Neural Pocket

Neural Pocket Inc.

FY2021Q2 Financial Results Briefing Meeting

August 16, 2021

Presentation

Moderator: Thank you very much for taking time out of your busy schedule today to participate in Neural Pocket Inc.'s financial results briefing for Q2 of the fiscal year ending December 2021.
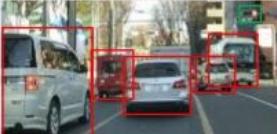
Today, we will make a presentation using the financial results presentation materials disclosed on our IR website on August 13.

Now, let me explain today's flow. First, Mr. Shigematsu, Chief Executive Officer, will give a 30-minute presentation on business overview and performance. After that, we will have a question-and-answer session until 1:00 PM, at most. Both Mr. Shigematsu, Chief Executive Officer, and Mr. Tane, Director, Chief Financial Officer, will answer your questions.

Thank you for your patience. Chief Executive Officer Shigematsu will now give an overview of our business and performance. Then, I will hand over to the CEO.

Shigematsu: Thank you for joining us today despite your busy schedule. We have just announced the financial results for H1 of our fourth fiscal year, and I would like to explain the details.

First of all, since there are many new participants, I would like to give a brief business overview.

We are an AI engineering company that uses deep learning, and we are developing a lot of such analysis centered on AI images and videos, and we detect various images with AI. There are about 30 to 40 types, and by developing various algorithms independently, we are creating new services that other companies aren't providing.

Neural Pocket aims to digitize real spaces and solve social issues by bringing AI cameras to the world.

We are calling this the AI Smart City Revolution. There are very few companies in the world that are doing this, and we are promoting our business with the goal of being a pioneer in this area.

A vast, entirely new Smart City market is being created

Global Smart City market size is approx. $1-2 trillion USD

Research Company / Report Name	Global Market Size
Allied Market Research Smart Cities Market by Functional Area : Global Opportunity Analysis and Industry Forecast, 2018 – 2025	In 2025 **2.4T USD**
Mordor Intelligence Smart Cities Market - Growth, Trends, and Forecast (2020 - 2025)	In 2025 **1.7T USD**
IMARC Smart Cities Market: Global Industry Trends, Share, Size, Growth, Opportunity and Forecast 2020-2025	In 2025 **1.0T USD**
Markets And Markets Smart Cities Market by Smart Transportation, Smart Buildings, Smart Utilities, Smart Citizen Services - Global Forecast to 2023	In 2023 **0.7T USD**

Asia is the source of growth for smart cities

Smart City Market Growth Rate by Region (2019-2024)
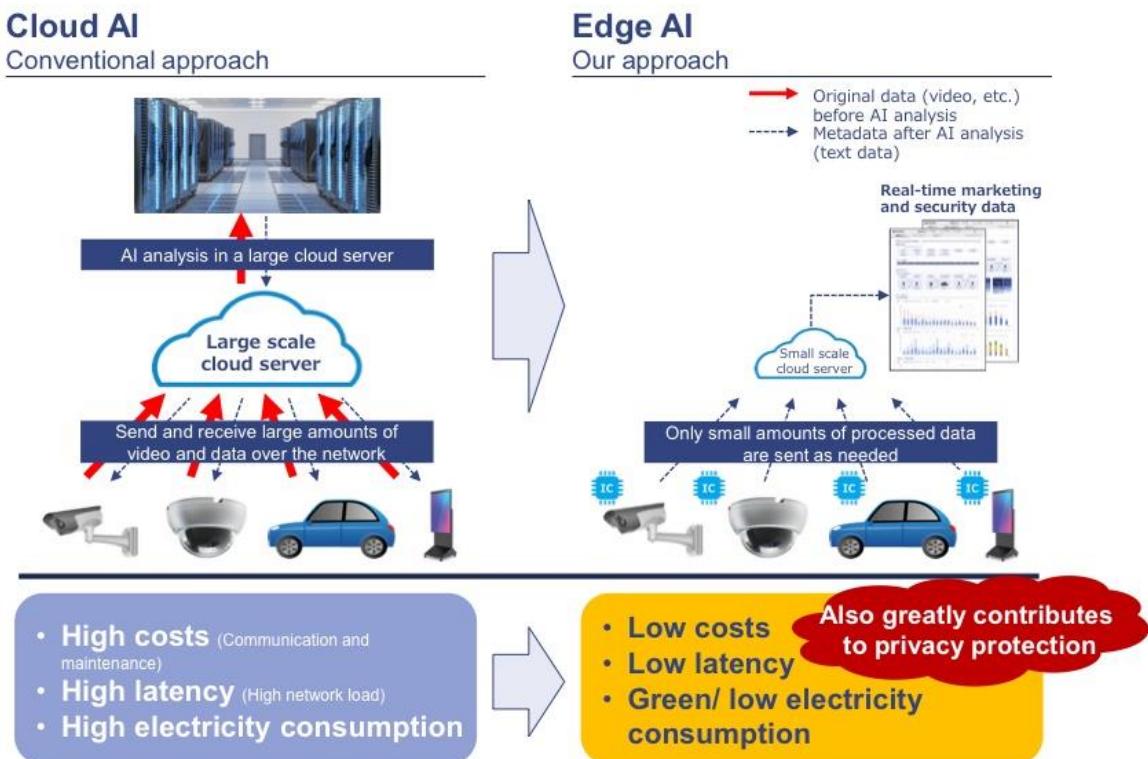
Growth rate
- High
- Medium
- Low

Source: Mordor Intelligence

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The reason why we are applying AI to smart cities is because of the overwhelming size of the market and the high expectations. There is also a huge social need for such AI.

Edge AI is a technology that overcomes many of the problems traditional Cloud AI faces

One of the overwhelming strengths of our company is that we conduct deep learning processing at the edge, and not in the Cloud.

As for Cloud AI, you would take images and send them to a server via the Internet, they are processed in a cloud server, and then sent back via the communication network for feedback.

