

This English translation of the financial report was prepared for reference purposes only and is qualified in its entirety by the original Japanese version. The financial information contained in this report is derived from our unaudited consolidated financial statements appearing in item 2 of this report.

ARTERIA Networks Corporation Consolidated Financial Report For the Six-month Period Ended September 30, 2020 [IFRS]

November 13, 2020

Company name	ARTERIA Networks Corporation	Stock listing: Tokyo Stock Exchange – First Section
Stock ticker	4423	URL https://www.arteria-net.com/
Representative	(Position) Representative Director, President & CEO	(Name) Koji Kabumoto
Name of contact	(Position) Managing Executive Officer & CFO	(Name) Seiichi Tateishi TEL 03 (6823) 0349
Schedule date of quarterly report filing:	November 13, 2020	
Scheduled date of dividend payment:	-	
Supplemental quarterly results materials:	Yes	
Earnings results briefing:	Yes (For institutional investors, security analysts)	

(Millions of yen; amounts are rounded down to the nearest million yen)

1. Consolidated Financial Results For the Six-month Period Ended September 30, 2020 (April 1, 2020 – September 30, 2020, “the second quarter”)

(1) Consolidated Operating Results

(Percentages are shown as year-on-year changes)

	Net sales		Operating profit		Profit before income taxes		Profit		Profit attributable to owners of the parent		Comprehensive income	
		%		%		%		%		%		%
Six-month period ended September 30, 2020	25,869	1.6	4,163	(1.8)	3,976	(1.1)	2,764	(1.3)	2,581	(1.3)	2,828	(2.4)
Six-month period ended September 30, 2019	25,459	7.1	4,237	15.0	4,021	16.4	2,800	11.0	2,614	12.3	2,896	11.1

	Basic earnings per share	Diluted earnings per share
	Yen	Yen
Six-month period ended September 30, 2020	51.65	-
Six-month period ended September 30, 2019	52.29	-

(Reference) (Percentages are shown as year-on-year changes)

	Adjusted EBITDA	
		%
Six-month period ended September 30, 2020	8,677	5.4
Six-month period ended September 30, 2019	8,230	10.5

(2) Consolidated Financial Position

	Total assets	Total equity	Equity attributable to owners of the parent	Ratio of equity attributable to owners of the parent to total assets
As of September 30, 2020	86,159	22,378	20,634	23.9%
As of March 31, 2020	90,779	22,706	20,709	22.8%

2. Dividends

	Dividends per share				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
	Yen	Yen	Yen	Yen	Yen
Fiscal year ended March 31, 2020	-	-	-	52.97	52.97
Fiscal year ending March 31, 2021	-	-			
Fiscal year ending March 31, 2021 (forecasted)			-	54.01	54.01

Note

Revision of forecasted dividend: None

3. Consolidated Financial Results Forecast for the Fiscal Year Ending March 31, 2021 (April 1, 2020 to March 31, 2021)

(Percentages are shown as year-on-year changes)

	Net sales		Operating profit		Profit before income taxes		Profit		Profit attributable to owners of the parent		Basic earnings per share
		%		%		%		%		%	Yen
Fiscal year ending March 31, 2021	52,235	1.4	8,854	2.1	8,374	2.0	5,777	1.9	5,401	2.0	108.02

Note

Revision of forecast: None

* Notes

(1) Changes in significant consolidated subsidiaries (which resulted in changes in scope of consolidation) during the six-month period ended September 30, 2020: None

(2) Changes in accounting policies and estimates

- (i) Changes in accounting policies required under IFRS: None
- (ii) Other changes in accounting policies: None
- (iii) Changes in accounting estimates: None

(3) Number of outstanding shares (Common stock)

(i) Number of shares outstanding (including treasury stock)	As of September 30, 2020	50,000,000 Shares	As of March 31, 2020	50,000,000 Shares
(ii) Number of treasury stock	As of September 30, 2020	39,761 Shares	As of March 31, 2020	61 Shares
(iii) Number of weighted average common stock outstanding	As of September 30, 2020	49,977,377 Shares	As of September 30, 2019	49,999,939 Shares

* This consolidated financial report is not subject to interim review procedures by certified public accountants or an audit firm.

* Regarding appropriate use of forecasts and other special notes

Regarding appropriate use of forecasts

This report contains statements that constitute forward-looking statements including estimations, forecasts targets and plans. Such forward-looking statements do not represent any guarantee by the Company of future performance. Our actual results may vary materially from those we currently anticipate. Any forward-looking statements in this report are based on the current assumptions and beliefs of the Company in light of the information currently available to it, and involve known and unknown risks, uncertainties and other factors. Regarding the use and definition of forecasts please refer to “Forecasts” under “1. Qualitative Information.”

