



CRESCO LTD

Q2 Financial Results Briefing for the Fiscal Year Ending March 2020 for Securities Analysts

November 14, 2019

Event Summary

[Company Name]	CRESCO LTD	
[Event Type]	Earnings Announcement	
[Event Name]	Q2 Financial Results Briefing for the Fiscal Year Ending March 2020 for Securities Analysts	
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[Date]	November 14, 2019	
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[Venue]	Kabutocho Heiwa Building 2F, 3-3 Kabutocho Nihonbashi, Chuo-ku, Tokyo 103-0026 (Hosted by The Securities Analysts Association of Japan)	
[Venue Size]	145 m ²	
[Participants]	24	
[Number of Speakers]	2	
	Hiroyuki Nemoto	President
	Michiaki Yonezaki	Department Manager, Public Relations & IR Office

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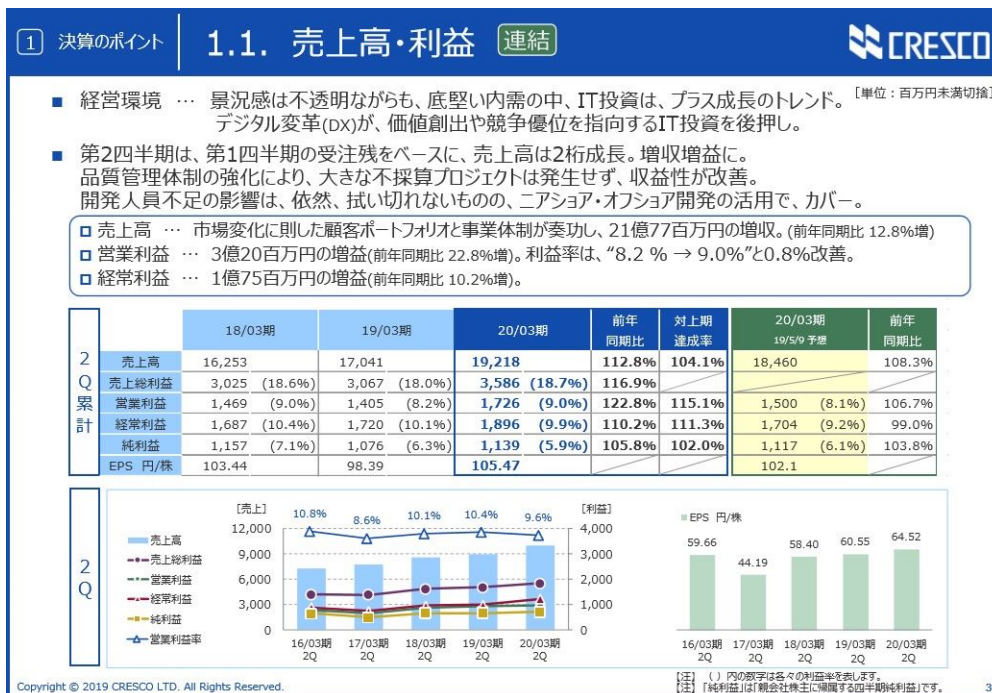


Presentation

Moderator: Now it is time to start the Second Quarter Financial Briefing for the fiscal year ending March 2020. I would like to introduce Mr. Hiroyuki Nemoto, President and Mr. Michiaki Yonezaki, Department Manager, Public Relations & IR Office.

An hour briefing is scheduled. Please fill out the questionnaire later.

Nemoto: I am Nemoto, CRESCO LTD. Thank you for coming in this evening. I would like to talk for about 20 minutes and then we will proceed to the question-and-answer session. Please look at the materials including the slides which are distributed.



First, even though there is some uncertainty depending on the industry, I feel that IT investment is still very active. Based on the keywords "Digital Innovation" and "DX," I feel that investment is continuing based on the recognition that IT investment is necessary for companies to revitalize their businesses.

Regarding the second quarter, the double-digit growth in net sales has resulted in higher sales and profits as described here. It shows that sales were 19.2 billion yen, 112.8% increase compared to the same quarter of the previous year. In addition, we are seeing double-digit growth in profits and operating income; therefore I believe that this is a good outcome for the first half of the fiscal year.

