational efficiency, expand synergies, strengthen consolidated earnings capability, and increase consolidated corporate value. The Company and NCXX Solutions continued to conduct joint development related to IoT after the transfer.

In addition, in February 2018, the Company subscribed to part of a private placement of new shares to raise capital by the apparel brand CSMEN Co., Ltd. (Listing: 3083 TSE JASDAQ; Headquarters: Chuo-ku, Tokyo; President: Masao Aoki), thereby entering a capital and business alliance. CSMEN Co., Ltd. is expected to form synergies with the Company's brand retail platform business.

In April 2018, the Company procured ¥200 million by issuing the 7th Series of Unsecured Convertible Bond-Type Bonds with Share Acquisition Rights by private placement to fund basic research and development for providing AI solutions and distributed applications using blockchain, as well as development of agricultural ICT systems, which will be the Company's main focus areas going forward.

In July 2018, the Company decided to start a cryptocurrency mining operation at its Head Office in Hanamaki City, Iwate Prefecture. The mining of cryptocurrency refers to authentication work performed to ensure that blocks of transaction data found on networks are consistent with one another. Cryptocurrency miners who authenticate data at the fastest pace are rewarded by receiving payment in the relevant cryptocurrency. Because massive amounts of computations must be performed to conduct this authentication work, cryptocurrency miners require high-performance computers. Ordinarily, in order to conduct a mining business, cryptocurrency miners require a considerable number of cooling fans and air conditioning systems to dissipate the heat generated by mining equipment, as well as the physical space to house this equipment plus an immense amount of electric power to operate the mining facility. Therefore, a key priority in business is to efficiently solve these problems at the lowest possible cost. Hanamaki, Iwate Prefecture is located in a relatively cold region. In winter, temperatures fall to the freezing point while in the summer, the average temperature is fairly low at 23.8 ℃ (almost 74.8℉) (Source: Japan Meteorological Agency). Accordingly, the Group can expect to significantly reduce its electricity bills by relying on natural ventilation for most of its cooling needs throughout the year. Moreover, Iwate Prefecture is ranked second in terms of its potential for renewable energy. Notably, Iwate Prefecture has an extremely high potential for wind power and geothermal power. In the future, the Group plans to target the procurement of low-cost electric power based on this abundant supply of renewable energy. Moreover, the heat released by mining equipment will be reused in the Group's agricultural ICT business (NCXX FARM). At NCXX FARM, the Group grows cherry tomatoes year-round in greenhouses. In winter, the outdoor temperature falls below freezing, so heaters are run 24 hours a day to maintain the optimal temperature for growing vegetables in the greenhouses. The mining equipment generates a considerable amount of heat as it is operated 24 hours a day. Therefore, this heat can be reused to reduce heating costs in the winter. Looking ahead, the Group will seek to build a self-sufficient agricultural system not only by reusing the heat generated by mining operations, but also by using the mined coins to procure the seedlings, fertilizer and agrichemicals needed in the agriculture business. In this manner, the NCXX Group will conduct a unique cryptocurrency mining business by working to optimize overall efficiency, including initiatives involving other businesses. The Group's mining business will thus be markedly different than mining operations undertaken in overseas countries where electricity is available at low cost.

In October 2018, the Company sold a part of its equity-method affiliate CAICA to procure funds for the Company's growth, and CAICA was excluded from the scope of application of the equity method. The Company has a well-established cooperative relationship with CAICA based on a capital and business alliance, which will continue unchanged going forward. They will continue joint development combining NCXX Inc.'s ("NCXX") IoT technology, CAICA's blockchain, and AI technology, and continue to conduct initiatives toward development of new services in the FinTech business field.

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Also in November 2018, the Company's consolidated subsidiary Versatile Inc. ("Versatile") conducted a corporate split of part of its business (incorporation type split), which was transferred to the newly established company, NCXX Premium Group, Inc. ("NCXX Premium Group"), and NCXX Farm Holdings, Inc. ("NCXX Farm Holdings"), while the newly established company became a wholly owned subsidiary of Versatile. Subsequently, also in November, in order to restructure the business, it was decided to apply to conduct a special liquidation in which all shares of NCXX Premium Group and NCXX Farm Holdings, which were held by Versatile, would be transferred to the Company, making them into subsidiaries of the Company, and Versatile would be dissolved.

