Special Feature: Discussions by Visionaries

Medium- to Long-Term Financial Strategies

The MEDIA DO Group aims to become a Publishing Platformer. We arranged a discussion between CFO Ryo Yamada, who is responsible for financial strategies and fund procurement, and CSO Hiroshi Kanda, who is charged with developing management strategy drafting and execution processes, on topics including the management strategies to be implemented toward accomplishing this goal and the financial strategies that will support these strategies.

Review of the Fiscal Year Ended February 28, 2021

What are your thoughts regarding the fiscal year ended February 28, 2021, from your respective standpoints as CFO and CSO?

Yamada: In the fiscal year ended February 28, 2021, MEDIA DO posted net sales of ¥83.5 billion, a year-on-year increase of 26.8%, and operating profit of ¥2.6 billion, a massive rise of 43.7%. Both of these figures represented record highs. This impressive performance was largely a result of growth in eBook demand stemming from the rise in demand from people seeking forms of entertainment that can be enjoyed inside as they increasingly stayed at home due to the COVID-19 pandemic.

Kanda: Performance was particularly strong in the first half of the fiscal year, which spanned the period from March 1 to August 31, 2020, as aggressive promotions by eBook companies spurred rapid growth in the overall market. This strong performance prompted us to institute upward revisions to our full-year forecasts for sales and profit in October. In the second half of the fiscal year, we felt the impacts of piracy websites. Although these impacts have not been too severe since the closure of particularly damaging websites in 2017 and 2018, we have been able to confirm the existence of numerous overseas piracy websites even today, and the access numbers of these websites are rising. Luckily, there has been progress in the development of regulatory frameworks for fighting piracy, as seen in the revisions to Japan's Copyright Act instituted in November 2020 and January 2021. The MEDIA DO Group is also taking action to eliminate piracy websites through coordination with the publishing industry, the communication industry, and the relevant government authorities. Returning to performance, the impacts of such websites resulted in us falling slightly short of our higher forecasts, but we achieved substantial growth, nonetheless, accomplishing the final net sales target for the previous medium-term management plan, which was launched in 2018, two years ahead of schedule.

Ryo Yamada
Executive Officer and CFO
(Chief Financial Officer)

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Hiroshi Kanda
Executive Officer and CSO
(Chief Strategy Officer)

Yamada: The COVID-19 pandemic sparked a rapid rise in digital transformation needs in all corners of society. In the publishing industry, this has translated to growth in demand for services that call upon the technologies and expertise of MEDIA DO. We are actively investing in growth from a medium- to long-term perspective, and ensuring financial health while conducting ongoing growth investments has been an important priority for the Company. MEDIA DO recently received two major boosts to its financial base: fund procurement through the issuance of share acquisition rights announced in October 2020, which raised our equity ratio to 28.0%, and a third-party allocation of shares to TOHAN CORPORATION in March 2021. These two transactions resulted in the Company acquiring ¥7.4 billion worth of funds, in total. At the same time, we sought to lay the foundations for future growth. We achieved three major successes with this regard during the second half of the fiscal year with the acquisitions of Nagisa, Inc., the Firebrand Group (Quality Solutions, Inc., NetGalley LLC, and their subsidiaries), and NIHONBUNGEISHA Co., Ltd.

Policies for Medium- to Long-Term Financial Strategies

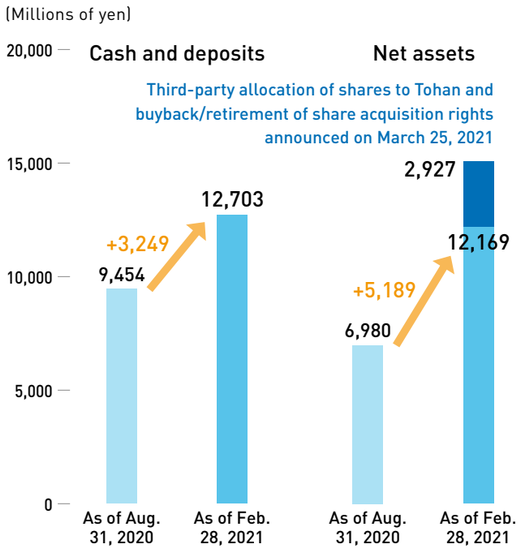
What financial strategies will MEDIA DO implement going forward?

Yamada: Looking first at our financial position, goodwill exceeded net assets up until the fiscal year ended February 28, 2019. However, the aforementioned fund procurement activities, among others, caused net assets to rise to ¥12.1 billion on February 28, 2021, more than double the ¥5.7 billion in goodwill on the same date. As a result, the debt-to-equity (D/E) ratio fell below 1.0 times, indicating a substantial improvement in our financial balance. In terms of management efficiency, meanwhile, we maintain a high level of 17.0% for return on equity (ROE).