Last year, there was a quality problem occurring in the first quarter and it was delayed. Since there is no major unprofitable project in this fiscal year, which I will discuss later, it is said that profitability is improving. In terms of profit margins, operating income is 8.2% to 9.0%, which means that operating income has been rising accordingly.

On the other hand, there is a shortage of development personnel. Even though demand is still high, we are still unable to deal with many problems because of a shortage of people or because of the inability to establish a system. However, the current situation is that we are gradually solving this problem by the near-shore and offshore development.

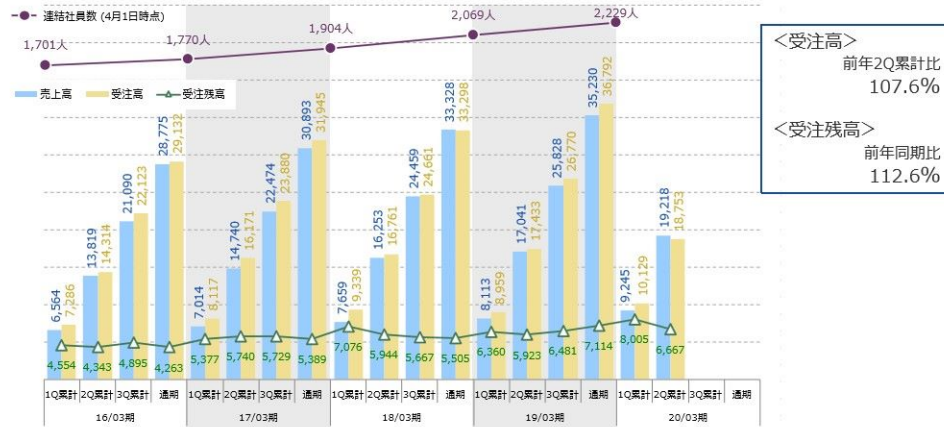
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【単位：百万円未満切捨】

- 顧客の引合いは、攻めのIT投資やデジタル変革(DX)を背景に活況が続く。
 - ソフトウェア開発 … 金融関連は微増、既存顧客(公共サービス、流通・その他)の引合いが増加。
 - 組込み型ソフトウェア開発 … 車載関連顧客の受注計上が一部10月に。主要顧客の引合い自体は、順調。
- サービス事業の拡販、デジタル変革(DX)案件の受注が拡大。グループ連携による開発体制の強化が、課題。



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We feel that the amount of orders received and order backlog were steadily increasing year-on-year, at 112.6% compared with the same period of the previous fiscal year.

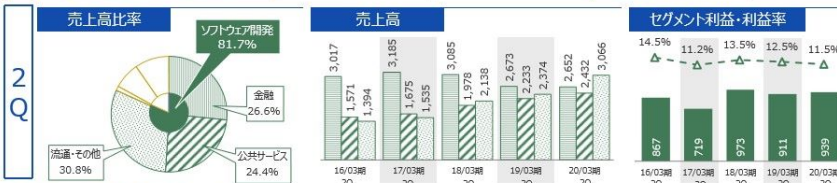
【単位：百万円未満切捨】

■ ソフトウェア開発

- 営業および開発体制(オフショアを含む)の強化、グループ連携を徹底し、売上高は 13.1%の増収。
- プロジェクトマネジメント、品質管理の強化に注力し、収益性が改善。セグメント利益は 22.2%の増益。
- 前年度に実施したM&A(アルス、イーテクノ)による連結効果は、プラス材料。

- 金融 … 顧客毎の濃淡が大きく、微増。全体では回復基調。(前年同期比 11百万円の増収)
- 公共サービス … 既存大口顧客(人材、旅行、運輸)のIT投資が増加。(前年同期比 4億2百万円の増収)
- 流通・その他 … 子会社(アイソ、クレスコ北陸、ネクサス)における受注が拡大。(前年同期比 14億6百万円の増収)

		18/03期	19/03期	20/03期	前年同期比
2Q累計	ソフトウェア売上高	13,586	13,937	15,756	113.1%
	金融	6,083	5,224	5,235	100.2%
	公共サービス	3,521	4,211	4,613	109.6%
	流通・その他	3,982	4,501	5,907	131.2%
セグメント利益(率)		1,648 (12.1%)	1,419 (10.2%)	1,734 (11.0%)	122.2%



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This is an analysis for each segment. Software development revenues rose 13.1% year-on-year. In terms of profits, since we strengthened project quality control and had no major losses, segment profit was up 22%. We conducted M&A between a company called ARS Corporation Ltd. and a company called e-techno.Co.,Ltd. Although they are not a large company, the effect of consolidation has been slightly positive.