[Operating Results]

Looking at consolidated business results, e frontier began to record revenues after commencing investment in cryptocurrency on its own account. e frontier conducted trials of software under development for the development of the abovementioned AI trading system for cryptocurrencies. It then began investing in bitcoin and achieved considerable success. On the other hand, revenue declined following the removal of NCXX Solutions from the scope of equity-method affiliates. Furthermore, sales at the Company's consolidated subsidiary, e-tabinet.com fell short of target. Turning to income, operating income declined year on year as the cost ratio at the Company's consolidated subsidiary TITICACA Co., Ltd. ("TITICACA") rose in the fourth quarter after selling, general, and administrative expenses were seen to increase throughout fiscal 2018. Looking at ordinary income, TITICACA recorded a loss on sale of cryptocurrency of ¥201 million and a loss on valuation of cryptocurrency of ¥192 million. Recently, the cryptocurrency market has seen some fairly prominent price declines; however, in the event of a drastic decrease in cryptocurrency prices, TITICACA executes stop-loss transactions as needed as part of its risk control measures. In this manner, TITICACA always conducts trading activities with an emphasis on capital efficiency. As a result, the cryptocurrency business has achieved a certain level of profit for the fiscal year; however, since investment in cryptocurrency was not one of TITICACA's main businesses, it has been recorded under non-operating expense.

Loss attributable to owners of parent resulted from impairment of the CoSTUME NATIONAL trademark of ¥888 million, which was offset by extraordinary income of ¥651 million from sale of shares held by the Company. The write-down of the trademark reflected a conservative revision of CoSTUME NATIONAL's business plan in light of its current performance. Looking forward, the Group will start a worldwide license business, and examine business alliances offering synergies with the business in order to expand it, aiming to grow sales rapidly.

In the same way, a ¥136 million impairment of goodwill of FACETASM was the result of a more conservative revision due to falling below the initial target, despite sales growing.

As a result of these efforts, consolidated net sales were ¥11,125 million, down 8.8% year on year. Operating profit was ¥419 million, compared with an operating loss of ¥914 million in the previous fiscal year. The ordinary loss was ¥47 million, compared with an ordinary loss of ¥940 million in the previous fiscal year. Loss before income taxes was ¥265 million, compared with a profit before income taxes of ¥1,024 million in the previous fiscal year. Loss attributable to owners of parent was ¥473 million, compared with a profit attributable to owners of parent of ¥902 million in the previous fiscal year.

Business performance by segment in the fiscal year under review was as follows:

(IoT Related Business)

NCXX Inc. focused on providing solutions using GX410NC and GX420NC, OBD II-type automotive telematic data collecting units launched in 2015. In collaboration with NCXX Solutions, NCXX Inc. developed the safe driving assistance service Drive Care (http://www.care-dynamics.jp/obd2/), an OBD II solution for nursing care transportation service vehicles, and rolled it out in August 2016.

This system enables the managers or supervisors of businesses that provide various transportation services for nursing care facilities and other customers to confirm the status of multiple fleet vehicles operating simultaneously. The system can ascertain all dangerous driving behaviors (sudden starts, sudden stops, sharp turns)have occurred when the vehicle is en route to a destination. By displaying these incidents in formats that are easy for managers and supervisors to understand, such as lists and graphs, they will be able to monitor the driving behavior of drivers and provide appropriate instructions tailored to each driver. In addition, managers and supervisors will be able to ascertain the extent of improvement of each driver and follow up on drivers appropriately by continuously checking driving performance data.

Also, the system can be used to reduce the maintenance and management costs of welfare service vehicles by making effective use of the various types of data that can be obtained. For example, managers and supervisors will be able to improve average fuel economy by instructing drivers on environmentally friendly driving practices, curtail wear of tires and other parts of vehicles, and issue vehicle inspection alerts to prevent vehicle malfunctions.

In recent trends, the U.S. National Defense Authorization Act for Fiscal Year 2019 ("NDAA 2019") was passed in August 2018, greatly strengthening restrictions on five companies: Huawei, ZTE, HIKVISION, Dahua Technology, and Hytera; and calling for a ban on transactions between them and U.S. government institutions. The Group has received numerous inquiries regarding whether NCXX products are also subject to the NDAA 2019.