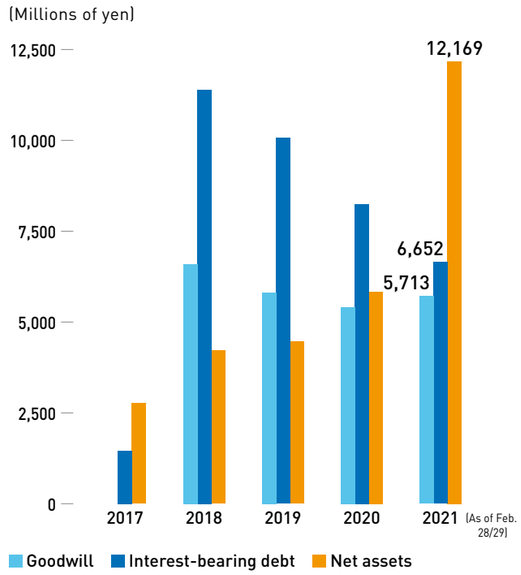
Kanda: The five-year medium-term management plan launched in 2018 positioned the fiscal year ending February 28, 2023, its final year, as the period for reaping the benefits of the initiatives implemented thus far. However, the market growth seen after the closure of major piracy websites in 2018 exceeded our expectations. Meanwhile, the advent of digital content using blockchain technology presented massive potential the likes of which had not been seen since the birth of smartphones. These changes in the operating environment led to the decision to revise our medium-term management plan. The new plan will position the fiscal years ending February 28, 2022 and 2023, as a period for continuing upfront investments from which full-fledged returns and earnings growth are projected to appear in the fiscal year ending February 29, 2024, and beyond. Moreover, we examined MEDIA DO's growth prospects from a medium- to long-term perspective. Through this examination, we reached the conclusion that our top priority at the moment should be establishing a solid position in the content market. As for the specific timing of earnings contributions and investment recovery, we intend to inform investors once the new plan has been fully compiled.

For growth investments, meanwhile, we have established policies based on two themes. The first theme is investment in the eBook distribution business, our current core business. In Japan, this business is expected to

Stabilization of Financial Balance



Major Balance Sheet Items



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continue to grow centered on manga going forward. We also see potential to explore markets for other text-based content for which digitization has not yet been pursued. The second theme is investment in new businesses for developing and distributing digital content with an eye to the entire content market that expands beyond written works. MEDIA DO began using blockchain technology to develop new digital content in 2018. These efforts have put us in the position to provide various products and services that are cutting-edge even when viewed from a global perspective.
Yamada: The domestic eBook market currently has a scale of roughly ¥400.0 billion, and MEDIA DO boasts a massive share of this market. Meanwhile, the overall content market is significantly larger, with a scale of approximately ¥4 trillion. MEDIA DO's entry into the overall content market will be a substantial undertaking, and I hope stakeholders will look forward to our endeavors in this market.

It has been stated that MEDIA DO intends to continue investments in even greater amounts. What type of internal investment standards and post-merger integration frameworks are in place?

Kanda: We have established the Investment Committee under the Board of Directors for the purpose of making decisions regarding investments. The establishment of this committee was based on the lessons learned after recording losses in association with past M&A investments in the fiscal year ended February 28, 2019. This committee helps us maintain discipline by only approving investments after adequate examinations of the background and goals of investments, the appropriateness of investment amounts, post-merger integration plans, and exit standards. During the pre-investment screening phase, risks and opportunities are identified from a variety of perspectives, including that of the relevant business divisions as well as financial, legal affairs, and human resource perspectives. We also formulate investment strategy policies that define target investment fields and candidates as well as investment budgets, and our Companywide portfolio is reviewed regularly.