By segment, we see a slight increase in the financial services sector, which is on a recovery trend. It is already a bottom out.

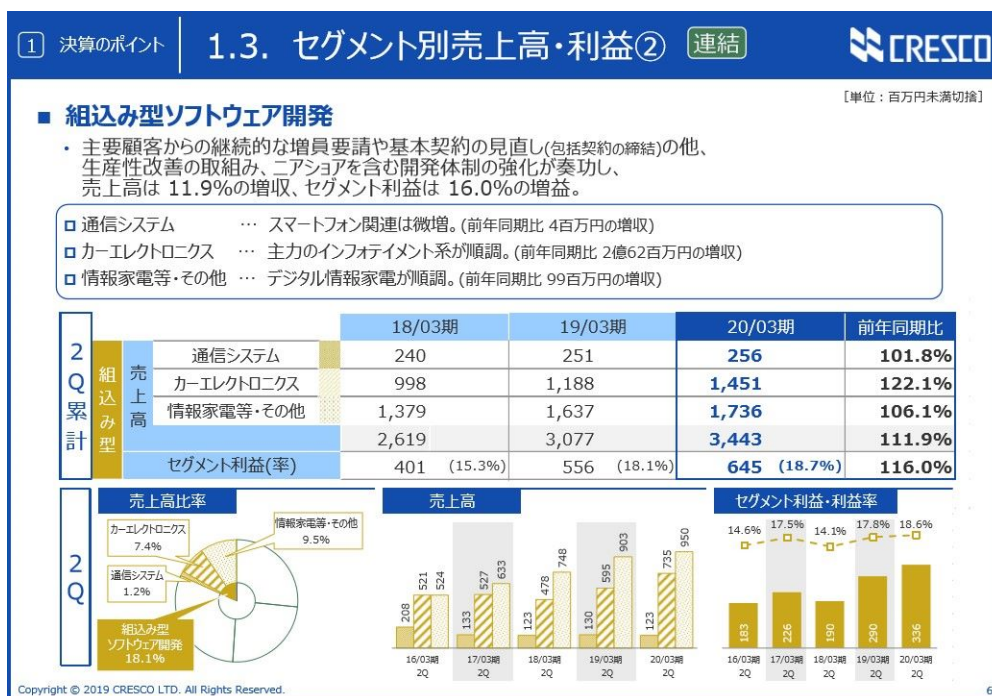
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In terms of public services such as human resources, travel, and transportation, IT investment is increasing. However, as I mentioned earlier, the system is not sufficiently organized. We have received many requests from customers for better organized system.

In distribution and other sectors, the number of large projects at subsidiaries and other sectors has also been increasing. The sales increased 130% year-on-year.



It is about the embedded software development. There have been ongoing requests from major customers to increase the number of personnel and revisions to the basic contract. The near shore development in suburban cities has become possible, which in a past a great deal of action had been done primarily in Tokyo. This resulted in that the net sales and segment profits grow.

There was a slight increase in telecommunications-related projects. However, we do not expect that this work will grow significantly in the future, we will continue to do so.

The car electronics market has been growing by 20%, but it is slightly uncertain. I feel that customer investment will decline somewhat or remain flat soon. Looking at the year-on-year rate of increase, it has been steadily increasing by approximately 20% in the Fiscal Year 2018 and Fiscal Year 2019, but I feel that this is not the momentum.

As for home information appliances, sales of digital consumer electronics have been favorable, reaching 106.1% increase, and the figure is as high as 1.7 billion yen.