Regarding (Reference) information

- (1) Adjusted EBITDA = profit + income taxes – finance income + finance costs + depreciation and amortization + loss on disposal of supplies and equipment installed at customers’ premises + IPO preparation expenses
- (2) IPO preparation expenses consist of expenses incurred in preparing for our IPO that are not expected to recur. Such expenses include fees paid to accounting and other advisors in connection with preparation for our IPO and are included as part of IPO related costs.
- (3) Loss on disposal of supplies and equipment installed at customers’ premises consist of such losses recorded as part of cost of sales and other expense in our consolidated statement of income.
- (4) Adjusted EBITDA is not prepared in accordance with article 193-2 (1) of the Financial Instruments and Exchange Act of Japan and has not been audited or reviewed by the Company’s independent auditors.
- (5) Adjusted EBITDA reflects some expenses incurred in preparing for our IPO that are not expected to recur after the completion of our IPO and do not reflect the underlying performance of our business. These non-IFRS measures are supplemental financial measures that we believe are useful for investors to assess the operating performance and profitability of our business.
- (6) Adjusted EBITDA excludes certain items which impacts profit. These non-IFRS measures should not be considered in isolation or as a substitute for the most comparable financial measures presented in accordance with IFRS. These indices are meant to be illustrative only and are calculated based on assumptions which might differ from those used by other companies and should therefore not be used as a basis for comparison.

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1. Qualitative Information / Consolidated Financial Statements, etc.

(1) Operational Results

During the second quarter as a result of the spread of the COVID-19 pandemic, the global and domestic economy have been significantly affected and economic conditions remain tough. Although domestic consumer consumption is gaining traction and the economy has shown signs of recovery, the future impact of COVID-19 will need to be monitored continuously.

In the information and telecommunications market, where the Group operates, we have seen a sudden slowdown in corporate revenues leading to curbing, postponement and cancellations of ICT-related capital expenditure as a result of COVID-19.

The spread of the virus resulted in less populated offices and demand for IP phone services diminished. The promotion of a new workstyle, allowing people to work anywhere and anytime, has driven up the use of telecommuting and satellite offices. This is creating additional needs for high-speed communications and secure network services.

In this business environment, sales of the core services in each of our main business areas continued to grow year on year. However, in certain of our services we saw a decrease in sales while expansion of telecommuting led to higher traffic volumes and countermeasure-related costs exceeded our forecast.

Anticipating further demand growth for high-quality communications in the future, we announced the build-out of a service infrastructure using SD-WAN*¹ technology in September 2020. We are currently developing services utilizing this new infrastructure.

In internet services, sales for our core products FTTx and ISP services increased steadily year on year.

Driven by increased cloud usage and the promotion of telecommuting generating more external access to corporate networks, the roll out of our best effort basis maximum 10Gbps (uplink and downlink) service is going well. Demand for large bandwidth and high-quality FTTx services remain firm.

In ISP services, orders for VNE*² services, which we started offering in April 2020 and enable the provision of a higher quality service, are growing steadily. Consumers are increasingly reexamining the quality of their internet access services new orders and inquiries from our OEM Flet's partners continue to trend upwards.

On the other hand, impacted by the shift in workstyles, phone calls generated from offices decreased and our IP phone service showed negative growth year on year. We expect this trend to continue for the foreseeable future.

In network services, our customers' operations have been impacted by the spread of COVID-19 and some delays in service provision and requests for payment reductions occurred. We also experienced a loss of business opportunities impacting certain areas of our business as a result of the postponement of the Olympic Games.

Although demand for leased circuits from OTTs*³ and mobile operators, who are proactively investing in the build-out of proprietary backbone networks, is still trending strong the year-on-year growth rate has decreased as a result of the above-mentioned impact on corporate operations.

In VPN services, while we have realized net sales growth year on year, the growth rate is slowing down.

Furthermore, as a result of customers reviewing their cost structures, we experienced some large cancellations in our data center services leading to a year-on-year decrease.

In condominium internet services, both orders and sales increased year on year in our main market the owned condo market, and the rental apartments market. In order to accommodate higher traffic volumes generated in condos, driven by more telecommuting, we enhanced our telecommunication infrastructure. We also reinforced our call center operations to cater to the increased amount of incoming calls. Both these initiatives drove up costs beyond our forecasts.

