Consolidated Financial Results for the Nine Months Ended September 30, 2017 [Japanese GAAP]

November 9, 2017

Company name: KANRO CO., LTD.
Stock exchange listing: Tokyo Stock Exchange
Code number: 2216
URL: http://www.kanro.co.jp/
Representative: Kazuyasu Misu, President
Contact: Kenji Morimoto, Director and Senior Managing Executive Officer and General Manager of Administrative Headquarter
Phone: +81-3-3385-8811
Scheduled date of filing quarterly securities report: November 10, 2017
Scheduled date of commencing dividend payments: -
Availability of supplementary briefing material on quarterly financial results: No
Schedule of quarterly financial results briefing session: No

(Amounts of less than one million yen are rounded down.)

1. Consolidated Financial Results for the Nine Months Ended September 30, 2017 (January 1, 2017 to September 30, 2017)

(1) Consolidated Operating Results (% indicates changes from the previous corresponding period.)

	Net sales		Operating income		Ordinary income		Net income attributable to owners of parent	
Nine months ended	Million yen	%	Million yen	%	Million yen	%	Million yen	%
September 30, 2017	15,127	6.1	455	92.1	468	86.6	299	144.3
September 30, 2016	14,258	1.3	237	－	251	－	122	－

(Note) Comprehensive income: Nine months ended September 30, 2017: ¥356 million [240.9%]
Nine months ended September 30, 2016: ¥104 million [- %]

	Basic earnings per share	Diluted earnings per share
Nine months ended	Yen	Yen
September 30, 2017	83.19	－
September 30, 2016	33.84	－

* The Company conducted a share consolidation of common stock at a ratio of one share for five shares with July 1, 2017 as the effective date. Accordingly, the figures for basic earnings per share have been calculated assuming that the share consolidation had been conducted at the beginning of the previous fiscal year.

(2) Consolidated Financial Position

	Total assets	Net assets	Equity ratio
	Million yen	Million yen	%
As of September 30, 2017	17,140	9,757	56.9
As of December 31, 2016	17,947	9,736	54.3

(Reference) Equity: As of September 30, 2017: ¥9,757 million
As of December 31, 2016: ¥9,736 million

2. Dividends

	Annual dividends				
	1st quarter-end	2nd quarter-end	3rd quarter-end	Year-end	Total
	Yen	Yen	Yen	Yen	Yen
Fiscal year ended December 31, 2016	—	6.00	—	6.00	12.00
Fiscal year ending December 31, 2017	—	6.00	—		
Fiscal year ending December 31, 2017 (Forecast)				30.00	—

(Note) Revision to the forecast for dividends announced most recently: No

* The Company conducted a share consolidation of common stock at a ratio of one share for five shares with July 1, 2017 as the effective date. Accordingly, the year-end dividend per share for the fiscal year ending December 31, 2017 (forecast) show the amount after taking into consideration the consolidation of shares. The total amount of annual dividends is indicated with "—." The year-end dividend per share for the fiscal year ending December 31, 2017 would be ¥6 and the total annual dividends per share would be ¥12 if the share consolidation were not considered. Please refer to "Explanation of the proper use of financial results forecast and other notes" for details.

3. Consolidated Financial Results Forecast for the Fiscal Year Ending December 31, 2017 (January 1, 2017 to December 31, 2017)

(% indicates changes from the previous corresponding period.)

	Net sales		Operating income		Ordinary income		Net income attributable to owners of parent		Basic earnings per share
	Million yen	%	Million yen	%	Million yen	%	Million yen	%	Yen
Full year	21,000	6.5	830	40.3	850	38.9	510	1.9	140.72

(Note) Revision to the financial results forecast announced most recently: No

* The Company conducted a share consolidation of common stock at a ratio of one share for five shares with July 1, 2017 as the effective date. Accordingly, the figures for basic earnings per share have been calculated assuming that the share consolidation had been conducted at the beginning of the fiscal year ending December 31, 2017. Please refer to "Explanation of the proper use of financial results forecast and other notes" for details.

*** Notes:**

(1) Changes in significant subsidiaries during the nine months ended September 30, 2017 (changes in specified subsidiaries resulting in changes in scope of consolidation): No

(2) Accounting policies adopted specially for the preparation of quarterly consolidated financial statements: No

(3) Changes in accounting policies, changes in accounting estimates and retrospective restatement
1) Changes in accounting policies due to the revision of accounting standards: No
2) Changes in accounting policies other than 1) above: No
3) Changes in accounting estimates No
4) Retrospective restatement: No

(4) Total number of issued shares (common shares)
1) Total number of issued shares at the end of the period (including treasury shares):
September 30, 2017: 3,828,901 shares
December 31, 2016: 3,828,901 shares

2) Total number of treasury shares at the end of the period:
September 30, 2017: 245,798 shares
December 31, 2016: 205,013 shares

3) Average number of shares during the period:

Nine months ended September 30, 2017: 3,601,197 shares
Nine months ended September 30, 2016: 3,624,443 shares

*1. The Company conducted a share consolidation of common stock at a ratio of one share for five shares with July 1, 2017 as the effective date. Accordingly, the figures for the total number of issued shares at the end of the period, total number of treasury shares at the end of the period and average number of shares during the period have been calculated assuming that the share consolidation had been conducted at the beginning of the previous fiscal year.