However, there are several problems, and the reason why deep learning technology has not spread to the world is the high cost of using AI in the Cloud, including communication costs and maintenance costs. In addition, the delay in sending images over the network cannot be ignored, and the high-power consumption have been issues.
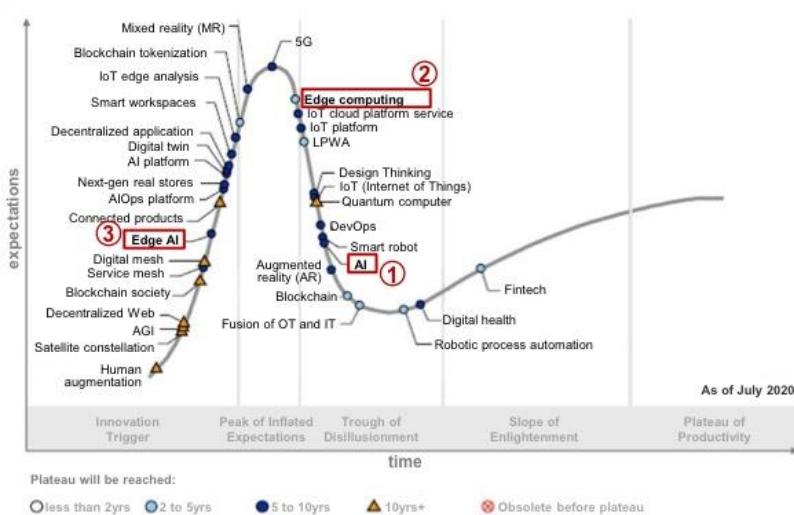
Our company has always been in the business of solving all of these issues, in the area of Edge AI. What "edge" means is a device located at the edge of the network, where chips that process AI are installed in devices such as cameras and cars. In this way, the moment a video is captured, AI is processed in the terminal, and only the metadata and value-added information will be sent to the server, where it can be immediately used for marketing and security purposes.

The advantage of this is that it will greatly reduce the load on the network. Cost can be reduced by reducing server room investment, and also since the AI is instantly processed on the terminal side, the delay can be minimized to about 3/1,000 of a second, resulting in low latency.

The other thing is that it's environmentally friendly, and the most important point is that we don't have to share images that contain personal information to the network. We can protect privacy by sending only value-added information necessary for anonymized marketing or security to the Cloud.

Technological evolution of AI and the positioning of "Edge AI"

Technology trend by Gartner[*1]

Mixed reality (MR)
Blockchain tokenization
IoT edge analysis
Smart workspaces
5G
② Edge computing
IoT cloud platform service
IoT platform
LPWA
Decentralized application
Digital twin
AI platform
Next-gen real stores
AIOps platform
Connected products
Design Thinking
IoT (Internet of Things)
Quantum computer
DevOps
Smart robot
③ Edge AI
Digital mesh
Service mesh
Augmented reality (AR)
AI ①
Blockchain society
Blockchain
Fintech
Decentralized Web
AGI
Fusion of OT and IT
Digital health
Satellite constellation
Robotic process automation
Human augmentation

As of July 2020

expectations

Innovation Trigger | Peak of Inflated Expectations | Trough of Disillusionment | Slope of Enlightenment | Plateau of Productivity

time

Plateau will be reached:
○ less than 2yrs ◐ 2 to 5yrs ● 5 to 10yrs △ 10yrs+ ⊗ Obsolete before plateau

AI technology evolution and the implications for Neural Pocket

① Since the development of deep learning in 2012, AI has continued to evolve and the **evolution of the technology has eased**

② The **generalization of edge computing** has progressed through technological innovation by NVIDIA and other edge device manufacturers

③ On the other hand, there are only a few companies globally that have the ability to develop **compact, high-quality AI** that can be installed on edge devices, making **"Edge AI" an area ripe for innovation where first-mover advantage can still be captured**

*1 Gartner regularly publishes the above emerging technology hype cycle schematic. Web URL: https://www.gartner.co.jp/ja/newsroom/press-releases/pr-20200910

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I would like to share the technology cycle curve published from Gartner which captures where Edge AI stands today.

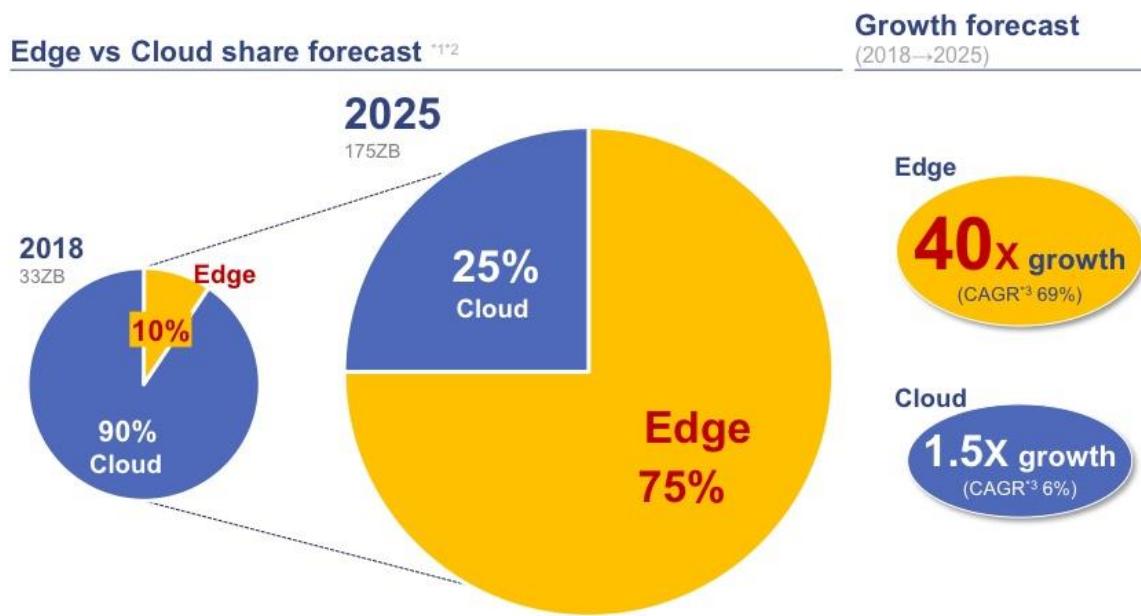Deep learning, or AI, as described under number 1, has been making progress since 2012.

As you know, there is no company that has achieved the digitization of information in the city using artificial intelligence and so-called deep learning. I have always mentioned SenseTime, which is a Chinese company, but other than this company, it has been difficult to see any other companies, including those from the US. 1 of the reasons is that artificial intelligence is in a period of disillusionment.

On the other hand, there has been this technological innovation called "edge computing," and as you can see in number 2, a number of companies which produce graphics boards that can manufacture edge computers, such as NVIDIA and Intel, has emerged. Then, the technology to process AI on top of that graphics board, inside the device, came out in about 2017 to 2018.

It's about [2017], and the edge is expanding, and the biggest market concern right now, especially on the technology side, is companies that are putting AI on the edge. This is very few.

Edge AI, which is described as Innovation Trigger, has been the most studied area in the field of AI. At the moment, there is no company in the world that is ahead of us in terms of edge, and although we are taking the lead in Japan, we believe that we will benefit greatly from expanding this leadership from Japan to overseas.

A major macro transition from the Cloud to the Edge is in progress

Edge vs Cloud share forecast [*1*2]

Growth forecast (2018→2025)

2025
175ZB

2018
33ZB

Edge
10%

90%
Cloud

25%
Cloud

Edge
75%

Edge
40X growth
(CAGR[*3] 69%)

Cloud
1.5X growth
(CAGR[*3] 6%)

- As data volumes explode, processing data in the cloud becomes more and more inefficient
- In response, computer power is being rapidly pushed from the Cloud onto the Edge

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In fact, if you look at the edge area over a few years from 2018 to 2025, according to Gartner IDC, the data processed on the edge was about 10% of the total data volume a few years ago.

