

November 15, 2021

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(Code number: 5070, Mothers market of the Tokyo Stock Exchange)

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Supplementary explanation regarding consolidated financial results for the first nine months of the fiscal year ending December 31, 2021

DRAFT Inc. has received questions from investors regarding the consolidated financial results for the first nine months of the fiscal year ending December 31, 2021 (explanation of business results as well as explanation of consolidated financial results forecast and other forward-looking information) released on November 11, 2021. In response, we have provided a supplementary explanation as below.

1. Full-year net sales forecast

(1) Outlook for the fourth quarter (October–December 2021)

Because the previous fiscal year was an irregular nine-month period from April to December 2020, we were not able to make an accurate year-on-year comparison between financial results of the previous fiscal year and the current period under review. For reference, however, net sales in the nine months ended September 2021 were down 7.8% compared with the same nine-month period of January–September 2020, and net sales in the third quarter (July–September 2021) were down 19.5% versus the three-month period of July–September 2020. There was a concern among investors regarding whether the full-year net sales target of ¥8,300 million could be achieved, considering net sales were ¥1,611 million in October–December 2020. However, we expect a substantial increase in net sales in the fourth quarter of the fiscal year under review (October–December 2021) versus the October–December 2020 period.

(2) Project stock

In the medium-term management plan (overview of business plan and growth potential) disclosed on October 29, 2021, the DRAFT Group has used its stock of projects as an indicator for formulating

the full-year performance forecast.

Project stock is the sum of order backlogs (Note 1) of projects scheduled to be completed and delivered to clients during the fiscal year under review and expected orders (Note 2). As of September 30, 2021, the project stock was in the range of ¥2,900 million to ¥3,300 million (Note 3). We decided to maintain our full-year net sales forecast released on May 13, 2021, taking into account the status of the project stock and orders expected in October and later (October–December 2021).

(Note 1) Order backlogs include only those projects for which contracts and other documents to confirm the receipt of orders exist, and do not include those that cannot be backed by these documents, for the purpose of reporting in the annual securities report. Because the time required for concluding a contract varies depending on the situation of the client and details of each project, it may be difficult to predict future business conditions based on year-on-year comparisons of order backlogs.

(Note 2) Expected orders are obtained by multiplying all prospective projects by the Group's close rate. These include projects for which contracts have not yet been signed (but informally agreed upon) and those waiting for competition results.

(Note 3) The close rate is calculated based on historical data, but because the project stock includes projects for which contracts have not yet been formally signed, every year there are some projects whose completion timing gets pushed out to the next term. The project stock ranges from the lower bound of ¥2,900 million, estimated using only those projects highly likely to be completed and booked as sales within the fiscal year, to the upper bound of ¥3,300 million, which, in addition to the backlog of confirmed orders, takes into account projects whose completion timing may be delayed to the next fiscal term and orders expected by the end of the fiscal year.

(3) Seasonal variations

The Group books sales after services have been provided to the client, i.e., when projects have been completed and delivered to the client. Hence, the timing of sales booking depends on clients' schedule and plan.

The Group's annual net sales had followed a certain cycle up until the COVID-19 outbreak, with higher net sales often booked in quarters including March or September. However, since the outbreak, this cycle has been disrupted, making it difficult to predict full-year performance based on comparisons with the previous year's results.

The Group's full-year net sales forecast for the fiscal year under review is estimated based on the abovementioned project stock (sum of order backlogs and expected orders). Taking into consideration changes in seasonal variations and order status, we expect a substantial increase in net sales in the fourth quarter of the fiscal year under review versus the October–December 2020 period.

2. Operating profit and ordinary profit

The Group budgets SG&A expenses so that the full-year ordinary profit will be around 8–9% of full-year net sales. However, due to the COVID-19 pandemic, expenses (advertising expenses and activities [travel and transportation] expenses) came in below plan particularly in the first half of the fiscal year under review (January–June 2021), resulting in operating profit and ordinary profit substantially exceeding the forecast (Note).

Of the expenses curtailed in the first half of the fiscal year under review, advertising expenses and expenses for implementing new initiatives in particular have been carried over to the second half of the fiscal year (July 2021 and later). As a result, SG&A expenses in the July–December 2021 period are expected to be much higher than those in the same six-month periods of previous years. In the third quarter of the fiscal year under review (July–September 2021), operating profit was down 76.5% compared with the same three-month period last year (July–September 2020), and ordinary profit was down 77.4%. These declines were due to changes in the booking of net sales compared with pre-pandemic years and the delay in timing of SG&A spending. We believe we can secure a reasonable level of operating profit and ordinary profit for the full year.

(Note) For details, please see the “Notice regarding the difference between performance forecast and actual results” (Japanese only) disclosed on August 12, 2021.