NCXX explains that its products can be used with confidence, since none of the products currently on the market are manufactured by outsourcing to the abovementioned five companies related to the recently passed NDAA 2019, or use parts sourced from them. Moreover, NCXX will strengthen controls to ensure that its products do not infringe on any of the prohibitions going forward.

Analysis of Operating Results and Financial Position

The Group will continue to monitor trends carefully, and continuously manage and monitor its contract manufacturing providers while developing trustworthy new contract manufacturing providers. The Group will work to further expand its product groups to meet the needs of the market as a domestic Japanese manufacturer. The Group will continue to provide mobile computing solutions such as LPWA, which is expected to spread in markets in Japan and overseas going forward, and the next-generation 5G telecommunications standards, automotive telematic solutions that integrate high-valued-added communication devices and software, as well as various other types of solutions.

Care Dynamics Limited is a provider of ASP systems to nursing care businesses. It has already deployed ASP systems at more than 400 nursing care facilities. With the launch of services such as support for the introduction of nursing care robots and the provision of nursing care ICT, Care Dynamics has evolved into a comprehensive nursing care business support enterprise.

As a service for assisting caregivers, Care Dynamics offers nursing care robots as a sales agency, distribution of instructive leaflets of corporations using manga illustrations, and services for creating advertisements. Care Dynamics continues to provide tours of nursing care facilities that have adopted the “Drive Care” OBD II solution for nursing care transportation services, and offers free trials of the solution.

Moreover, Care Dynamics provide a replacement support service and reassess electricity providers to help nursing care facilities cut their electricity bills. Care Dynamics also offer a service that introduces systems for saving water.

Care Dynamics concluded a new network building support service for corporations, concluded a sales agreement with PARAMOUNT BED CO., LTD., and began selling PARAMOUNT BED’s sleep management system.

e frontier has a track record in developing and selling software, such as AI-driven programs for the games of go, shogi and mahjong. The company is currently developing a system for cryptocurrency trading that leverages its AI technologies. Last year, e frontier concluded a business alliance with FCCE, and both companies have been conducting trials of AI technology. In addition, e frontier has received provision of a vast amount of past transaction data from FCCE, as well as expertise in derivative systems and high frequency trading systems* from a user standpoint, and aims to develop systems with even better usability.

In addition, in June 2018, the Company concluded a general agency agreement for Japan with major U.S. manufacturer Other World Computing, Inc. (“OWC”) and now plans to expand sales of computer peripheral devices such as Thunderbolt 3 products and eGPUs, as well as ancillary services, in Japan.

* Derivative systems and high frequency trading systems:
Designed to cover multiple cryptocurrency exchanges in Japan and overseas, checking and analyzing their trends to obtain profit automatically. The systems control risk appropriately while being able to wait for profit taking opportunities.

As a result, segment sales in the fiscal year ended November 30, 2018 were ¥950 million, down 76.3% year on year. Segment profit was ¥48 million, compared with segment loss of ¥465 million in the previous fiscal year.

(Internet Travel Business)

In the Internet travel business, e-tabinet.com and its subsidiaries have received a large number of positive comments from many highly satisfied customers for their ability to fulfill increasingly diverse and sophisticated needs, amid a proliferation of travel products and services. The crucial factor behind this success is that e-tabinet.com has been able to build a solid structure as Japan’s only Internet-based travel agency offering customized services with a carefully chosen staff of highly experienced registered “travel concierges” (travel consultants).

In 2015, e-tabinet.com launched a specialized site for inbound tourists visiting Japan from abroad, and implemented search engine optimization with a focus on Asia. The number of tourists visiting Japan is projected to increase by 14% to 32 million by the end of the fiscal year ended November 30, 2019, which is expected to lead to shortages in accommodation facilities. Against this backdrop, in cooperation with Group company Jitsugyo no Nihon Sha, Ltd., e-tabinet.com set up a new dedicated skiing website in English featuring 204 ski fields in Japan to address the strong demand for this information among information for inbound tourists visiting Japan. Additionally, Gloria Tours Inc., a company specializing in sending Paralympic athletes to various events and organizing numerous international para-sports tournaments, will increase its focus on the para-sports market. Along with the concierge business of Web travel Co., Ltd. (“Web travel”), e-tabinet.com seeks to build a niche market base that most general travel agencies would find difficult to serve.