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[単位：百万円未満切捨]

- 2019年度下半期の経済環境は、米中経済摩擦や日韓関係の悪化、世界景気の減速感、10月からの消費税増税等、多くの懸念はあるものの、IT投資は、「攻めのIT経営」を主眼としたデジタル変革(DX)や東京オリンピック、インバウンドへの対応などが下支えとなり、勢いを継続すると予測。
- 上期業績および足元の業況から、上振れ可能性はあるものの、現時点では、期末業績予想に変更無し。技術および品質面での更なる強化を図るとともに、AI、クラウド技術者の拡充教育をはじめ、他社とのアライアンス推進、オープンイノベーション・産学連携による新ビジネスの創出に注力し、質的、量的成長を目指す。
- 2019年5月9日に発表した、**業績予想に変更なし**。

通期	19/03期				20/03期			
	18/5/8 予想	前年同期比	実績	前年同期比	達成率	19/5/9 予想	前年同期比	
	売上高	35,500	106.5%	35,230	105.7%	99.2%	37,880	107.5%
売上総利益			6,673 (18.9%)	105.8%				
営業利益	3,280 (9.2%)	106.1%	3,207 (9.1%)	103.7%	97.8%	3,400 (9.0%)	106.0%	
経常利益	3,580 (10.1%)	102.5%	3,658 (10.4%)	104.8%	102.2%	3,813 (10.1%)	104.2%	
純利益	2,416 (6.8%)	109.7%	2,285 (6.5%)	103.8%	94.6%	2,416 (6.4%)	105.7%	
EPS 円/株	220.84		208.92			228.55		

[注] () 内の数字は各々の利益率を表します。
 [注] 「純利益」は「親会社に帰属する当期純利益」です。

As for the outlook for the current Fiscal Year 2019, we expect investment to continue in the areas of aggressive IT investment and IT management. However, as I mentioned earlier, it appears that there is some uncertainty in the manufacturing and automotive sectors, so we must constantly look at the situation.

In particular, the work of the fourth quarter involves the start-up of work that will lead into the next fiscal year, but I am now seeing the work to further solidify the fourth quarter. For this reason, although the first half figures are good, we do not expect the full-year figures to change from the earnings forecasts announced on May 9, 2019. We think that we can do this.

[配当金総額：百万円未満切捨]

- 2019年5月27日に、**配当方針の変更**を実施。
- 2019年11月6日に、**中間配当および期末配当予想の増配**(各34円→36円、各2円増)を発表、年間配当金は72円(4円増)に。

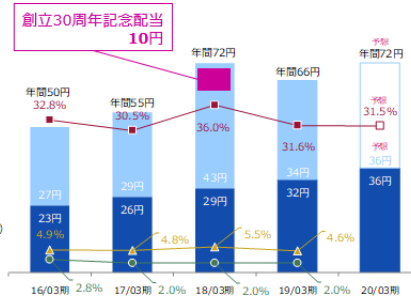
	前回公表 <2019/5/9 予想>	今回公表 19/11/6 予想	増減
中間	34円	36円	2円
期末	34円	36円	2円
年間	68円	72円	4円
配当性向	30.8%	31.5%	0.7%

株主方針

- 当社は株主のみならずに対する利益還元を経営の重要課題と位置づけ、株主資本の充実と長期的な安定収益力を維持するとともに、業績に裏付けられた適正な利益配分を維持することを基本方針としております。
- 特段の株主優待は行っておりません。
- 配当に関しては、原則、**連結経常利益**をもとに、特別損益を差した場合には算出される**親会社に帰属する当期純利益**の30%相当を目途に継続的に実現することを目指してまいります。

	18/03期	19/03期	20/03期	
	実績	実績	実績	19/11/6 予想
中間	※ 29円	32円	36円	36円
期末	43円	34円	36円	2円
年間	72円	66円	72円	6円
配当性向	36.0%	31.6%	31.5%	-0.1%
配当利回り	2.0%	2.0%		
DOE (期末)	5.5%	4.6%		
配当金の総額	781百万円	722百万円		

※2018年3月期の期末配当は、創立30周年記念配当含む



We will talk about a dividend. The dividend policy was changed on May 27 because we want the dividend to be decided in the base of the consolidated figures. Based on this we have made various calculations, then we

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decided to increase the dividend from the interim dividend because we were able to make a considerable profit in the first half of the fiscal year, which was far better than we had anticipated.

Until now, the medium-term dividend forecast has remained largely unchanged and we adjusted the figures and the amount at the end of the final fiscal year. However, we decided to increase the dividend by 2 yen each in the first half and the second half because we were able to make a good profit in the first half.