2. Total number of treasury shares at the end of the period include the Company's treasury shares owned by Japan Trustee Services Bank, Ltd. (Trust Account) (September 30, 2017: 55,000 shares and December 31, 2016: －shares).

* These quarterly financial results are outside the scope of the quarterly review.

* Explanation of the proper use of financial results forecast and other notes

The earnings forecasts and other forward-looking statements herein are based on currently available information and certain assumptions deemed reasonable. Actual results may differ significantly from these forecasts due to a wide range of factors. Please refer to "(3) Explanation of Consolidated Financial Results Forecast and Other Forward-looking Information" on page 6 of the Appendix for assumptions on financial results forecasts and notes on the use of such forecasts.

(Dividends after the stock consolidation and financial results forecast)

The Company conducted a share consolidation of common stock at a ratio of one share for five shares with July 1, 2017 as the effective date, which was approved at the 67th Ordinary General Meeting of Shareholders held on March 29, 2017.

Meanwhile, dividends and financial results forecast would be as follows if the share consolidation were not considered:

1. Dividends forecast for the fiscal year ending December 31, 2017
   Dividend per share: ¥6 for year-end (Note 1)
2. Financial results forecast for the full fiscal year ending December 31, 2017
   Net income per share: ¥28.14 for year-end

Notes: 1. This is a dividend amount calculated before the share consolidation.
2. The total annual dividends per share for the fiscal year ending December 31, 2017 (before the share consolidation) would be ¥12.

Table of Contents

1. Qualitative Information on Quarterly Financial Results for the Period under Review 5
(1) Explanation of Business Results 5
(2) Explanation of Financial Position 5
(3) Explanation of Consolidated Financial Results Forecast and Other Forward-looking Information 6

2. Matters Regarding Summary Information (Notes) 7
(1) Additional Information 7

3. Quarterly Consolidated Financial Statements and Primary Notes 8
(1) Quarterly Consolidated Balance Sheets 8
(2) Quarterly Consolidated Statements of Income and Comprehensive Income 10
Quarterly Consolidated Statements of Income 10
Quarterly Consolidated Statements of Comprehensive Income 11
(3) Notes to Quarterly Consolidated Financial Statements 12
(Notes on going concern assumption) 12
(Notes in the case of significant changes in shareholders' equity) 12
(Significant subsequent events) 12

1. Qualitative Information on Quarterly Financial Results for the Period under Review

(1) Explanation of Business Results

The Japanese economy during the nine months ended September 30, 2017 followed a moderate recovery trend as the employment and income environment continued to improve, and signs of a recovery were seen in domestic consumer sentiment. However, in the candy market, while the consumption of gummies was robust, the consumption of candies remained on a decreasing trend despite the favorable factor of cooler weather after August. As a result, sales in the overall candy market decreased slightly year on year and harsh conditions continued.

In such a business environment, under the sales structure renewed in April this year with the aim of strengthening our proposal capabilities, we continued to actively promote sales through mass retailers and convenience stores and strove to increase net sales.

Furthermore, as part of the Company's initiatives to revitalize its mainstay brand, the *Kenko Nodoame* (healthy throat lozenges) series, consumer marketing campaigns were implemented in line with the launch of the new products *Kenko Nodoame Tatakau Nyusankin* (throat lozenges featuring protection by probiotics) and *Kenko Nodoame Tatakau Manuka Honey* (throat lozenges featuring protection by Manuka honey).

For the nine months ended September 30, 2017, net sales of candies increased by 9.9% year on year owing to factors including greater sales of *Kinno Milk Candy* (premium milk candy) and *Super Menthol Nodoame* (menthol throat lozenges), products of mainstay brands. Net sales of gummies increased by 4.8% year on year, owing to greater sales of the mainstay brands *Puré Gummy* and *Candemina Gummy*. For Healthy Snacks, net sales decreased 5.8% year on year, due to a decline in sales of *Kuki-wakame Ume-aji* (salt-pickled plum-flavored wakame-stem) and *Marugoto Oishii Hoshi-ume* (tasty whole dried salt-pickled plums), despite a slight increase in the sales of *Nori to Kishu-ume no Hasami-yaki* (grilled seaweed chips with salt-pickled plum bits). As a result, net sales increased by ¥868 million (6.1%) year on year to ¥15,127 million.