While costs were incurred to sustain the quality of our service increased, the demand for high-quality and wide broadband services, driven by more telecommuting, has also grown recently. We saw an increase in inquiries for our high-quality broadband access service up to 10 Gbps using a dedicated fiber line, which we were first to introduce in the market. We expect to see further future growth in orders and sales for this product.

In June 2020 we announced a newly developed internet service catering to small and medium sized condos named Five.A which boasts high quality and low cost. Orders for Five.A are increasing steadily, hereby contributing significantly to our share expansion in the rental market.

In addition, we will aim to announce new services utilizing the SD-WAN technology which we announced in September 2020.

As a result, during the second quarter net sales increased by 410 million yen (1.6%) year on year to 25,869 million yen. Operating income decreased by 74 million yen (1.8%) year on year to 4,163 million yen, profit before income taxes for the period decreased by 44 million yen (1.1%) year on year to 3,976 million yen. Profit for the period attributable to owners of the parent decreased by 33 million yen (1.3%) year on year to 2,581 million yen.

Notes:

- 1 Software Defined Wide Area Network: a specific application of software-defined networking (SDN) technology expanding from LAN (Local Area Network) to WAN (Wide Area Network) connections. SDN offers bandwidth on demand, security, and other functions through software to enable shorter network connection times and easy changes to configurations and functions.
- 2 Virtual Network Enabler: service provider that offers network facilities and systems required for IPoE connection to internet service providers.
- 3 Over The Top

(2) Financial Position

	March 31, 2020	September 30, 2020	Change
Total assets (millions of yen)	90,779	86,159	(4,620)
Total equity (millions of yen)	22,706	22,378	(328)
Equity attributable to owners of the parent (millions of yen)	20,709	20,634	(75)
Ratio of equity attributable to owners of the parent (%)	22.8	23.9	1.1
Balance of borrowings (millions of yen)	40,162	39,240	(921)

During the second quarter, total assets decreased by 4,620 million yen from the end of the previous fiscal year, to 86,159 million yen. Equity attributable to owners of the parent decreased by 75 million yen year on year, to 20,634 million yen. As a result, the ratio of equity attributable to owners of the parent amounted to 23.9%.

Overview of Cash Flows

During the second quarter, there were no COVID-19 related matters that had a significant impact on our business and the group maintained a stable cash flow. Against this backdrop, the balance of cash and cash equivalents decreased by 991 million yen year on year, to 7,789 million yen.

(Cash flows from operating activities)

Cash generated by operating activities increased by 4 million yen year on year, to 6,058 million yen, mainly due to an increase in trade payables, while there was an increase in income taxes paid.

(Cash flows from investing activities)

As a result of acquiring fixed assets and intangible assets, cash used for investing activities increased by 1,678 million yen year on year, to 4,800 million yen.

Consequently, free cash flow (*) in the second quarter decreased by 1,674 million yen year on year to 1,257 million yen cash generated.

(Cash flows from financing activities)

Cash used for financing activities increased by 2,025 million yen year on year, to 5,465 million yen, due to payment of dividends and repayment of lease liabilities.

* Free cash flow: cash flows from operating activities + cash flows from investing activities.

(3) Forecasts

Although the Group experienced some COVID-19 related impact during the second quarter, all core services in our main business areas sustained year-on-year growth. While we expect the COVID-19 impact to continue throughout the current fiscal year, the trend in new orders and inquiries is improving. Costs related to higher traffic volumes have reached their peak and we intend to execute reduction measures going forward.

It is our view that the combination of cost controls and the improving trends in new orders and inquiries will enable us to limit the COVID-19 impact within the scope of our forecasts announced at the beginning of the fiscal year. We are therefore reiterating our earnings forecasts, announced in the “Consolidated Financial Report For the Fiscal Year Ended March 31, 2020” disclosed on May 15, 2020, at this point in time. We will announce any necessary future forecast revisions timely depending on the movement of our earnings results.