② 今期の見通し
2.3. 対処すべき課題の対応状況①
連結

※2Qの対応状況は口頭でご説明し、後日、議事録を当社サイトで公開いたします。

1
鉄板品質の提供

1 Q時

- 4月から担当の役員を置いて体制強化。
- 現時点で、グループ会社を含めて大きな不採算プロジェクトはなく、順調に推移。

2
生産性の追求

1 Q時

- クレスコ本体の基幹系システムを、10月末に刷新予定。事務の生産性が向上。
- 開発現場の生産性向上は顧客から求められている。

3
リソース戦略の強化

1 Q時

- ベトナムのオフショア開発は、現地法人化を検討中。
- ベトナムのパートナー会社とは、長期パートナーシップを締結。

4
人材の採用と育成

1 Q時

- 2020年度の新卒採用は、本体は予定通りに完了し、子会社は終盤。
- 今年度4月入社の新人70名は、6月末で集合研修が終わり、7月から現場に配属。

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I will explain a little bit of this verbally. There are 11 issues that we have identified as issues for our company and group in this fiscal year. During the first quarter fiscal briefing, I talked about this and I'll update a bit.

First, regarding the provision of quality-based steel plates, as I mentioned earlier it is at the end of the second quarter, which is at the end of September, losses for the projects in the parent company and another subsidiary were expected. Since there was a prospect of a loss occurring in the second half after October, the losses of 60 million were allocated. Accordingly, the allowance for losses of 60 million was accounted for in the first half of the fiscal year under review.

Thereafter, these two projects are currently operating under these assumptions. However, in a somewhat harsh environment, the project itself will be in a difficult situation. Compared to last year, which there were more than 100 million losses from the projects, it is still manageable in this year.

Second issue is the pursuit of productivity. In pursuit of productivity, the mission-critical systems of CRESCO LTD. have been fully operational since October 1. The monthly settlement of accounts for October has been made once. This is a new change and we are still learning. However, we expect to steadily increase the productivity of our clerical work in the future and we will be expanding this system to our business companies as well.

The third issue is the resource strategy. As I mentioned in the first quarter, we have established a local subsidiary in Vietnam on October 1. In terms of near shores in Hokkaido and Kyushu, the situation is that they are also quite active and the number of jobs has increased considerably as a result of expanding project rooms.

The next issue is recruiting and training of personnel. As for the recruitment of new graduates, we have been able to hire for April of next year, 2020. However, the recruitment of mid-career employees has been

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somewhat difficult. Because of the current shortage of personnel, it is not easy to hire staffs. Since the number of recruiting targets has not been achieved or has not yet been achieved, we are talking about spending a little more money on mid-career recruitment. As you know, it is probably true that GAF A and other consulting companies are trying to fight for recruiting people.

② 今期の見通し
2.3. 対処すべき課題の対応状況②
連結

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5
新技術の研究・開発

1Q時 • AIに関する特許をアメリカで取得したことを、7月24日にリリース済み。

6
グループ連携の強化

1Q時 • 子会社アイオスが同社子会社イーテクノを10月1日に統合することを、7月22日にリリース済み。
アイオスの人材の補充と、事業領域の拡大が目的。統合により300名規模に。

7
営業体制およびお客様とのリレーションシップの強化

1Q時 • 100名越え体制を年間契約する包括契約を、4月に1社、6月に1社締結。
受注残高に影響。

8
新規ビジネスの組成

1Q時 • 2018年10月からセミナービジネスを開始。内容はDX等。
70~80名の集客があり、営業の顧客開拓に期待。

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The fifth issue is the research and development of new technologies. It is the AI that we are now putting all our efforts into. Regarding AI, we are making an appeal to the public by presenting papers at academic conferences, giving lectures at academic conferences, and posting interview articles as publicity. We have received a variety of business inquiries; however, in terms of monetary value, we have not achieved large figures yet.

We are convinced that AI will become more widespread in the future. We have been doing the evangelism activities such as announcing to the public about our AI activities including to train the staff.

Regarding the sixth issue, strengthening of Group collaboration, as I mentioned at the previous first quarter briefing, the integration of ARS Corporation Ltd. and e-techno.Co.,Ltd was completed on October 1.