In terms of profits, net sales of mainstay brand products with a high profit ratio increased, manufacturing costs were cut owing to reform efforts at manufacturing sites, and cost of sales were reduced from factors including a reduction in loss on abandonment. As a result, gross profit increased by ¥632 million (10.2%) year on year to ¥6,832 million.

Operating income increased by ¥218 million (92.1%) year on year to ¥455 million, despite greater selling expenses in line with greater net sales, and increased expenses due to active efforts in research and development and the nurturing of human resources for the future. Ordinary profit increased by ¥217 million (86.6%) year on year to ¥468 million. Net income attributable to owners of parent increased by ¥176 million (144.3%) year on year to ¥299 million.

(2) Explanation of Financial Position

Total assets at the end of the third quarter of the fiscal year under review decreased by ¥806 million (4.5%) from the end of the previous fiscal year to ¥17,140 million. This is mainly attributable to decreases in notes and accounts receivable - trade as well as property, plant and equipment by ¥733 million and ¥258 million, respectively, despite an increase in investments and other assets by ¥189 million.

Liabilities decreased by ¥828 million (10.1%) from the end of the previous fiscal year to ¥7,382 million. This is mainly attributable to decreases in accrued expenses, income taxes payable and long-term loans payable by ¥271 million, ¥334 million and ¥367 million, respectively, despite an increase in provision for bonuses by ¥155 million.

Net assets increased by ¥21 million (0.2%) from the end of the previous fiscal year to ¥9,757 million. This is mainly attributable to the recording of ¥299 million in net income attributable to owners of parent, an increase in retained earnings by ¥81 million due to the payment of ¥217 million in dividends, an increase in valuation difference on available-for-sale securities by ¥50 million, in addition to an increase in treasury shares, including shares contributed to the trust in line with the introduction of the share compensation system for Directors, etc., by ¥136 million.

(3) Explanation of Consolidated Financial Results Forecast and Other Forward-looking Information

No revisions have been made to the full-year consolidated financial results forecast for the fiscal year ending December 31, 2017 released on February 9, 2017.

2. Matters Regarding Summary Information (Notes)

(1) Additional Information

(Application of Revised Implementation Guidance on Recoverability of Deferred Tax Assets)

The Company has applied the Revised Implementation Guidance on Recoverability of Deferred Tax Assets (Accounting Standards Board of Japan ("ASBJ") Guidance No. 26, March 28, 2016) from the first quarter of the fiscal year under review.

3. Quarterly Consolidated Financial Statements and Primary Notes

(1) Quarterly Consolidated Balance Sheets

(Thousand yen)

	As of December 31, 2016	As of September 30, 2017
Assets		
Current assets		
Cash and deposits	2,375,943	2,305,119
Notes and accounts receivable - trade	4,829,981	4,096,043
Merchandise and finished goods	559,463	571,917
Work in process	3,998	54,964
Raw materials and supplies	218,565	218,562
Other	429,881	436,965
Total current assets	8,417,834	7,683,572
Non-current assets		
Property, plant and equipment		
Buildings and structures	8,667,258	8,421,968
Accumulated depreciation	(5,207,570)	(5,138,086)
Buildings and structures, net	3,459,687	3,283,881
Machinery, equipment and vehicles	12,688,805	12,673,826
Accumulated depreciation	(9,880,195)	(10,229,944)
Machinery, equipment and vehicles, net	2,808,609	2,443,882
Land	1,909,312	1,822,491
Construction in progress	15,547	369,887
Other	957,224	924,877
Accumulated depreciation	(740,582)	(693,717)
Other, net	216,642	231,159
Total property, plant and equipment	8,409,799	8,151,303
Intangible assets	148,149	144,611
Investments and other assets		
Investment securities	443,052	516,449
Other	528,576	644,539
Total investments and other assets	971,628	1,160,988
Total non-current assets	9,529,577	9,456,902
Total assets	17,947,411	17,140,474

(Thousand yen)