2. Quarterly Condensed Consolidated Financial Statements

(1) Quarterly Condensed Consolidated Statement of Financial Position

	Previous fiscal year (March 31, 2020)	Second quarter of the current fiscal year (September 30, 2020)
	Millions of yen	Millions of yen
Assets		
Current assets		
Cash and cash equivalents	11,996	7,789
Trade and other receivables	6,362	6,287
Other financial assets	10	8
Inventories	151	235
Other current assets	1,526	1,977
Total current assets	20,047	16,298
Non-current assets		
Property, plant and equipment	38,152	37,618
Goodwill	12,646	12,646
Intangible assets	15,362	15,090
Other financial assets	3,012	3,117
Deferred tax assets	821	700
Other non-current assets	735	688
Total non-current assets	70,732	69,861
Total assets	90,779	86,159

	Previous fiscal year (March 31, 2020)	Second quarter of the current fiscal year (September 30, 2020)
	Millions of yen	Millions of yen
Liabilities and Equity		
Liabilities		
Current liabilities		
Borrowings	1,938	2,089
Trade and other payables	5,310	3,810
Lease liabilities	2,609	2,544
Income and other taxes payable	1,369	1,008
Provisions	181	181
Other current liabilities	4,214	3,724
Total current liabilities	15,624	13,359
Non-current liabilities		
Borrowings	38,223	37,151
Long-term lease liabilities	7,146	6,069
Retirement benefit liabilities	718	798
Provisions	2,880	2,919
Deferred tax liabilities	2,668	2,589
Other non-current liabilities	810	892
Total non-current liabilities	52,448	50,421
Total liabilities	68,072	63,780
Equity		
Common stock	5,150	5,150
Capital surplus	4,640	4,647
Retained earnings	10,873	10,806
Treasury stock	(0)	(79)
Other components of equity	46	109
Total equity attributable to owners of the parent	20,709	20,634
Non-controlling interests	1,997	1,744
Total equity	22,706	22,378
Total liabilities and equity	90,779	86,159

(2) Quarterly Condensed Consolidated Statement of Income and Quarterly Condensed Consolidated Statement of Comprehensive Income
(Quarterly Condensed Consolidated Statement of Income for the six-month period ended September 30)

	For the six-month period ended September 30, 2019 (From April 1, 2019 To September 30, 2019)	For the six-month period ended September 30, 2020 (From April 1, 2020 To September 30, 2020)
	Millions of yen	Millions of yen
Net sales	25,459	25,869
Cost of sales	16,934	17,673
Gross profit	8,525	8,196
Selling, general and administrative expenses	4,229	3,951
Other income	100	34
Other expenses	159	115
Operating profit	4,237	4,163
Finance income	50	60
Finance costs	266	246
Profit for the period before income taxes	4,021	3,976
Income taxes	1,221	1,212
Profit for the period	<u>2,800</u>	<u>2,764</u>
Profit for the period attributable to:		
Owners of the parent	2,614	2,581
Non-controlling interests	185	183
Profit for the period	<u>2,800</u>	<u>2,764</u>
Earnings per share		
Basic earnings per share (yen)	52.29	51.65
Diluted earnings per share (yen)	-	-

(Quarterly Condensed Consolidated Statement of Comprehensive Income for the six-month period ended September 30)

	For the six-month period ended September 30, 2019 (From April 1, 2019 To September 30, 2019)	For the six-month period ended September 30, 2020 (From April 1, 2020 To September 30, 2020)
	Millions of yen	Millions of yen
Profit for the period	2,800	2,764
Other comprehensive income		
Items that will not be reclassified to profit or loss		
Financial assets measured at fair value through other comprehensive income	95	63
Total items that will not be reclassified to profit or loss	95	63
Total other comprehensive income, net of tax	95	63
Comprehensive income for the period	2,896	2,828
Comprehensive income for the period attributable to:		
Owners of parent	2,710	2,644
Non-controlling interests	185	183
Comprehensive income for the period	2,896	2,828

(3) Quarterly Condensed Consolidated Statement of Changes in Equity
For the six-month period ended September 30, 2019 (From April 1, 2019 To September 30, 2019)

	Equity attributable to owners of the parent					
	Common stock	Capital surplus	Retained earnings	Treasury stock	Other components of equity	
					Financial assets measured at fair value through other comprehensive income	Total
Millions of yen	Millions of yen	Millions of yen	Millions of yen	Millions of yen	Millions of yen	
As of April 1, 2019	5,150	5,951	5,575	(0)	(28)	(28)
Profit for the period	-	-	2,614	-	-	-
Other comprehensive income	-	-	-	-	95	95
Comprehensive income for the period	-	-	2,614	-	95	95
Cash dividends	-	(1,310)	-	-	-	-
Total transactions with owners	-	(1,310)	-	-	-	-
As of September 30, 2019	5,150	4,640	8,190	(0)	66	66