The reason for such a small number is that, in addition to the main restrictions on the devices at the edge, when the equipment is restricted, the number of companies that have developed AI programs or data analysis programs to process the data on the devices has been very limited.

It will be about 40 times by 2025. The annual growth rate is also expected to increase by about 70%. Our company's sales have been growing at an annual rate of about 70%, and we are currently growing in line with the growth of the market, but I think we will need to grow significantly in the future.

Neural Pocket's unique strengths in the Edge AI space

Develop and possess ultra-lightweight AI that is 1/10th the size of general AI through the usage of proprietary AI logic
(A single edge device can be equipped with multiple AI programs)

Involved in defining requirements for domestic and international edge AI devices
(Utilize specialized equipment with optimal specs to run our edge AI)

Possess abundant and diverse training data of people, cars, etc. enabling high AI quality
(Can provide proprietary packaged solutions vs conducting a demonstration experiment using customer data)

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The competition in the field of Edge AI is about to intensify, but let me explain why Neural Pocket has been ahead in the field of Edge AI so far.

There are 3 reasons I would like to introduce here.

First, AI is not placed on the edge because the AI that was normally processed in the Cloud room was created without considering the limitations of the computer hardware. This means that everything is added, and the size of the program is large. Then, if they try to put it on the edge, they can't put software on it. It's over capacity.

Our AI, however, has developed its own logic, and we are able to produce the same or even better quality of that AI at 1/10 the size.

It's the same with games. If you have only 3 games on a single piece of hardware, or if you have 30 games, you can enjoy a variety of games if you have 30 games. For example, compared to an Edge AI that can only detect a person's skeleton in the same AI camera analysis, for example, we have 10 of them. It can detect skeletal structure, clothing, face recognition, crime prevention, movement, group detection, walking speed, car detection, type of car number, et cetera. The overwhelming strength is that various things can be processed on the edge with such a single device.

Secondly, we have been involved in defining the requirements for edge devices for many companies in Japan and overseas. The reason why Neural Pocket AI is placed on the edge is not only that it is placed in a compact form as I mentioned above, but also that the hardware is designed according to our specifications, and we are actively involved in creating industry standards.

Thirdly, it is also very important to have our own learning data. Until now, the mainstream of AI companies has been to develop anything if a customer requests a project, and such AI companies receive the customer's data.

However, since we have our own learning data, we can work together with our customers to develop so-called experiments in deep learning. However, because we have all our own training data, we do not work with our customers on development as a so-called experiment of deep learning, but instead, even if they are not aware that they are using deep learning when they install. For example, a parking lot occupancy solution, a call center solution, or people flow analysis, they can just install it as a package.

The point was that it was easy to spread the so-called installation.
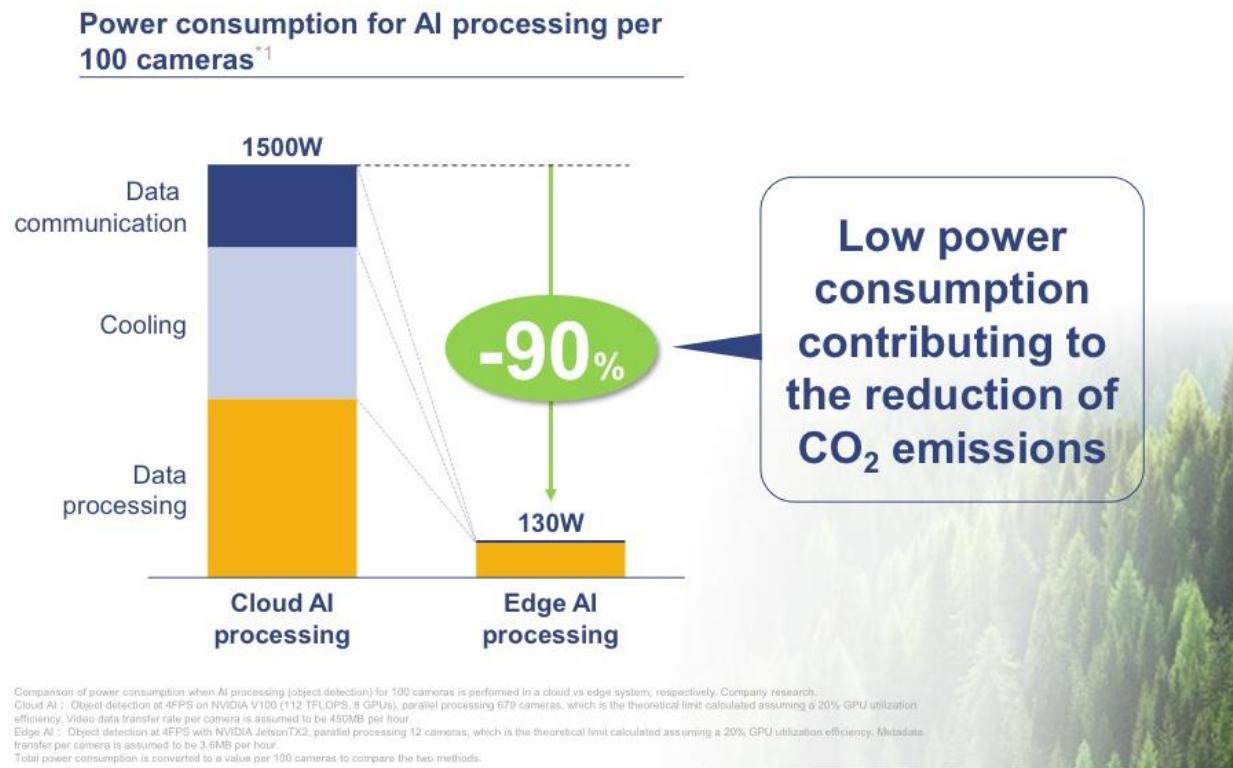
I will skip here, but as I mentioned in the last financial results briefing, the power consumption of the edge system is reduced by about 90% compared to the server system.

This is a very simple mechanism that does not require a server or communication. The amount of AI processing that goes through networks and servers is greatly reduced, which reduces power consumption.

We provide 5 unique packaged smart city-related AI services that capture large cross-industry general needs

People flow, crime prevention — **DigiFlow**

Parking and Mobility[*1] — **DigiPark** — Powered by Smart-Kun

Signage Advertisements — **SIGN DIGI**

WFH security — **RemoDesk**

Fashion Analysis — **AI MD®**

*1. 3D City Map related services such as "Smart-kun" are included within Parking and Mobility

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We have been explaining in our financial results briefing that we have a variety of technologies, but the major progress in H1 of this fiscal year is that we have packaged our services.