Meanwhile, the number of registered travel concierges has grown steadily, but with a significant amount of the concierges churned, the number was decreased slightly to 440 as of September 30, 2018. In addition, e-tabinet.com has been advancing the crowdsourcing business as a platform for concierges to make the most of their unique talents in areas other than travel. By fostering a stronger sense of community and belonging among concierges, e-tabinet.com will work to recruit and retain talented personnel.

The business alliance with SAISON UC Card, which has been in place since February 2018, is more than a supple advertising agreement, with the business alliance regarding travel concierges being positioned as a function of the card itself. This has encouraged even greater social trust in Web travel’s concierge service, and contributed to an increase in requests for travel estimates and orders.

Overseas travel business sales were ¥2,215 million, centered on standard round trip packages to Europe and honeymoon packages, and domestic travel business sales were ¥170 million. As the number of requests for travel estimates from customers began to recover slightly, the number of requests for travel estimates on the Web travel website increased by 2% year on year. For the e-tabinet.com website, the number of requests for travel estimates remained level year on year. However, as a result of measures to enhance order rates, the number of orders received increased by 16% year on year, and the gross profit margin was maintained at 14%. The total number of staff handling requests also increased by 12% year on year to 7,438.

As a result, segment sales in the fiscal year ended November 30, 2018 were ¥2,367 million, up 8.4% year on year. Segment profit was ¥38 million, compared with segment loss of ¥2 million in the previous fiscal year.

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(Brand Retail Platform Business)

In its stores business, TITICACA had 93 stores as of October 31, 2017, opened two stores in 2018 (Yokohama World Porters, Aeon Mall Sapporo Hassamu) and closed one store (Aeon Mall Nagoya Dome Mae) leaving 94 stores as of the end of October 2018. In the e-commerce business, the Company expanded its six-store lineup including its own online stores to an eight-store lineup by opening stores on au Wowma! (former Wowma!) and Alinoma in fiscal 2018. The Company also continued to promote structural reforms such as closing unprofitable stores and revising personnel structures.

Moreover, in its sales measures, the Company, Japanese actress Alice Hirose and TITICACA introduced a second round to their collaboration effort in 2018, opening a stall at the Aichi Block Conference Tahara Conference held by the Junior Chamber International Japan, where visitors could listen in person to Alice Hirose talking about her experiences of overseas cooperation activities. One of the objectives of the conference is to stimulate interest in overseas cooperation among young people and inspire them to take action. TITICACA sold collaboration T-shirts and tote bags as an immediate form of international collaboration. ¥500 from each unit sold was donated to social contribution organizations supported by Alice Hirose. Purchases of the merchandise leads to future happiness.

In fiscal 2019, the Company will continue to expand its customer contacts through social media and its own app in an effort to expand the customer base. In addition, from a perspective of staff development, the Company will work to enhance its manuals and education systems, and to stabilize earnings.

As a result, segment sales in the fiscal year ended November 30, 2018 were ¥6,445 million, up 8.7% year on year. Segment loss was ¥460 million, compared with segment loss of ¥71 million in the previous fiscal year.

(Cryptocurrency and Blockchain Business)

e frontier and TITICACA are conducting investment operations based on trading using an AI-based cryptocurrency trading system currently being developed by e frontier. In contrast to 2017, the cryptocurrency market has seen some fairly prominent price declines in 2018. In the event of a drastic decrease in cryptocurrency prices, e frontier and TITICACA execute stop-loss transactions as needed as part of their risk control measures. In this manner, e frontier and TITICACA always conduct trading activities with an emphasis on capital efficiency. In addition, the companies are considering investment operations aimed at accumulating small returns from margins while mitigating risk. In these and other ways, the two companies will establish an investment style that does not rely on the direction (upward or downward movements) of market prices.

As a result, segment sales in the fiscal year ended November 30, 2018 were ¥1,326 million. Segment profit was ¥1,320 million.

[Financial Position]

(Assets)

Total assets were ¥9,302 million as of November 30, 2018, a decrease of ¥2,229 million from a year earlier. The main components of this change were decreases of ¥1,500 million in cash and deposits, ¥669 million in advance payments—trade, and ¥1,033 million in investment securities, and increases of ¥1,000 million in short-term loans receivable and ¥317 million in long-term loans receivable.