The seventh issue is strengthening our sales system and relationships with our customers. There is no further comment on this today.

Regarding the establishment of new businesses, we are now working to increase sales of solutions, not just development work within the Company. There is something to say about whether this is new. In the second quarter, we announced two services.

First is the Creage Account Plus, which is the cloud for AWS and Amazon. We have been handling this since 2012 and we now have more than 100 engineers. We have announced the new services which making Creage Account Plus as a serviced menu for a variety of customers making contracts with Amazon.

The next one is a security diagnosis services. I think other companies in the same industry are also doing this, making a diagnosis of the net to ensure the safety of the net. We have developed a net security diagnose service and announced it. For this service, we use the external services.

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9 コーポレートガバナンスの推進

- 1Q時
- 子会社で、ガバナンスやセキュリティに関するインシデントが発生。注意喚起の継続が必要。

10 健康管理と働き方改革の推進

- 1Q時
- 月2回、保健師による健康相談を実施。
 - ライザップ社による健康セミナーを、今年から年1回開催していく。

11 ダイバーシティへの取り組み

- 1Q時
- 女性役員は未だ誕生していないが、今年はじめて、事業部長級に女性が昇格。部長級の女性は4名在席。

The ninth is the promotion of corporate governance. I have nothing to update today.

The tenth issue is the promotion of health management and work style reforms. Recently, there is a guidance to clearly declare the Company's efforts for employee's health management from the Ministry of Economy, Trade and Industry. We announced our overview on the website at the end of September. We have published two A4 papers, which include various work style reforms, talks about overtime work and the use of paid work, medical checkups, and various other initiatives.

As our General Affairs Department says that there is a certified level for the guideline, I would like to add more to reach that point. I don't know how far this can be done; however, this is the current trend in the world and we have made this Health Management Declaration in September.

Regarding our effort toward diversity, I would like to introduce our activity called platinum Kulumin which our company got certified. This diversity initiative has originally started in September. The Ministry of Health, Labour and Welfare certify the organizations which are working hard on giving a high degree of support for raising children employees not only giving women a childcare leave but also giving men a childcare leave as platinum Kulumin. The standard which the Ministry of Health, Labour and Welfare certifies the organizations as Kulumin is based on the percentage of employees' acquiring childcare leave and so on.

That is all from me. We will proceed to go to a question and answer session.

Moderator: Thank you for the briefing.

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Question & Answer

Moderator: Now we proceed to a question and answer session. Please don't hesitate to ask us any questions. Please raise your hand, I will bring a microphone.

Participant: I have two questions. The first one is about car electronics. In the first half of the fiscal year, it increased 22% remarkably. Currently, car electronics consists of ADAS and conventional car electronics. The ADAS has grown and the number of conventional car electronics is now decreasing due to the number of cars is decreasing slightly. In your company, what is the percentage of ADAS? Is it big?

Nemoto: ADAS is autonomous driving. ADAS includes the autonomous driving, this is not all it includes though. I think Adas is about 10% to 20% of the total amount of car electronics.

Participant: President said car electronics will probably remain flat. The reason is why I mentioned earlier, isn't it?

Nemoto: Yes, it is.

Participant: Is it because the number of cars is decreasing?

Second question about DX. This is not a short-term story, but a little longer-term. I don't know how it is progressing even if there is a digital transformation. For your company, will it become a big service business in the future?

Nemoto: In the service business, as I mentioned earlier, the service business will be the one that develops AWS. However, we believe that our mainstay in DX will also be commissioned development.

Participant: I don't really know about it. When it comes to Amazon online, the mainstream is packaged software. There seems no need to develop. What do you think about it?

Nemoto: Amazon or Google is really a platform. After all, what customers want to do must be on that platform. Since customers have defined a different development method, such as agile, in many ways, as DX we will provide Amazon platforms for our businesses, for example. That's also a business. Monthly money comes in. Operational monitoring and such services are carried out within the Creage account plus. It is also a business to build applications on commissioned services together with customers. It is also a business to maintain and expand these applications. That's why DX has a variety of business formats.

Participant: Considering it a little, it becomes a stock business as well, doesn't it?

Nemoto: Yes, it does.

Participant: It sounds like you're developing with options on top of your stock business.