We are very confident in this area, and now that we have completed the packaging of the 5 major services, sales of these products are expanding.

The first is a people flow and crime prevention called DigiFlow. We have a lot of experience in this area.

In addition to those announced in our past financial results briefing, we also have DigiPark. This is an innovative parking solution that breaks away from the conventional pattern of flapper gates and sensors embedded in the basement and allows you to view all the availability information with just 1 camera.

In addition, we have been doing signage advertising, which is called SIGN DIGI, for 3 years now, and have been introducing it for a long time.

RemoDesk is a service that we started this year, and now we've launched the SaaS version, so I think telecommuting support will accelerate in the future. First of all, we are currently selling this to call centers, but from now on, it is a solution that has a wide range of expansion, considering the so-called general home-based work other than call centers and the use in virtual offices in general.

Fashion analysis AI MD, which we have been working on since our establishment, is expanding steadily.

Our business model

	Contracted Development (AI delivery)	Licensing Revenues	Co-Business Development
Business model description	• Develop solutions based on customer requirements • Submission of software, including intellectual property • Need to continuously propose and receive orders for new projects	• Providing solutions through a subscription model • Number of new contracts, average licensing price, and retention rates are measures of business growth	• Share sales by developing medium-to-long term, large-scale businesses jointly with multiple companies • Leverage the strengths of each company's different assets to create synergies
Our services	-	DigiFlow DigiPark RemoDesk AiMD	SIGN DIGI
Value provided by AI companies As a result, the durability and scale of sales	Low	Mid - High	High

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I will introduce it again in our business model, but as I mentioned earlier, it is not about developing and delivering orders, but mainly license income.

Basically, we receive income from customers who install our packages and use them on a continuous basis.

Business highlights for the FY2021 Q2

1. **Released commercial packaged offerings as planned**
   - **RemoDesk** SaaS version launched to allow for the usage by smaller accounts, whilst new functions were developed
   - **DigiPark** In addition to the monitoring of occupancy of flat parking lots, new functions such as indoor parking and license plate recognition were released
   - **SIGNDIGI** Offering a unique standalone device that can be installed immediately from a single device

2. **Progress towards unit-based sales with expansion of services across commercial customers and governments**
   - Further deepened relationships with major developers, logistics companies, SoftBank Corp., METI[1], and MIC[2].
   - Scheduled to appear in SoftBank World 2021, and activities for further external communication are underway.

3. **Improved hardware and software packaging and testing environment for commercial scaling**
   - **"Cataloged" products capturing cross-industry general-purpose needs:** Previously, services were typically installed individually depending on customer/ location requirements. Now, AI services are being catalogued, allowing for simplified installation and reduction in lead time and costs.
   - **"Packaging" services with improved quality assurance:** Rigorous selection of cameras, edge boxes, and software libraries has optimized cost and performance of AI implementation and can now be offered as a packaged service. In addition, in order to conduct comprehensive quality control of such services, "AI Test Field," has been established to conduct quality verification with integrated hardware and software.

4. **Although sales are expected to be concentrated in Q4, the business is progressing in line with the business plan for FY2021. Packaging of services is progressing.**

Secondly, I would like to introduce our business progress in Q2. As I mentioned at the beginning of this presentation, I would like to highlight 4 things.

First, we were able to release commercial package offerings as planned.

Second, the installation of the system has progressed considerably, and we feel that we are making good progress in this business in FY2021. I think the balance between government and private sectors is getting better.

As for the private sector, in addition to SoftBank, our largest customer, we have a very wide range of relationships with major developers, and in addition to that, logistics companies and commercial facilities have been installing the system.

Third, while we have been packaging the hardware and software for commercialization, we have been preparing the test environment for it.

As I have already said, we would like to disclose the unit base, or KPI, somewhere in the next year. This year's theme is not to receive so-called AI as this fee base from customers, but to expand it by linking it to the number of installed units, dividing it into the number of installed units and the unit price.

Toward that end, although the package itself has not been used by any AI company in terms of quality and robustness of installation, we determined to take responsibility there and have established a research facility, AI test field, experimental facility, quality experiment guarantee, and experimental system base. I believe that this is a very advanced attempt for an AI company.

I think it was our remarkable progress in order to work hard to achieve this kind of scale in the future as an AI company.

In terms of sales, there was a slight shift in sales in Q2 to Q4, but we believe that 2021 will be very smooth. In the short term, we are experiencing some volatility in the stock price, but I think it is important for us to continue to firmly promote our business.

Let me give you a brief introduction.

This is RemoDesk, which was announced for the summer of 2021, but it is a SaaS version. We have introduced a system that allows users to use the RemoDesk by logging in on their Internet browser.

The adoption of this technology is now spreading, and we are planning to make press releases and other announcements at appropriate times.

