

ENGLISH TRANSLATION ONLY

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Please refer to the original release in case of any discrepancy or inconsistency.



September 6, 2013

Summary of Earnings Report for the First Quarter of the Fiscal Year Ending April 30, 2014

Name of listed company **ZAPPALLAS, INC.** Listed stock exchange: TSE first section
Code **3770** (URL <http://www.zappallas.com>)
Representative: **Mari Kawashima, Chairperson and CEO**
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Scheduled date of filing **September 11, 2013** Supplementary materials for financial results **Yes**
Financial Reports: **Investor conference** **None**

1. Consolidated First Quarter Results for the fiscal year ending April 30, 2014 (Millions of Yen, rounded down)

(from May 1, 2013 to July 31, 2013)

(1) Consolidated Business Results (%: comparison with same period in previous year)

	Net Sales		Operating Income		Ordinary Income		Net Income	
	¥ million	%	¥ million	%	¥ million	%	¥ million	%
1Q (May 1, 2013 to July 31, 2013)	1,882	(20.6)	175	(70.9)	152	(74.9)	86	(75.2)
1Q (May 1, 2012 to July 31, 2012)	2,369	(16.8)	603	(21.3)	606	(21.1)	348	(23.4)

(Notes) Comprehensive Income: July 31, 2013 158 million yen (down 56.8%), July 31, 2012 366 million yen (down 19.3%)

	Net Income per Share	Diluted Net Income per Share
	Yen	Yen
1Q (May 1, 2013 to July 31, 2013)	685.38	680.55
1Q (May 1, 2012 to July 31, 2012)	2,776.07	2,745.99

(2) Consolidated Financial Conditions

	Total Assets	Net Assets	Shareholders' equity ratio	Net Assets per Share
	¥ million	¥ million	%	Yen
1Q (May 1, 2013 to July 31, 2013)	9,861	8,038	80.9	63,281.12
1Q (May 1, 2012 to July 31, 2012)	10,126	8,409	82.4	66,182.87

(Notes) Shareholders' Equity: July 31, 2013 7,981 million yen, April 30, 2013 8,347 million yen

2. Dividends Information

Record Date	Dividend per Share				
	1Q	Interim	3Q	Year end	Yearly
	Yen	Yen	Yen	Yen	Yen
Year ended April 30, 2013	-	0.00	-	4200.00	4200.00
Year ending April 30, 2014	-				
Year Ending April 30, 2014 (Forecast)		0.00	-	22.00	22.00

(Notes) A planned stock split (100 to 1) will take place on Nov. 1, 2013

3. Forecast of Consolidated Financial Results for the Year Ending April 30, 2014 (from May 1, 2013 to April 30, 2014)

(%: Comparison with same period in previous year for "Interim", comparison with previous year for "Full year")

	Net Sales		Operating Income		Ordinary Income		Net Income		Net Income per share
	¥ million	%	¥ million	%	¥ million	%	¥ million	%	Yen
Interim	4,080	(10.8)	140	(84.6)	140	(84.8)	80	(86.6)	6.34
Full Year	10,100	13.6	1,000	(29.7)	1,000	(39.6)	620	(32.4)	49.16

(1) Consolidated Management Analysis Report

In terms of the environment surrounding our mobile business, the size of the mobile content market, comprising the mobile content market and mobile commerce market, was 2.3507 trillion yen in fiscal year 2012 (growth of 23.3% from the previous fiscal year), and mobile markets continued to grow (*1). Of the 851.0 billion yen mobile content market (growth of 15.9% from the previous fiscal year), although the feature phone (*2) market shrunk rapidly to 479.3 billion yen (a decrease of 26.7% from the previous fiscal year), the smartphone (*3) market grew explosively to 371.7 billion yen (growth of 361.2% from the previous fiscal year). In this way, as mobile users continue to transition from feature phones to smart phones, the Zappallas Group has in response taken a variety of steps in our content business for both feature phone users and smartphone users.

In our commerce business, we worked to expand our product lineup to ensure a full lineup of original, high value-added products, and also focused on growing the new commerce sites that were launched during the previous consolidated fiscal year.

In addition, we have started full-scale business operations overseas at our U.S. subsidiary that was established in December 2012.

As a result of the above, net sales during the consolidated first quarter were 1,882.260 million yen (down 20.6% year-on-year). Operating income was 175.423 million yen (down 70.9% year-on-year). Ordinary income was 152.314 million yen (down 74.9% year-on-year), and net income was 86.443 million yen (down 75.2% year-on-year).

*1: *Size of Mobile Content Markets in 2012*, from media materials released by the Mobile Media Forum on August 9, 2013.

*2: These are conventional types of mobile phones which are centered primarily on communication functions, but which also incorporate other functions such as a camera and one-segment television reception.

*3: These are multifunction portable information terminals such as the iPhone and Android devices, and functions equivalent to a personal computer.

An overview of the business conditions by segment is as follows.