Yamada: One of the financial indicators we use as a standard for investment decisions is weighted-average cost of capital (WACC). MEDIA DO's level of WACC is between 6% and 7%, and returns exceeding this level have been defined as the minimum hurdle rate for investments. However, we recognize that acquisitions targets can be in various growth stages and have differing investment recovery periods. Accordingly, there are cases in which we might underestimate risks if we simply apply this WACC standard uniformly to all candidates. We therefore set WACC standards for each candidate based on their respective risk levels. By adjusting the current value of the candidate by this standard, we confirm whether the acquisition price being proposed in negotiations is appropriate.
Kanda: M&A activities are an important means of acquiring management resources MEDIA DO lacks as part of the process of expanding its business domain. For example, the Firebrand Group, which we acquired in the fiscal year ended February 28, 2021, possesses substantial expertise regarding ERP systems for publishing paper books and other articles. Nihonbungeisha, meanwhile, has a robust lineup of content centered on digital manga for male readers, and this company will be a powerful asset in expanding our imprint business. Moreover, the capital and business alliance with major paper book wholesaler Tohan announced in March 2021 has the potential to generate massive synergies in the distribution of physical and digital content, which will be produced by combining the differing competitive advantages of Tohan and MEDIA DO.
Yamada: MEDIA DO has conducted numerous M&A transactions, meaning that post-merger integration is a matter of utmost importance. Based on this recognition, we intend to incorporate detailed guidelines for post-merger action into the new medium-term management plan. As a recent example of our post-merger integration efforts, we worked closely with Nihonbungeisha to align our visions and set qualitative and quantitative targets to be pursued by both companies. Progress with regard to these targets will be gauged during the post-merger integration process in accordance with a monitoring sheet. As for the staff that will be responsible for actually advancing the integration, MEDIA DO will supply half of the members of Nihonbungeisha's Board of Directors, and representatives will be assigned by both companies to guide the integration process.

> **We reached the conclusion that our top priority for pursuing medium- to long-term growth should be establishing a solid position in the content market.**

> **I will support the corporate strategies overseen by the CSO through financing and timely information provision.**

Growth investments will primarily be funded using operating cash flows, and these cash flows will be supported by the foundations we have established for generating consistent earnings in the eBook distribution business, which accounts for 98.6% of the Company's net sales, through the incorporation of market growth and the expansion of our customer base. However, as we are preparing for the massive undertaking that will be advancing into the overall content market, it can be expected that MEDIA DO will remain in the growth investment phase for quite some time. It is therefore possible that we will require funds that go beyond the scope of operating cash flows for conducting the necessary investments. Given that the fund procurement efforts undertaken in December 2020 and March 2021 greatly improved our financial position, debt finance centered on borrowings will be our primary instrument for meeting additional funding demand. However, we also anticipate that we might have to once again undertake equity finance measures in the medium term. Such measures will be based on consideration of our financial position as well as the growth potential of the respective investment candidate. As for dividend payments, we plan to target a total return ratio of 20% over the foreseeable future as MEDIA DO will still be in a growth phase. I hope that shareholders and investors will be accepting of this policy based on the promise that we will pay them back in long-term returns fueled by the growth to be achieved going forward.

Roles of the CFO and CSO in MEDIA DO's Future Growth

What do you both see as the roles you need to fulfill at MEDIA DO going forward?

Kanda: I oversee the Corporate Planning Office. This division is responsible for the establishment of medium-term management plans and other Companywide strategies, investor relations (IR) and other information disclosure activities, and M&A activity-related processes spanning from candidate selection to investment execution. I am thus tasked with helping propose investment candidates that match our growth strategies and with formulating and implementing post-merger integration policies that will get investees operating in line with MEDIA DO's corporate governance policies while preserving the positive aspects of their corporate culture. Moreover, I practice careful and effective monitoring of trends in the performance of investees and disclose this information to outside stakeholders. I thereby aim to engage in appropriate communication with stakeholders while contributing to the growth of MEDIA DO and to shareholder returns.

Up until now, one could not be blamed for thinking that the sales increases MEDIA DO has enjoyed have merely been a product of the growth of the eBook market or of the resulting favorable operating environment. For this reason, it is important for MEDIA DO to evolve into a company that stakeholders will recognize as a driving force behind the growth of the market. Our approach toward achieving this evolution should involve establishing a cycle of effectively managing investment projects to grow the associated businesses and generate earnings as part of our efforts to develop various new services that lead the publishing and content industries. As CSO, I look to help chart our course for becoming such a new MEDIA DO and to proactively communicate this course to those outside of the Company.
Yamada: The Finance Department is responsible for procuring the funds necessary for M&A activities as well as controlling levels of invested capital on a by-business basis and ensuring that investments have a sufficient chance of being recovered. In this manner, our role is to secure the funding necessary for the overarching corporate strategies overseen by the CSO. At the same time, we devote a lot of funds to personnel expenses given that MEDIA DO is a technology company. Investing in human capital and comfortable workplace environments is a priority I think we should focus on when it comes to future M&A activities and other aspects of operations. Moreover, corporate strategies and financial strategies must be closely coordinated. For this reason, I look to maintain close communication with CSO Kanda and work together with him to improve MEDIA DO's corporate value and return appropriate profits to our shareholders and other stakeholders.