Secondly, we have been working on this digital signage for some time now, but now that we have established it as a service package, it is being introduced more widely.
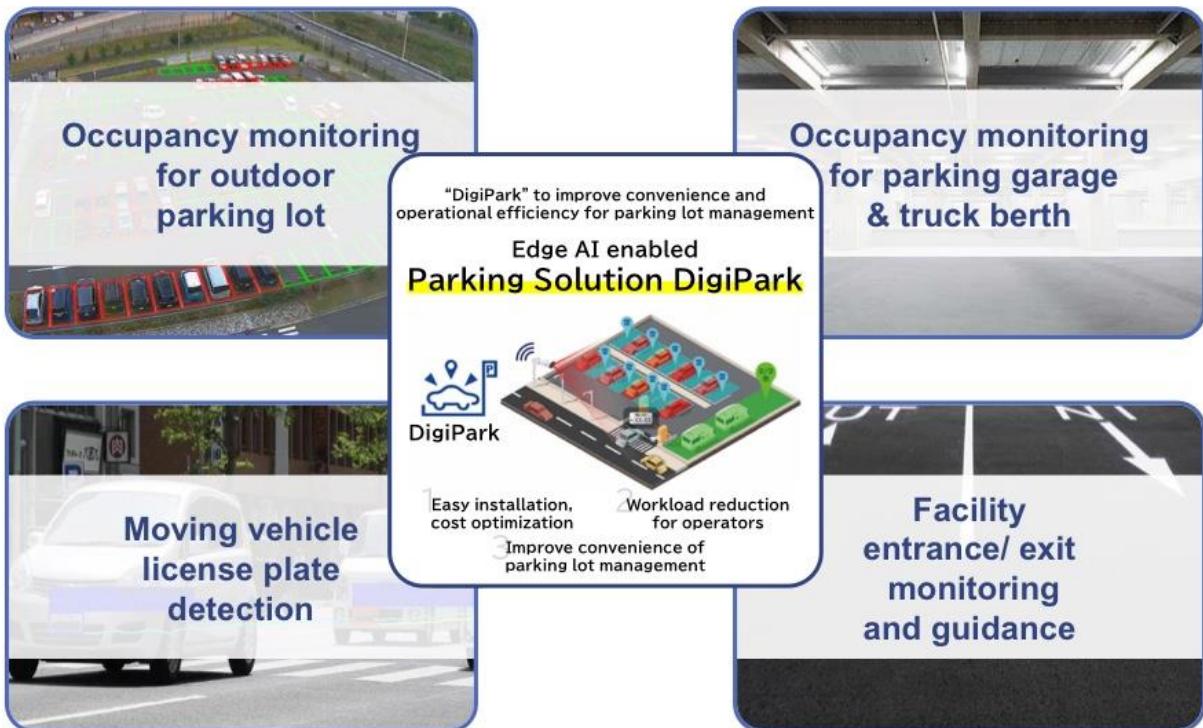
As for the DigiPark, we have been able to visualize the package to some extent since the beginning of this year and have been expanding it.
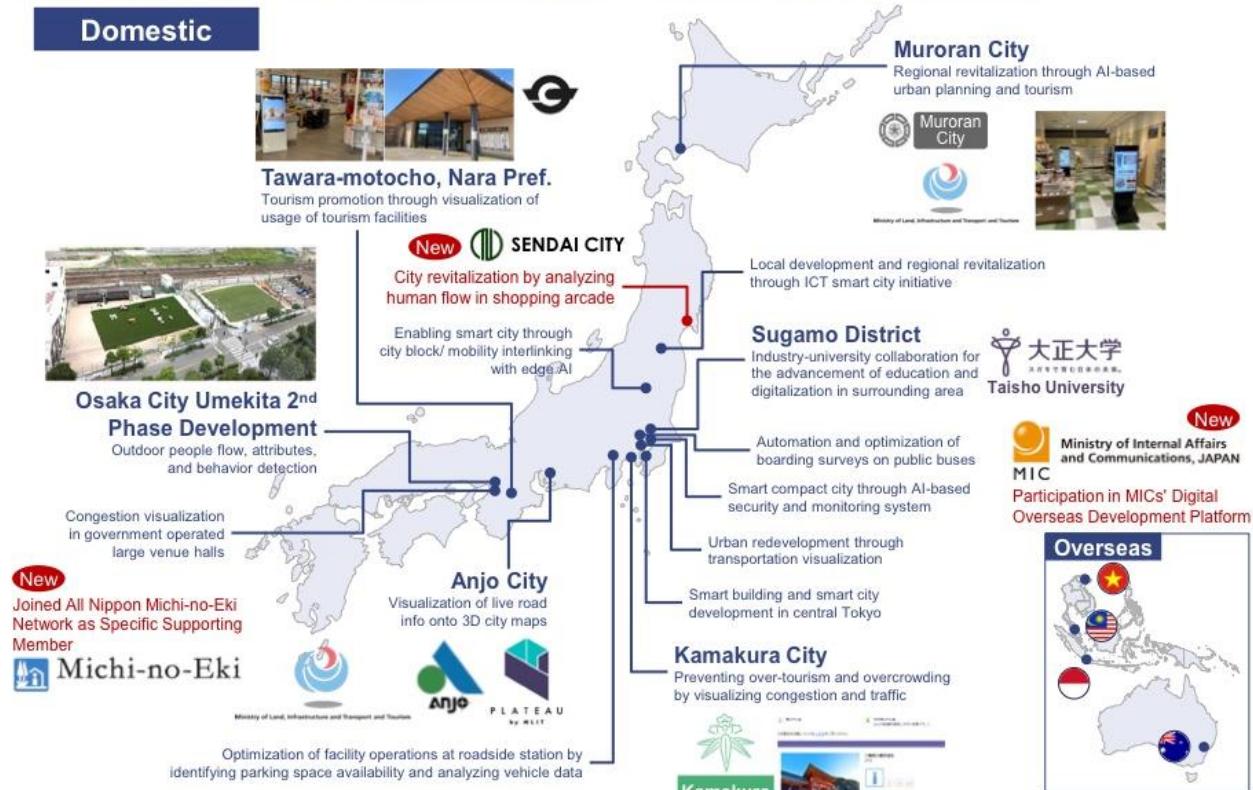
We have already released a number of IR projects in this area, but this has also been expanding in the private sector and the government.

This is an area that we will focus on in H2 of the fiscal year.

This is a visualization of the overall status of the introduction of the system for the government, and I think it has expanded considerably throughout Japan.

In Q1 and Q2, rather than increasing the number of new locations, we were trying to expand the services within those locations, such as introducing parking lots to municipalities that had introduced the so-called people flow system.

Thus, in line with our packaging strategy, we have been introducing various types of packages rather than increasing the number. However, in H2 of the fiscal year, we would like to increase that area and the number of introductions to some extent.

This is a case study of Sendai City.

Neural Pocket

Service development domestic and overseas through deepening cooperation with various government agencies

Ministry of Internal Affairs and Communications, JAPAN
MIC

Japan Platform for Driving Digital Development: JPD3

Ministry of Land, Infrastructure, Transport and Tourism

Michi-no-Eki

- **The Ministry of Internal Affairs and Communications (MIC) established the "JPD3[1]"** as a framework for public-private cooperation **promoting overseas projects**

- As an initial member of JPD3, we will **accelerate overseas development,** mainly in Southeast Asia, through **public-private partnerships in collaboration with the government**

- There are **1,154 roadside stations nationwide** (cumulatively +200 million annual visitors) under the jurisdiction of the Ministry of LITT

- We have been contributing to **regional revitalization by introducing the latest AI technology** to roadside stations

- With our **new participation as a specific supporting member,** we will continue to contribute to "regional revitalization" and "enhancement of disaster countermeasures"

[1] Japan Platform for Driving Digital Development: JPD3 webpage: https://jpd3.jp/about/

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The Ministry of Internal Affairs and Communications and the Ministry of Land, Infrastructure, Transport, and Tourism have been working on the overseas development, and although the number of infected people with the coronavirus has been increasing, I think it is time for companies to move forward, taking the overseas coronavirus passport into account. In order to take the first-mover advantage of such overseas expansion, I think it is time for our company to start moving.

We would like to accelerate the development of Southeast Asia as soon as the vaccine passport is available, in cooperation with the government and various private sector partners.

The Ministry of Land, Infrastructure, Transport, and Tourism is a general incorporated association, and we are also a member of the "all Nippon Michi-no-Eki network," and we are making progress in introducing systems at various roadside rest areas under the MLIT. The introduction to media and Tawaramoto Town, Nara Prefecture, has begun to spread, as a result of good feedback, and we will announce the progress in H2 of this fiscal year. However, we are feeling a good response.

Industry Collaboration

Expanding the scope of cooperation and accelerating collaboration through participation in SoftBank 5G Consortium [*1]

"SoftBank 5G Consortium" established in June 2021 as an organization where 5G communication device, cloud/ edge computing/ IoT device providers and other partners will conduct open demonstration experiments on themes across industries.