As one part of measures to attract smartphone customers, a new division was added beginning from this consolidated first period for the purpose of acquiring advertising revenue. As a result, the reporting segments have been changed so that a portion of the content which was previously included in "Contents business" has been moved to "Other business." The content which is included in each reporting segment has also been reviewed based on this organizational change. Year-on-year comparisons are made using the current consolidated first quarter that has been reorganized to reflect these changes.

(1) Content business

In the content business, we worked to create a new mechanism for attracting customers aimed at capturing the growing ranks of smartphone users, and also continued to invest in new content and expand our menu of services with per-use fees.

During the consolidated first quarter, sales of services for smartphones grew steadily as a result of expanding smartphone services, advertising, and an increase in members due to CRM (*4). However this growth was not sufficient to make up for the decline in sales of services for feature phones.

As a result of the above, net sales for the consolidated first quarter were 1,470.964 million yen (down 17.1% year-on-year), and segment income was 588.973 million yen (down 23.5% year-on-year).

*4: A method by which companies construct long-term relationships with customers through the use of information systems.

(2) Commerce business

The commerce business of the Zappallas Group includes the e-commerce business (mobile device and PC) and the company B×E Inc. which is engaged in wholesale and retail sales of natural cosmetics.

In the-commerce business, we focused on development of the new-style commerce sites which we launched during the previous consolidated fiscal year. "Fujimaki Department Store" successfully used Facebook for sales promotion and other activities in order to expand its sales, however because of declining sales at existing mobile commerce sites, sales in the e-commerce business as a whole continued to decline.

Because B×E Inc. did not plan to introduce any new products during the consolidated first quarter, sales were lower compared with the consolidated first quarter of the previous fiscal year, however the results were approximately as planned.

As a result of the above, net sales for the consolidated first quarter were 251.001 million yen (down 52.5% year-on-year), and the segment loss was 92.818 million yen (compared to segment income of 70.404 million yen during the consolidated first quarter of the previous fiscal year).

(3) Overseas business

For overseas business, we operate a divination business run by the Daily Insight Group (hereafter, "DIG") of Zappallas, Inc. (U.S.), our wholly-owned subsidiary in the United States.

During the consolidated first quarter, this company continued to add staff in order to reinforce its system foundations, and also worked to improve its marketing and management operations. Although the U.S. divination business model relies primarily on advertising revenue, we have begun new trials including providing a portion of per-use fee content from Japan to customers in the United States.

As a result of the above, net sales for the consolidated first quarter were 109.872 million yen, and the segment loss was 31.651 million yen.

(4) Other business

In other business, in addition to contracted mobile site development, operation of "Y! Suica" and other sites, and sales of advertising for the "Zenryaku Profile" profile site aimed at junior high and high school students, we also worked actively for the operation of new media and the development of new services.

During the consolidated first quarter, there was an increase in costs resulting from measures to attract smartphone customers and from active advertising for new business.

As a result of the above, net sales for the consolidated first quarter were 50.422 million yen (down 25.3% year-on-year), and the segment loss was 117.145 million yen (compared to a segment loss of 38.678 million yen during the consolidated first quarter of the previous fiscal year).

(2) Explanation of financial results

(3) Explanation of consolidated results forecasts and other future predictions

As users continue to shift from feature phones to smartphones, large changes are taking place in the environment surrounding our mobile business. In this kind of environment, the policy of the Zappallas Group is to carry out a "lifetime platform" strategy for providing a diverse range of service to meet the needs of many different age groups, aiming to ensure that our major customer segments continue to use our group's services as they age. Specifically, we will meet a diverse range of user needs by focusing on identifying and growing new content and services that will form a second base of business after divination, and on creating mechanisms for attracting customers that is not dependent on a particular device. Based on this policy, we will dedicate ourselves to optimizing SG&A expenses and other cost management as we carry out a multifaceted business, invest in advertising and publicity aimed at developing and growing new areas of business, and takes other active steps to strengthen our business foundation.

Regarding the forecast for the fiscal year ending April 30, 2014, we are progressing generally as initially planned and there are no changes to the results forecast that was announced on June 13, 2013.

3. Consolidated Financial Statements

(1) Quarterly consolidated balance sheets

(Units: 1,000s yen)

	Previous consolidated fiscal year (ended April 30, 2013)	Current consolidated first quarter (ended July 31, 2013)
Assets		
Current assets		
Cash and savings	4,188,950	4,181,038
Accounts receivable	1,696,899	1,373,361
Marketable securities	503,856	503,927
Merchandise and products	67,658	86,283
Income taxes receivable	88,167	119,026
Short-term loans receivable	—	11,419
Other	194,023	159,018
Allowance for doubtful accounts	(15,240)	(17,961)
Total current assets	6,724,317	6,416,114
Fixed assets		
Tangible fixed assets	137,266	171,967
Intangible fixed assets		
Software	369,462	330,174
Goodwill	1,991,846	2,010,711
Other	53,416	54,252
Total intangible fixed assets	2,414,726	2,395,138
Investments and other assets		
Investment securities	500,152	500,152
Long-term loans receivable	—	43,100
Other	349,848	356,253
Allowance for doubtful accounts	—	(21,604)
Total investments and other assets	850,001	877,901
Total fixed assets	3,401,994	3,445,008
Total assets	10,126,311	9,861,122
Liabilities		
Current liabilities		
Accounts payable - trade	304,100	262,665
Accounts payable - other	454,311	526,235
Long-term loans payable scheduled for repayment within 1 year	190,643	186,644
Corporate tax payable	384	90,573
Provision for web-point certificates	10,685	9,828
Other	124,434	158,870
Total current liabilities	1,084,557	1,234,816
Fixed liabilities		
Long-term loans payable	630,790	586,800
Other	1,008	900
Total fixed liabilities	631,798	587,700
Total liabilities	1,716,355	1,822,516