	Equity attributable to owners of the parent		
	Equity attributable to owners of the parent	Non-controlling interests	Total
	Millions of yen	Millions of yen	Millions of yen
As of April 1, 2019	16,647	2,089	18,736
Profit for the period	2,614	185	2,800
Other comprehensive income	95	-	95
Comprehensive income for the period	2,710	185	2,896
Cash dividends	(1,310)	(463)	(1,774)
Total transactions with owners	(1,310)	(463)	(1,774)
As of September 30, 2019	18,047	1,811	19,858

For the six-month period ended September 30, 2020 (From April 1, 2020 To September 30, 2020)

	Equity attributable to owners of the parent					
	Common stock	Capital surplus	Retained earnings	Treasury stock	Other components of equity	
					Financial assets measured at fair value through other comprehensive income	Total
Millions of yen	Millions of yen	Millions of yen	Millions of yen	Millions of yen	Millions of yen	
As of April 1, 2020	5,150	4,640	10,873	(0)	46	46
Profit for the period	-	-	2,581	-	-	-
Other comprehensive income	-	-	-	-	63	63
Comprehensive income for the period	-	-	2,581	-	63	63
Purchase of treasury stock	-	-	-	(79)	-	-
Cash dividends	-	-	(2,648)	-	-	-
Share-based payment transactions	-	7	-	-	-	-
Total transactions with owners	-	7	(2,648)	(79)	-	-
As of September 30, 2020	5,150	4,647	10,806	(79)	109	109

	Equity attributable to owners of the parent	Non-controlling interests	Total
	Millions of yen	Millions of yen	Millions of yen
As of April 1, 2020	20,709	1,997	22,706
Profit for the period	2,581	183	2,764
Other comprehensive income	63	-	63
Comprehensive income for the period	2,644	183	2,828
Purchase of treasury stock	(79)	-	(79)
Cash dividends	(2,648)	(436)	(3,084)
Share-based payment transactions	7	-	7
Total transactions with owners	(2,720)	(436)	(3,156)
As of September 30, 2020	20,634	1,744	22,378

(4) Quarterly Condensed Consolidated Statement of Cash Flows

	For the six-month period ended September 30, 2019 (From April 1, 2019 To September 30, 2019)	For the six-month period ended September 30, 2020 (From April 1, 2020 To September 30, 2020)
	Millions of yen	Millions of yen
Cash flows from operating activities		
Profit for the period before income taxes	4,021	3,976
Depreciation and amortization	3,892	4,401
Finance income	(50)	(60)
Finance costs	266	246
Loss on disposal of property, plant and equipment	101	97
Decrease (increase) in trade and other receivables	591	74
(Increase) decrease in inventories	125	(121)
(Decrease) increase in trade and other payables	(651)	(3)
Other	(1,591)	(870)
Subtotal	6,704	7,740
Interest received	0	0
Dividend income received	33	49
Interest paid	(193)	(175)
Income taxes paid	(491)	(1,556)
Net cash provided by (used in) operating activities	6,053	6,058
Cash flows from investing activities		
Purchases of property, plant and equipment	(2,848)	(4,107)
Proceeds from sale of property, plant and equipment	39	-
Disposals of property, plant and equipment	(128)	(178)
Purchases of intangible assets	(139)	(369)
Other	(44)	(144)
Net cash (used in) provided by investing activities	(3,121)	(4,800)
Cash flows from financing activities		
Repayments of long-term borrowings	(817)	(969)
Repayments of lease liabilities	(840)	(1,323)
Dividends paid	(1,309)	(2,647)
Dividends paid to non-controlling interests	(463)	(436)
Purchase of treasury stock	-	(79)
Other	(8)	(8)
Net cash (used in) provided by financing activities	(3,439)	(5,465)
Net increase (decrease) in cash and cash equivalents	(507)	(4,207)
Cash and cash equivalents at the beginning of the period	9,288	11,996
Cash and cash equivalents at the end of the period	8,780	7,789

(5) Notes to Consolidated Financial Statements

(Going Concern Assumption)

Not applicable.

(Accounting Estimates and Judgements involving Estimates)

In preparing the consolidated financial statements in accordance with IFRS, management is required to make judgments, estimates and assumptions that may affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. However, actual results may differ from those estimates and assumptions.

The estimates and underlying assumptions are reviewed on an ongoing basis. The effect of any changes in accounting estimates is recognized in the period in which the estimates are changed.

Judgments, estimates and assumptions, which may have a material impact on the amounts recognized in the quarterly condensed consolidated financial statements of the current fiscal year are the same as those for the consolidated financial statements of the previous fiscal year.