The 5 areas of focus are manufacturing, transportation, construction, medical care, and smart cities.

— Working group members

○ Manufacturing
○ Transportation
○ Construction
○ Medical
○ Smart City

— Suppliers

aws, CTC, vmware, uhuru, SCSK, SB Technology, NVIDIA, ERICSSON, OKI, 加賀電子, Catalyna, KYOCERA, Google Cloud, Groovenauts, cybereason, CCS, CISCO, JUNIPER, Sky, 住友電工, DELL Technologies, TREND, NEC, Hewlett Packard Enterprise, Microsoft, Neural Pocket, NOKIA, NOZOMI NETWORKS, VANTIQ, ptc, HITACHI 日立システムズ, HITACHI Inspire the Next, Hutzper, MACNICA, muRata, RENESAS

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We are also working with SoftBank, which is a private company.

The linkage between so-called AI and networks, and between Edge AI and networks, is very important. An AI edge terminal without a network is basically worthless, but in this context, we will expand nationwide in cooperation with major carriers. I think it is very important to work together on overseas development, and in this context, we would like to participate in the 5G Consortium to be more proactive in our activities.

In addition, we would like to strengthen the introduction of our products to the major companies that are lined up here, as well as export sales and joint sales here.

I would like to explain the progress of these businesses at SoftBank World 2021 next month on September 15, and I hope that you will join us.
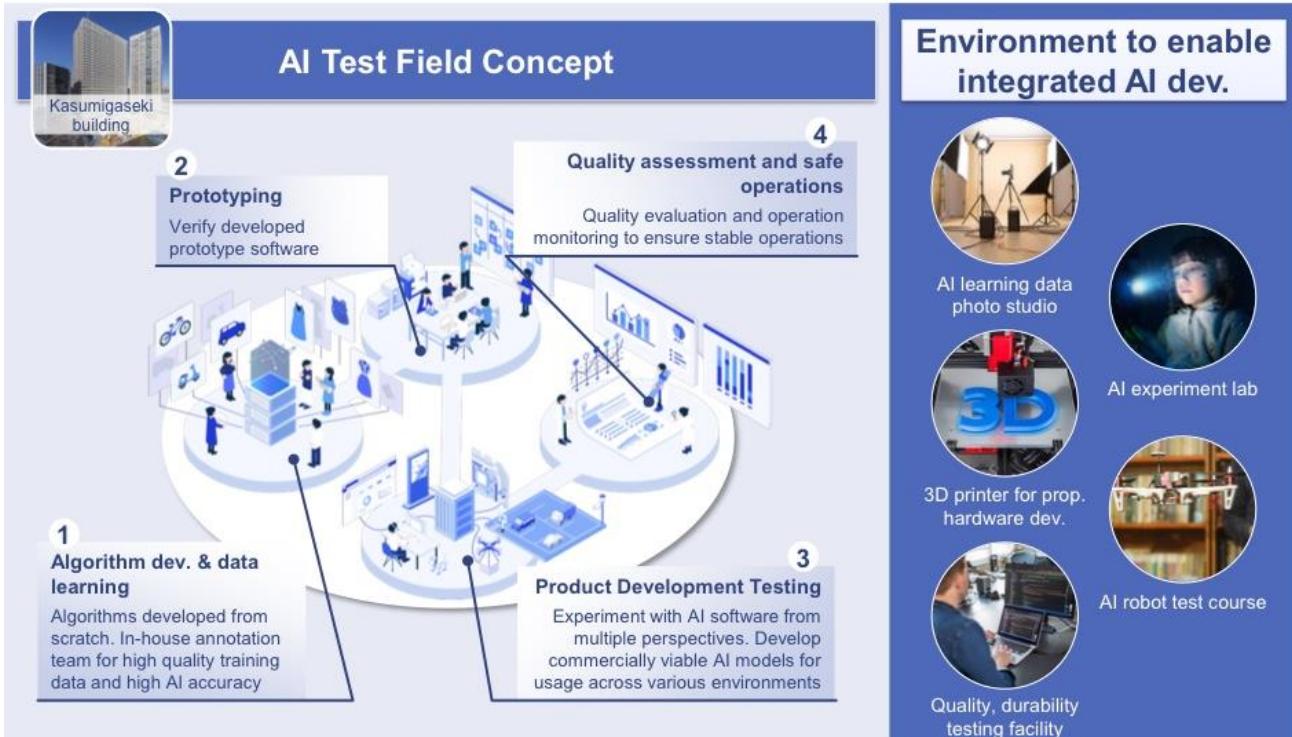
This is the AI test field.

As I mentioned earlier, the development of quality assurance for AI as a package is a very important activity, and we will continue to develop new libraries.

As for the question of where to build the AI engine when we expand overseas, our thinking is that our headquarters will secure the AI test field like this and build a solid AI development in Japan. We are considering a strategy to develop this as a global standard overseas, and this will be a central location for that.

Here is the progress in the apparel business.

FY2021 Q2 ended performance trajectory

- Steady business growth in FY2021 Q2
- Business progress in line with the annual forecast
- Sales and operating profits are expected to be concentrated in fourth quarter

(million JPY)

■ Net Sales   □ Operating Profit

+49.8%

490

327

Company Founded

94

0

52

+73.7%

91

-123

| 2018 Q2 (Cumulative) | 2019 Q2 (Cumulative) | 2020 Q2 (Cumulative) | 2021 Q2 (Cumulative) |

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Moving onto the business performance.

In H1 of the fiscal year, we achieved net sales of JPY490 million and an operating profit of JPY91 million.

In fact, I had thought that Q2 would be a little stronger, but due to procedural problems with the contracts in Q2, we were unable to complete them in time, and some of them were postponed to Q4, so Q2 probably did not meet the expectations of the market. I think that is probably reflected in the current stock price.

In our opinion, the back and forth between quarters within a full year will have no impact on our essential medium-term growth. We are very sorry to the individual and corporate investors for unnecessary volatility that has been caused. However, I do not believe that short-term business contracts in this area that go this way or that way will not undermine the essential strengths of our company, and we will continue to implement our business growth in a quiet manner.

We have already received a lot of questions to our IR team, so I will answer them first. This Q2 has no impact on Q3.

Q3 is to be the same as before, and for Q4, some of the data from Q2 will be recorded there, so Q4 may be a little stronger than necessary. I am very sorry about the volatility that will probably occur when the financial results and budget for next year are released, as there will be another debate on whether to base it on Q4 or when, but there is no problem with our policy of continuing to introduce the system, so we will continue to do our best.