(Liabilities)

Total liabilities were ¥5,349 million, a decrease of ¥1,656 million from a year earlier. The main components of this change were decreases of ¥1,165 million in current portion of convertible bond-type bonds with share acquisition rights, and ¥471 million in interest-bearing debt*.

(Net Assets)

Total net assets were ¥3,953 million, a decrease of ¥572 million from a year earlier. The main contributing factors were decreases of ¥522 million in retained earnings, and ¥77 million in valuation difference on available-for-sale securities.

* Interest-bearing debt is the sum of short-term loans payable, current portion of long-term loans payable and long-term loans payable.

[Cash Flows]

Cash and cash equivalents ("cash") at November 30, 2018 were ¥1,022 million, a decrease of ¥1,506 million from the previous fiscal year-end.

Cash flows during the fiscal year under review and analysis of the main components are as follows:

(Cash Flows from Operating Activities)

Net cash provided by operating activities was ¥981 million, compared with net cash used in operating activities of ¥1,388 million in the previous fiscal year. The primary reasons were impairment loss of ¥1,110 million, decreased in cryptocurrencies of ¥751 million, and advance payment of ¥667 million. These factors were partly offset by an increases in notes and account receivable—trade of ¥926 million and a gain in sales of investment securities of ¥705 million.

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(Cash Flows from Investing Activities)

Net cash used in investing activities was ¥1,099 million, compared with net cash provided by investing activities of ¥3,929 million in the previous fiscal year. This was mainly due to payment of ¥3,112 for purchase of cryptocurrencies, payment of ¥320 million for purchase of investment securities, payment of ¥960 million for purchase of intangible assets, and an increase in long-term loans receivable of ¥760 million, the main factors reducing cash. These cash outflows were partly offset by proceeds from sale of cryptocurrencies of ¥1,961 million and proceeds from sale of investment securities of ¥1,998 million.

(Cash Flows from Financing Activities)

Net cash used in financing activities was ¥1,389 million, compared with net cash used in financing activities of ¥1,851 million in the previous fiscal year. This was mainly due to payment of long-term loans payable of ¥1,055 million and payments for redemption of bonds of ¥1,165 million, the main factors reducing cash. These cash outflows were partly offset by proceeds from short-term loans payable of ¥241 million, proceeds from long-term debt of ¥392 million and proceeds from issuance of bonds with share acquisition rights of ¥200 million, the main factors increasing cash.

[Risk Information]

The Group presents the main factors that could pose a risk to its business development and related activities. From the standpoint of actively disclosing information to investors, the Group discloses matters that could have a material impact on investor judgment, even external factors beyond the control of the Company and matters that may not necessarily be considered as business risks.

The items outlined below do not represent an exhaustive listing of all risks affecting investment in the Company's stock.

The items in the following section that concern the future were assessed by the Group based on information available as of November 30, 2018. They are subject to uncertainties and may differ from actual results.

(1) Business Characteristics

1. Group Driven by Research and Development

The Group primarily comprises companies driven by research and development (R&D), and its source of competitiveness is the constant internal accumulation of new technology. If the Group has difficulty securing and nurturing competent technicians, or suffers an outflow of competent human resources, this could have a material impact on the Group's business and operating results.

As a policy, the Group adapts to technological and other advancements through its R&D activities. However, the Group may not be able to adapt promptly to changes in the business environment if they were brought about by new unforeseen technologies. Adapting to changes in the business environment may also involve large sums of R&D expenses and other expenses. Such events could have a material impact on the Group's business and operating results.

2. Fabless Manufacturing

The Group outsources the manufacturing of mobile telecommunications devices and other products to a large extent. As a result, business conditions at the outsourcing contractors, as well as the Group's cultivation and retention of outsourcing contractors and the Group's in-house manufacturing capabilities, could have a material impact on the Group's business and operating results.

3. Relationship with Telecommunications Service Providers

The Group's core products are data telecommunications terminals and other mobile devices developed and manufactured based on the specifications of telecommunications service providers. Furthermore, in these transactions the telecommunications service providers purchase all of the contracted output. As a result, changes in the content of the contracts, sales prices, and transaction terms with the telecommunications service providers, as well as the success or failure of renewing the contracts, could have a material impact on the Company's business and operating results.