Nemoto: Yes. Since development occurs to a certain extent, it doesn't mean there is no development because it was done using Amazon, Google, or Salesforce. It is small though. For example, there are many projects that can be developed by 10 or 20 people, even though they may not be as large as a truly bank backbone system.

Participant: There are a little fewer books, compared to banks, aren't there?

Nemoto: Yes. That's right.

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Participant: Thank you.

Moderator: Thanks for your question. Let's move on to the next question. Please raise your hand. Please do not hesitate.

Participant: I apologize for the simple questions. It would be helpful if you could tell me the factors that have deviated more than planned in the first half?

In addition, I think that there was a valuation loss on derivatives at the time of the first quarter, which put downward pressure on profits from the operating stage. This time, I feel that the loss has become invisible. I would like to know whether the gains and losses on derivatives have improved or whether they have absorbed a considerable upside since the operating stage.

Nemoto: Okay. I believe that the biggest factor behind the favorable performance in the first half of the fiscal year had the increase in the top line. This means 12%.

Even for the parent company and its subsidiary companies, there was a sense that a large project was like a special demand and I think that this was a factor behind the growth in profits. That's why we were able to take on new challenges in the absence of people as orders were quite favorable. That is the answer to the first question.

Second, I would like to talk about gains and losses on derivatives. The answer is that there are two types of gains and losses on derivatives, which have been on an improving trend, but have not been completely improved. The definite thing is now on the lower side of net income. As a result, we are now able to see more than ordinary profit. The answer; therefore, is that the stock price is rising, so the whole is improving. However, if we were to say that we have made a complete improvement, the current net income is still 105 compared to the same period of the previous year, so the answer is that it has not yet fully recovered. Is it clear for you?

Participant: I understand it very clearly.

Moderator: Do you have any other questions?

Participant: I would like to ask you a little bit about the development personnel. You said that from the beginning, there has been a shortage of development personnel. You are trying to recruit new graduates and mid-career personnel as well as offshore and nearshore recruitment. For example, the number of employees currently stands at 2,000. Roughly speaking, how many development personnel do you have? Can you disclose the number?

Nemoto: Approximately 90% are engineers and development personnel.

Participant: 90%?

Nemoto: Yes, it is.

Participant: Okay. Then, from a different viewpoint, in your company, there are two broad divisions between software and embedded. Which staff shortage is noticeable?

Nemoto: Until last year, it was incorporated. As I mentioned earlier, the situation in the manufacturing industry has become a little more difficult. Now, as there is a question about software earlier, in the area of new technologies such as DX projects, there is a shortage of such members even though we are continuing to cultivate such engineers through technological change.

Participant: Thank you.

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One more thing. From a slightly different point of view, it means that there will be a considerable shortage of software in the new technologies. Because 90% of the development staff are from this sales scale, can you deviate significantly from this sales scale even if the ratio of development staff is roughly the same as the sales scale? Do you deviate?

For example, sales of this software are 13.9 billion yen. The embedded one is 3.5 billion yen. Roughly in proportion. That's about four to one.

Nemoto: It is correct roughly in proportion. Of course, it also includes service sales that are not involved with people, so although there are some that are not involved with people, it is generally acceptable for people to see it as being proportional to sales.

Participant: Apologies for asking again. About the DX, the new technology, it is related to most industries. I understand that the development of this software is divided into finance, public services, distribution, and others in your company. Does it mean that there are not enough of personnel in each field?

Nemoto: Yes, not enough.

Participant: Thank you.

Nemoto: We are focusing on cloud and Amazon. You will in other words, stop owning and use your computers yourself. You will use a computer power in a cloud, which trend has been increasing for about three years. Therefore, the job at all is still about to be done in all industries. After all, considering the issue of costs, it is probably better to include customers. Therefore, the number of such jobs is increasing with tremendous momentum.

Participant: Thank you.

Moderator: Thanks for your inquiry. What is your other question? Are you okay?

Since there seem to be no more questions, I would like to conclude the financial briefing. Thank you very much for your detailed briefing.

Nemoto: Thank you.

Moderator: Please fill out the questionnaire.

[END]

Document Notes

1. Portions of the document where the audio is unclear are marked as follows: [Inaudible].
2. This document has been translated by SCRIPTS Asia.

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