FY2021 Q2 ended Jun. Statement of Income

(million JPY)	FY2020 Q2 ended Jun. (cumulative)	FY2021 Q2 ended Jun. (cumulative)	Increase amount	Increase percentage
Net Sales	**327**	**490**	**+163**	**+49.8%**
Operating profit	**52**	**91**	**+38**	**+73.7%**
% of net sales	16.0%	18.6%		
Ordinary profit	**45**	**88**	**+43**	**+97.2%**
% of net sales	13.8%	18.1%		
Net profit	**44**	**87**	**+42**	**+95.3%**
% of net sales	13.7%	17.9%		

Here are the contents. For more details, please refer to the financial statements.

FY2021 Q2 ended Jun. Balance Sheet

(million JPY)	FY2020 Q4 ended Dec.	FY2021 Q2 ended Jun.	Increase amount
Total current assets	**1,673**	**1,803**	**+129**
Cash and cash deposits	*1,424*	*1,482*	*+57*
Total non-current assets	**247**	**367**	**+120**
Total assets	**1,920**	**2,171**	**+250**
Total liabilities	**714**	**799**	**+85**
Interest bearing debt	*564*	*662*	*+98*
Total net assets	**1,206**	**1,371**	**+164**

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There are no changes in the balance sheet, especially cash and deposits.

FY2021 Q2 ended Jun. Cash Flows

(million JPY)	FY2020 Q2 ended Jun. (cumulative)	FY2021 Q2 ended Jun. (cumulative)
Cash flows from operating activities	19	1
Cash flows from investing activities	-50	-118
Cash flows from financing activities	184	174
Increase of cash and cash equivalents	+153	+57
Cash and cash equivalents at the end of period	979	1,482

Cash flows from investing activities for various purposes.

FY2021 full-year ending Dec. forecast

(million JPY)	FY2021 Q2 ended Jun. results (cumulative)	FY2021 Q4 ending Dec. forecast (cumulative)	Progress percentage
Net sales	490	1,256	39.0%
Operating profit % of net sales	91 18.6%	380 30.3%	23.9%
Ordinary profit % of net sales	88 18.1%	370 29.5%	24.0%
Net profit % of net sales	87 17.9%	280 22.3%	31.3%

No change to full-year forecast

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The full-year forecast remains unchanged at JPY1.256 billion.

As I mentioned earlier, on a quarterly basis, H2 of the fiscal year is quite skewed. Our business model is a very high gross profit business model, and the majority of our costs are fixed costs.

On a quarterly basis, when sales rise and fall slightly, costs remain almost the same, so the 3 bottom lines below operating profit seem to fluctuate greatly. On the contrary, if it goes up, and if the sales go up, the operating profit margin will be generated more than necessary. This is because of the business model, but I think it is better to look at the profit amount and profit margin for the whole year.

If anything, costs will remain the same no matter what happens to sales, so I think you can see the correct progress of our business if you look at whether we can achieve sales properly in the future IR.

For the current fiscal year, there is no change in the forecast.

Future growth strategy (Illustration of business growth)
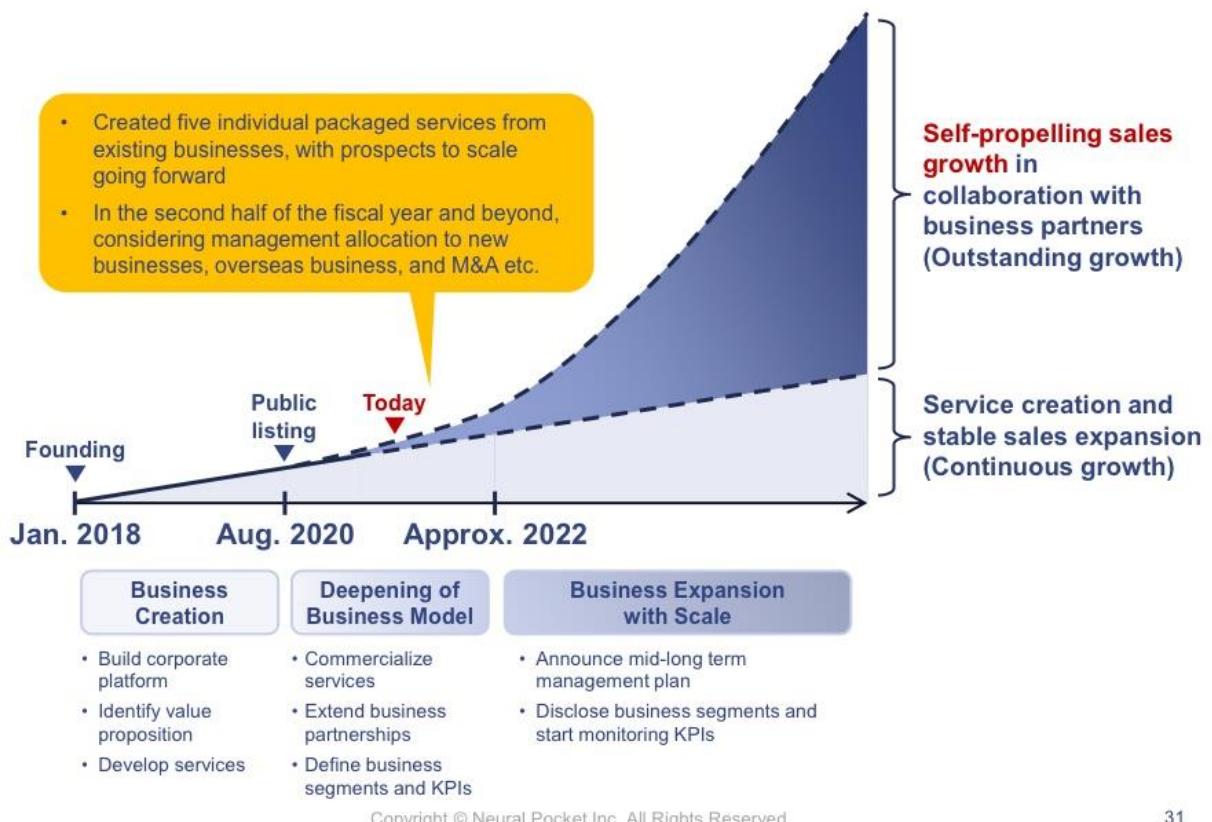
Regarding our vision for future growth from H2 of this year to next year, as I mentioned at the beginning, the business is progressing very well. I feel that we are making great progress, especially with regard to the packaging of these 5 services.

In particular, in addition to packaging, there is cataloging, which I didn't mention at the beginning of this, but it is mentioned in the yellow area. For example, if there is a parking service called DigiPark, the best camera set for DigiPark, or the best terminal set can be selected either by our company or the customer. We have been customizing the optimal specification level and combination of specifications for each customer, but this requires more man-hours when scaling up.

This cataloging means that we can include the standard hardware set that we recommend. Say that this set is suitable for this type of parking lot, for example, by creating a so-called "shouchikubai"—the first class, the second class, and third class—catalog. Customers can shorten the time from inquiries to installation, and from our point of view, the point here is to improve the efficiency of sales. We packaged it as a service and listed it in a catalog that includes hardware so that customers can automatically install it just by selecting this ABC "shouchikubai." I think we have made a lot of progress in this over the past 6 months.