4. Changes in Demand for Mobile Devices

Data telecommunications terminals and other mobile devices developed and manufactured by the Group are subject to severe product competition. As such, the trend in their demand has a tendency to change dramatically depending on such factors as technological advancement and the status of the product competition. The business is also characterized by the short turnaround in launching new products. As a policy, the Group seeks to adapt to changes in demand with fabless manufacturing. However, the Group is currently dependent on specific products because it develops and manufactures a limited variety of products. Consequently, drastic changes in demand and falls in the sale price of mobile devices brought about by factors such as business strategies of competitors and changing customer needs could have a material impact on the Group's business and operating results.

(2) Dependence on a Specific Business Partner

In the fiscal year ended November 30, 2018, the Group outsourced the manufacturing of mobile devices to TRICHEER TELECOMMUNICATION LTD. Consequently, changes in the business transaction policy and manufacturing framework between the Group and this contractor could have a material impact on the Group's business and operating results.

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(3) Risks Related to Protection of Intellectual Property Rights

The Group is driven by R&D and is the rightful owner of numerous intellectual properties that have been submitted and registered for patent and registered with design rights and trademarks. The Group also strives to make sure that the products it develops and manufactures do not infringe on the intellectual property rights of third parties, and understands that there are no infringements at present. However, the possibility of infringing on the intellectual property rights of a third party in the future cannot be eliminated. Should the Group infringe on the intellectual property rights of a third party, it may experience legal action seeking damages, a decline in credibility, a deterioration in its corporate brand, and so forth, which could have a material impact on the Group's business and operating results. Conversely, should the intellectual property rights of the Group suffer infringement by a third party, the Group would be obliged to divert management resources toward taking the party to court and other defensive measures, which could have a material impact on the Group's business and operating results.

(4) Quality Control

The Group must recall and repair the mobile devices it develops and manufactures in the event of a product malfunction. Moreover, should an accident caused by defective products occur, the Company may be subject to claims for damages under the Product Liability Act.

In order to prevent such product defects and accidents from occurring, the Group has developed a quality control system that also encompasses the management of outsourcing contractors and suppliers to improve product safety and promote compliance with laws and regulations. In addition, the Group also subscribes to product liability insurance as a contingency in the event of product accidents. However, should a serious product defect or incident violating the Product Liability Act occur, the Group may have to bear product recall and repair expenses and payment of damages, as well as experience a decline in its credibility with corporate clients and society, a deterioration in its corporate brand value, and so forth, which could have a material impact on the Group's business and operating results.

(5) Statutory Regulations on Telecommunications

The Group mainly develops products regulated by the Radio Act of Japan. As a result, trends regarding the Radio Act and other statutory regulations on telecommunications could have a material impact on the Group's business and operating results.

(6) Protection of Personal Information

The Group holds the personal information and so forth of its customers in the conduct of its business of selling and providing product support and so forth for mobile communication devices and selling apparel and general merchandise. To prevent the acquired personal information and so forth of customers from leaking externally, the Group takes ample precautions such as limiting access to the personal information and strengthening the internal control system by periodically conducting internal audits. However, should a leak in personal information occur, the Company may be in violation of laws and regulations as well as its confidentiality agreements with client companies. As a result, the Group may receive claims for damages from client companies and other customers as well as experience a decline in its credibility with corporate clients and society, a deterioration in its corporate brand value, and so forth, which could have a material impact on the Group's business and operating results.

(7) Corporate Organization

In order to continue growing while strengthening the internal control system further at the same time, the Group sees a need to bolster competent human resources, as well as further enhance the organization of its administrative divisions, at each stage of business development. Consequently, should the Group be unable to bolster human resources as required at each stage of business development, or suffer an outflow of competent human resources, this could have a material impact on the Group's business and operating results.

(8) Relationship with the Parent Company

FISCO Ltd. (listed on the Tokyo Stock Exchange JASDAQ Growth) is the parent company of the Company, holding 48.51% of the voting rights both directly and indirectly as of November 30, 2018.