	As of December 31, 2016	As of September 30, 2017
Liabilities		
Current liabilities		
Notes and accounts payable - trade	1,454,317	1,421,176
Short-term loans payable	490,000	490,000
Accounts payable - other	478,853	475,319
Accrued expenses	1,507,601	1,235,749
Income taxes payable	348,642	14,024
Provision for bonuses	325,128	480,198
Provision for directors' bonuses	31,200	25,510
Other	315,815	269,171
Total current liabilities	4,951,559	4,411,148
Non-current liabilities		
Long-term loans payable	1,247,500	880,000
Net defined benefit liability	1,884,252	1,941,584
Provision for directors' retirement benefits	90,050	—
Provision for directors' share benefits	—	15,864
Other	37,437	134,060
Total non-current liabilities	3,259,239	2,971,508
Total liabilities	8,210,798	7,382,657
Net assets		
Shareholders' equity		
Capital stock	2,864,249	2,864,249
Capital surplus	2,532,550	2,550,983
Retained earnings	4,565,929	4,647,652
Treasury shares	(336,050)	(472,322)
Total shareholders' equity	9,626,679	9,590,564
Accumulated other comprehensive income		
Valuation difference on available-for-sale securities	125,798	176,034
Remeasurements of defined benefit plans	(15,864)	(8,781)
Total accumulated other comprehensive income	109,933	167,253
Total net assets	9,736,613	9,757,817
Total liabilities and net assets	17,947,411	17,140,474

(2) Quarterly Consolidated Statements of Income and Comprehensive Income

Quarterly Consolidated Statements of Income

Nine Months Ended September 30

(Thousand yen)

	For the nine months ended September 30, 2016	For the nine months ended September 30, 2017
Net sales	14,258,717	15,127,302
Cost of sales	8,058,772	8,295,168
Gross profit	6,199,944	6,832,133
Selling, general and administrative expenses	5,962,904	6,376,788
Operating income	237,040	455,345
Non-operating income		
Interest income	259	155
Dividend income	6,035	6,093
Income from loss	4,688	—
Sold power income	9,142	10,074
Other	10,138	10,131
Total non-operating income	30,265	26,455
Non-operating expenses		
Interest expenses	7,419	5,943
Sold power expenses	4,892	4,885
Other	3,954	2,544
Total non-operating expenses	16,265	13,373
Ordinary income	251,039	468,427
Extraordinary income		
Gain on sales of non-current assets	—	371
Gain on donation of non-current assets	3,037	—
Insurance income	100,000	—
Total extraordinary income	103,037	371
Extraordinary losses		
Loss on retirement of non-current assets	2,594	3,382
Impairment loss	4,055	6,352
Total extraordinary losses	6,650	9,734
Income before income taxes	347,426	459,064
Income taxes - current	212,737	111,296
Income taxes - deferred	12,034	48,179
Total income taxes	224,771	159,475
Net income	122,654	299,588
Net income attributable to owners of parent	122,654	299,588

Quarterly Consolidated Statements of Comprehensive Income

Nine Months Ended September 30

(Thousand yen)

	For the nine months ended September 30, 2016	For the nine months ended September 30, 2017
Net income	122,654	299,588
Other comprehensive income		
Valuation difference on available-for-sale securities	(29,180)	50,236
Remeasurements of defined benefit plans, net of tax	11,219	7,083
Total other comprehensive income	(17,960)	57,319
Comprehensive income	104,693	356,908
Comprehensive income attributable to		
Comprehensive income attributable to owners of parent	104,693	356,908

(3) Notes to Quarterly Consolidated Financial Statements

(Notes on going concern assumption)

Not applicable.

(Notes in the case of significant changes in shareholders' equity)

Not applicable.

(Significant subsequent events)

(Absorption-type merger with consolidated subsidiary)

In the Board of Directors meeting held on November 9, 2017, the Company made a resolution to conduct an absorption-type merger with the Company's consolidated subsidiary Hikari Seika Co., Ltd. with July 1, 2018 as the effective date, and concluded a merger agreement on the same day.

1. Overview of transaction

(1) Name of company to be absorbed and its business activities

Name of company to be absorbed	Hikari Seika Co., Ltd.
Business activities	Manufacturing and sales of confectionery and food products

(2) Date of business combination

July 1, 2018 (Scheduled)

(3) Legal form of business combination

The business combination will be conducted through an absorption-type merger wherein the Company will be the surviving company and Hikari Seika Co., Ltd. will be dissolved.

(4) Name of company after business combination

KANRO CO., LTD.

(5) Overview of transaction including purpose of transaction

As part of the initiatives of the mid-term management plan "New KANRO 2021" that began in 2017, the aim of the business combination is to significantly reinforce profitability by raising the production efficiency of all facilities held by the Group as well as by further reducing cost of sales.

2. Overview of accounting treatment to be implemented

Based on the Revised Accounting Standard for Business Combinations (ASBJ Statement No. 21, September 13, 2013) and the Revised Guidance on Accounting Standard for Business Combinations and Accounting Standard for Business Divestitures (ASBJ Guidance No. 10, September 13, 2013), the business combination will be accounted for as a transaction under common control.