Therefore, although it says that we are on track for cataloging and scaling in the future, I believe that H1 of the fiscal year went very well.

From H2 of the fiscal year onward, we have 2 themes. 1 theme is that we are now in a position to spread our packaged and cataloged products and increase their adoption. In addition to expanding in Japan, the next thing we have to do is to accelerate our overseas expansion. This means that the package has already been created, and the important thing is how to sell it.

As you saw in the hype cycle of technology trends earlier, Edge AI has a huge first-mover advantage. Basically, there are not any customers who bother to switch, so it says about 2022, but the next 2 to 3 years from this point is the Innovation Trigger time in the hype cycle of Edge AI. I think it is very important to spread the area around it while we are in this stage.

Management policy for FY2021

From fee-based to unit-based sales

In addition to expansion through individual contracts with companies/ governments, we aim to accelerate sell-propelling sales from generalized services

【Theme 1】 Expansion of co-creation partners	【Theme 2】 Towards easy-to-use AI services	【Theme 3】 Commitment to AI technology dev.
Expand required elements such as sales, maintenance and support, and bidding rights for government through partnerships or mergers and acquisitions as needed.	Pursue ease-of-use of services designed around customer needs. Aim to achieve 10,000-unit service system, with high AI service quality and operational stability.	Collect and accumulate the industry's leading level of data. Continue to invest in the dev. of optimal AI logics using proprietary learning technologies, including CG.

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Lastly, I would like to talk about our management policy for FY2021. There is no change here from fee-based to unit-based.

In the past, we have had a lot of large business negotiations and received rather large business from large customers, but limited business through unit-based sales. I believe that there will be no future for AI unless we make the leap to the proliferation of individual packages and services. This is the theme for this year, and I mentioned earlier about packaging and cataloging.

We will expand the number of co-creation partners and provide AI services that people want to use. This AI service that people want to use has been packaged and cataloged as I mentioned earlier. In terms of our commitment to AI technology, we will not cover it in this briefing, but would like to further strengthen the uniqueness of our deep learning capabilities.

That is all from me. If you have any questions, please go ahead.

Question & Answer

Moderator: We are now moving onto the question-and-answer session. Mr. Shigematsu, Chief Executive Officer, and Mr. Tane, Director, Chief Financial Officer, will answer your questions.

Mr. Kobayashi from Mizuho Securities. Please go ahead.

Kobayashi: Thank you very much. This is Kobayashi of Mizuho Securities. I would like to address 2 major points.

Thank you very much for explaining that the sales in this Q2 will be shifted to Q4 due to the problem of contractual misalignment. On the other hand, your explanation up to now has been that the main revenue is licensing revenue, and we or market participants may have thought that fixed monthly revenue was the main revenue, so the Q2 results may have come as a bit of a shock.

Based on that, please share the ratio of fixed monthly sales among total sales? In contrast, how much sales are likely to move due to contractual misalignment? I would like to know when you expect to be able to disclose this information? Thank you.

Shigematsu: In principle, we receive fixed monthly fees, but the contract can be for 1 year or 6 months. In the last financial results briefing meeting, we were asked how many contracts we had, and I shared that we had about 20, but there are quite a few types of contracts that are renewed at various durations. The conditions for renewal vary, where various services provided, may be divided into individual parts, and contractual procedures are required to recognize such revenues during each part.

Under such circumstances, it happened to be that the final arrangement was not in time for the extension. In essence, this is no difference from the explanations we have given so far, and it does not mean that we are losing our continuity.

We do not disclose what percentage of total sales, but in principle, all of such sales have been continuous, with the same customers continuing for a long time, and the number of new customers has increased. There are quite a few areas where sales have increased, so the first point is that there was a slight bias toward extending contracts in Q2.

Also, you have to understand that sales recognition is a completely different thing. We have a SaaS business where we have an online contract and we charge every month, and sales increase every month, but some of them are recognized once a quarter, some of them are recognized once every 6 months, etc., depending on the company. Sales recognition is actually an accumulation of inconsistent things, and the fact that there is continuity, and at which timing sales are recognized, are completely different discussions.

Naturally, we involve our audit firm, and have been working on the recognition of sales by individually reviewing contract terms and conditions and deciding in which month the sales should be recorded for accounting purposes. The composition ratio was high in this Q2, and that there are many parts that are decreasing, but there was a bias in the timing of recording sales. Essentially, what percentage of each individual quarter was accounted for is completely different from the percentage throughout the entire fiscal year, if you can think of it that way.

Kobayashi: Thank you for your detailed explanation. The second point I would like to make is that in the future, the 5 packaged services will be solidified, including the signage service. I get the impression that you are very positive about expanding volume, but I would like to ask about your views on how to expand volume, such as

how to create a winning strategy, and whether it is important to have partners or to have your own sales force. That's all from me.

Shigematsu: Thank you very much. This is a really important point, and it's on page 11. There are 5 packaged services now, but each service is slightly different. To summarize, I think the most important thing is to create a track record of implementation and then expand horizontally.

Particularly in the smart city area, both the private sector and the government, and within the private sector, for example, real estate, logistics, etc., when introducing such services, they are always asking if such services have actually been introduced in the past, as is the case with call centers.

Until now, we have been introducing new services that have never existed in the past, packaged it, and expanded it horizontally. It is still important to increase the number of partner companies. But if anything, they are asking if it has actually been introduced, and if there is a merit, they want to try it.

Whether it is easy or difficult to install such products is asked repeatedly throughout the sales process. As with DigiPark, rather than us going out to sell the products directly, for example to individual roadside stations as I mentioned before, we are starting to see activities that are spreading horizontally within such groups.

We will be rolling out the results of such introduction horizontally. It's a good horizontal connection. It's a bit confusing, but for example, in the case of DigiPark, if it's a logistics company, the service will be introduced within the network of logistics companies. If it is a roadside station, we will join such a network of the roadside stations. In the case of real estate, for example, as a common, so-called generalized system for real estate, we are now selling various products on a horizontal basis, but I think it is important to be aware of such horizontal connections in the future, and we are currently working on that.

If we get support from the sales force of an external partner, we are happy sharing commissions. However, we are also promoting sales on our own, and we are currently thinking about how to expand our business, but we will explain our winning strategy when we have developed a more specific sales strategy. I would like to explain our winning strategy at the end of this fiscal year.

Kobayashi: Thank you very much. That's all from me.

Moderator: Thank you very much. Is there anyone else who would like to ask a question?

Shigematsu: No more questions? Are you sure?

Thank you very much for joining us today for Neural Pocket Inc.'s financial results briefing for Q2 of the fiscal year ending December 2021. We will now close the meeting.

[END]