The Company therefore belongs to a parent company group with FISCO at the center. As a result, changes in the parent company group's management policy and other circumstances could have a material impact on the Company's business and operating results.

(9) Fluctuations in the Foreign Exchange Market

The Company subcontracts the manufacturing of some of its products to overseas manufacturers and so forth to enhance price competitiveness and profitability. As a result, business transactions denominated in foreign currencies may be affected by fluctuations in the foreign exchange market. To reduce this impact, the Company strives to make use of instruments such as foreign exchange forward contracts, and to reconfigure its product portfolio. However, trading conditions and foreign exchange market trends in the future could have a material impact on the Group's business and operating results.

Also, fluctuations in the foreign exchange markets could impact the Group's operating results and financial position since the Group has assets overseas. Further, in the event that changes in legislation or government policies in Japan or overseas hinder smooth remittances, the Group's business operations and accounting processes may be affected, which could in turn impact the Group's operating results and financial position.

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(10) Profitability of System Development Projects

When undertaking system development, the Group estimates in advance the total number of work hours (labor hours) needed to meet customer requirements and determines the costs necessary to create the system as part of its activities to win orders. However, if problems arise during system development and work hours exceed the budgeted time, the Group could end up bearing that cost.

Additionally, the Group may be called on to bear the cost of an increase in labor hours even if it relates to specification changes made during development.

Further, the Group may incur the cost of fixing defects that arise after the developed system has been delivered to the customer and the customer has finished inspecting it and determined it to be free of issues.

The Group therefore strives to increase the accuracy of estimates at the time of the contract by creating detailed estimates for each development process (phase), and taking other steps to keep the actual number of labor hours in line with the budgeted number. While the Group gives sufficient consideration to project profitability, profitability could deteriorate due to factors such as development projects becoming large in scale and escalating competition to win orders.

(11) Investments and Loans

To expand business going forward, the Group may undertake M&As or business investments targeting alliances, or engage in joint venture business development, subsidiary establishment, or capital expenditures in Japan or overseas.

The Group's policy in making investments and loans is to thoroughly evaluate the recoverability and risks of those prospective investments and loans in advance. However, it is sometimes difficult to accurately project the impact on the Group from business conditions at investees and should investments or loans become unrecoverable, the Group's operating results and financial position could be affected.

(12) Merchandise Purchases

The Group company TITICACA mostly sells imported products. Therefore, events in relevant countries such as unanticipated changes in legislation, political uncertainty, major natural disasters, social unrest, and sharp fluctuations in foreign exchange rates could affect TITICACA's merchandise supply framework and the Group's operating results and financial position.

(13) Impairment of Property, Plant and Equipment

The Group recognizes impairment losses on the portion of the assets of stores that are persistently unprofitable or that it has decided to relocate or close for which the book value of property, plant and equipment is determined to be unrecoverable. In the event of an increase in such unprofitable stores going forward, the posting of significant impairment losses would be expected, which could affect the Group's business performance and financial position.

(14) Losses from Store Relocations and Closings

The Group may relocate or close stores due to tenancy agreements expiring. In that event, costs will arise for the removal of property, plant and equipment to restore the leased space to its original condition, new investments in relocation sites, and so forth. If store relocations and closings increase in the future, the posting of a large amount of losses associated with the removal of property, plant and equipment, as well as selling, general and administrative expenses would be expected, which could affect the Group's business performance and financial position.

(15) Investment in Cryptocurrency

The Group faces risks associated with investment in cryptocurrency, including price movements in cryptocurrency, the risk of losses stemming from the inability to trade in the cryptocurrency markets or being forced to trade on terms that are less advantageous than normal due to factors such as turmoil in the cryptocurrency markets. Other risk factors include disruptions in derivative trading systems for cryptocurrency, system disruptions and business failure of cryptocurrency exchanges, and theft due to unauthorized access to servers. The Group makes every effort to rigorously implement risk management. However, if the aforementioned risks materialize, the Group could incur higher costs to deal with the issue or suffer a decline in its credibility, which could have a material impact on the Group's business results and financial condition.

(16) Disasters, etc.

In the event that a major natural disaster or accident in the vicinity of stores, warehouses, and so forth causes physical damage to such facilities; disrupts sales, distribution, purchasing, or other business activities; or causes personal injury, the Group's business performance and financial position could be affected.