(Units: 1,000s yen)

	Previous consolidated fiscal year (ended April 30, 2013)	Current consolidated first quarter (ended July 31, 2013)
Net assets		
Shareholders' equity		
Capital stock	1,464,343	1,464,343
Capital surplus	1,389,718	1,389,718
Retained earnings	6,952,913	6,509,631
Treasury stock	(1,418,644)	(1,418,644)
Total shareholders' equity	8,388,331	7,945,049
Accumulated other comprehensive income		
Net unrealized holding gains on other securities	(1,804)	(1,804)
Foreign currency translation adjustments	(39,212)	38,086
Total accumulated other comprehensive income	(41,016)	36,282
Minority interests	62,641	57,274
Total net assets	8,409,955	8,038,606
Total liabilities and net assets	10,126,311	9,861,122

(2) Consolidated Profit and Loss Statement and Consolidated Comprehensive Income Statement
(Consolidated Profit and Loss Statement)
(Consolidated first quarter)

(Units: 1,000s yen)

	Previous consolidated first quarter (May 1, 2012 – July 31, 2012)	Current consolidated first quarter (May 1, 2013, - July 31, 2013)
Sales	2,369,332	1,882,260
Cost of sales	711,393	587,049
Gross profit on sales	1,657,938	1,295,210
Reversal of allowance for sales returns	5,385	—
Provision of allowance for sales returns	42	—
Net gross profit	1,652,595	1,295,210
Sales, general, and administrative expenses	1,049,084	1,119,786
Operating income	603,511	175,423
Non-operating income		
Interest income	107	283
Foreign exchange profit	—	1,880
Equity in earnings of affiliates	121	—
Reversal of allowance for doubtful accounts	3,424	1,945
Other	302	808
Total non-operating income	3,955	4,918
Non-operating expenses		
Interest paid	665	1,756
Provision of allowance for doubtful accounts	—	26,270
Other	32	—
Total non-operating expenses	698	28,027
Extraordinary loss	606,768	152,314
Extraordinary loss		
Loss on retirement and sales of fixed assets	122	76
Total extraordinary loss	122	76
Net income before income taxes and minority interest	606,646	152,238
Income taxes – current	212,961	86,847
Income taxes – deferred	26,814	(15,686)
Total income taxes	239,776	71,161
Net income before minority interests	366,870	81,076
Minority interests (losses) in net income	18,599	(5,366)
Net income	348,271	86,443

(Consolidated Comprehensive Income Statement)
(Consolidated first quarter)

(Units: 1,000s yen)

	Previous consolidated first quarter (May 1, 2012 – July 31, 2012)	Current consolidated first quarter (May 1, 2013, - July 31, 2013)
Income before minority interests	366,870	81,076
Other comprehensive income		
Foreign currency translation adjustments	—	77,298
Total other comprehensive income	—	77,298
Comprehensive income	366,870	158,375
(attributable to)		
Owners of the parent company	348,271	163,742
Minority interests	18,599	(5,366)

(Segment information)

I. Previous consolidated first quarter (May 1, 2012, - July 31, 2012)

1. Information about amounts of sales and income or loss for each reporting segment

(Units: 1,000s yen)

	Reporting segment			Other business	Total	Adjustment amounts	Quarterly consolidated profit/loss statement amount
	Content business	Commerce business	Total				
Sales							
Sales to outside customers	1,773,543	528,310	2,301,854	67,477	2,369,332	—	2,369,332
Inter-segment sales and transfers	—	—	—	—	—	—	—
Total	1,773,543	528,310	2,301,854	67,477	2,369,332	—	2,369,332
Segment income (loss)	769,795	70,404	840,199	(38,678)	801,521	(198,010)	603,511

II. Current consolidated first quarter (May 1, 2013, - July 31, 2013)

1. Information concerning sales and income or loss amounts for each reporting segment

(Units: 1,000s yen)

	Reporting segment				Reporting segment	Total	Adjustment amounts	Quarterly consolidated profit/loss statement amount
	Content business	Content business	Overseas business	Total				
Sales								
Sales to outside customers	1,470,964	251,001	109,872	1,831,838	50,422	1,882,260	—	1,882,260
Inter-segment sales and transfers	—	—	—	—	—	—	—	—
Total	1,470,964	251,001	109,872	1,831,838	50,422	1,882,260	—	1,882,260
Segment income (loss)	588,973	(92,818)	(31,651)	464,503	(117,145)	347,358	(171,934)	175,423