Consolidated Financial Results for the Six Months Ended June 30, 2018 and FY2018 Forecast

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Executive Officer
Senior Vice President, Accounting & Finance

Kao Corporation

July 26, 2018

FASF MEMBERSHIP

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Forward-looking statements such as earnings forecasts and other projections contained in this release are based on information available at this time and assumptions that management believes to be reasonable, and do not constitute guarantees of future performance. Actual results may differ materially from those expectations due to various factors.

- Kao Corporation changed its fiscal year end from March 31 to December 31 from the fiscal year ended December 31, 2012.

  [Term of consolidation for FY2012]
  - Group companies whose fiscal year end was previously March 31*: April - December 2012
  - Group companies whose fiscal year end was already December 31: January - December 2012

  * Kao Corporation and certain consolidated subsidiaries with the same fiscal year end

- The Kao Group adopted International Financial Reporting Standards (IFRS) from the fiscal year ended December 31, 2016.
- In the fiscal year ended December 31, 2017, the Kao Group adopted IFRS 15, “Revenue from Contracts with Customers” and its amendments early in tandem with a revision of its sales system for the Consumer Products Business in Japan.
- As of the three months ended March 31, 2018, the following changes have been made.
  1. The Beauty Care Business has been divided into the Cosmetics Business and the Skin Care and Hair Care Business, changing the four former reportable segments into five.
  2. The *Curél* derma care brand, which formerly had been classified as skin care and hair care products, has been included in the Cosmetics Business, and the *Success* men’s products brand, which formerly had been classified in the Human Health Care Business, has been included in the Skin Care and Hair Care Business. Net sales and operating income for the same period a year earlier have been restated accordingly.
  3. Due to the reorganization of the sales organization of the Consumer Products Business in Japan, operating income for the same period a year earlier has been restated.

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Overview of Consolidated Financial Results for the Six Months Ended June 30, 2018

2018 Initiatives

- Maintain businesses that are performing well and improve businesses with outstanding issues (cosmetics, hair care, beverages)
- Make proactive innovation-based proposals and prepare to create new businesses and continue to strengthen M&A initiatives
- Reform the structure of the Consumer Products Business and its sales organization in Japan

January - June 2018 Overview

- In a severe business environment, overall net sales and operating income were in line with projections. Changes in consumers, markets and retailing, and responding to competition, have become complex, and issues and progress differ by business. A shift to digital marketing, among other factors, led to more efficient use of expenses.
- Although the severe competitive environment will persist, aim to achieve the forecast of consolidated operating results for fiscal 2018 toward the achievement of Kao Group Mid-term Plan K20.
- Acquired Oribe Hair Care, LLC in January 2018.

Shareholder Returns

- Repurchased 6.23 million shares of stock for 50 billion yen.
- Dividend of 60 yen per share for the interim period of fiscal 2018, an increase of 6 yen per share, is in line with the announced forecast.

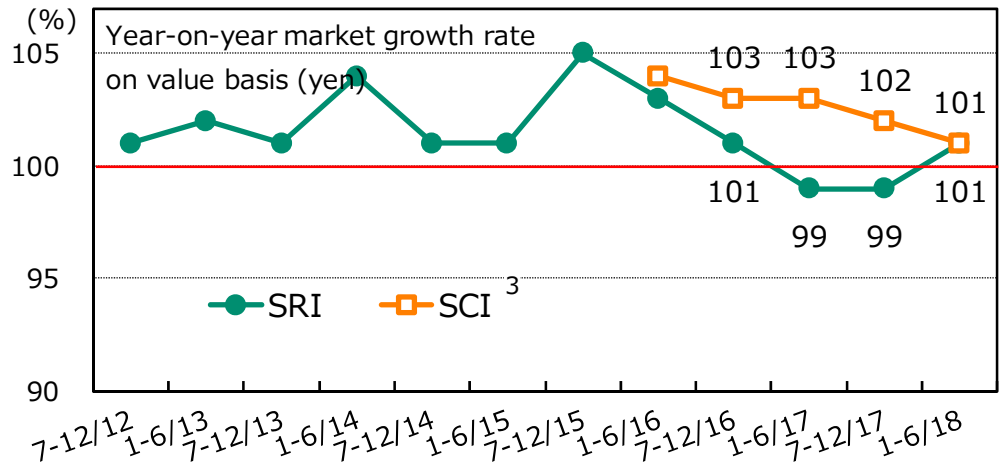
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Business Strategies and Progress

Cosmetics:	Structural reform of the mid- and high-price ranges progressed. In Japan, sales decreased compared with the same period a year earlier, but in Asia, sales and operating income grew substantially. *SUQQU, RMK, freeplus* and *Curél* performed strongly. Established a new global portfolio and began enhancing the prestige range, accelerating the global rollout of mass brands and reviewing the brand strategy for Japan.
Skin Care and Hair Care:	Skin care products performed strongly in Japan and Asia. In the Americas, *Bioré* struggled against fierce competition. In hair care products, shampoos and conditioners faced more intense competition in Japan and premiumization continued to be a struggle in the Americas and Europe. Enhanced high-value-added offerings with the launch in Japan of *Rerise*, a next-generation product for gray hair care.
Human Health Care:	Worked to maintain the premium status of *Merries* baby diapers, but sales decreased with the impact of initial shipments in China in the previous year. Sales of *Laurier* sanitary napkins and *MegRhythm* eye masks grew in Japan and China. *Healthya* functional drinks improved profitability through structural reform. Made an innovation-based offering of foaming toothpaste from the *Pyuora* brand.
Fabric and Home Care:	In fabric care products, competition was fierce in Japan. Worked to strengthen *Attack* laundry detergent by communicating the value of “changing tap water for washing to antibacterial water.” Sales grew in Thailand and elsewhere in Asia. Rolled out improved fabric softeners. Sales growth of home care products was firm.
Chemical:	Performed well due to increased demand outside Japan and stabilization of prices for oleo chemicals. Promoted more high-value-added products.

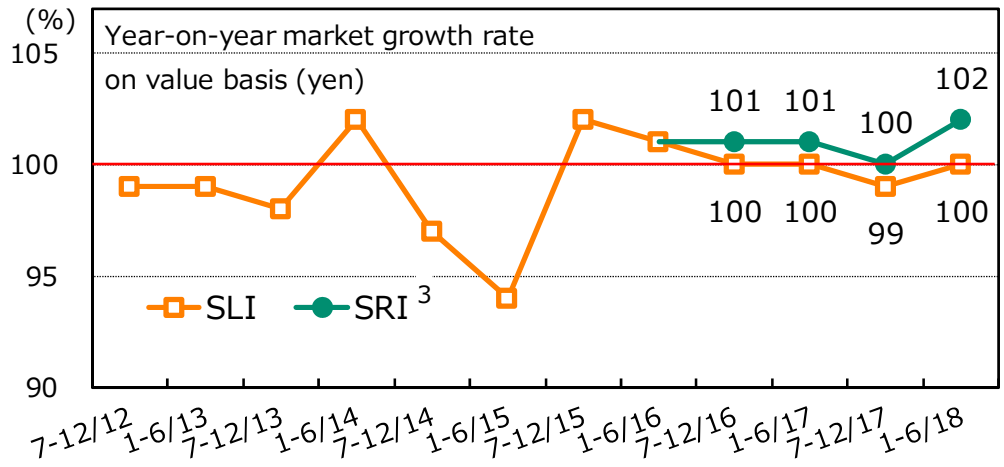
Consumer Products Market in Japan

Growth of household and personal care market[1]



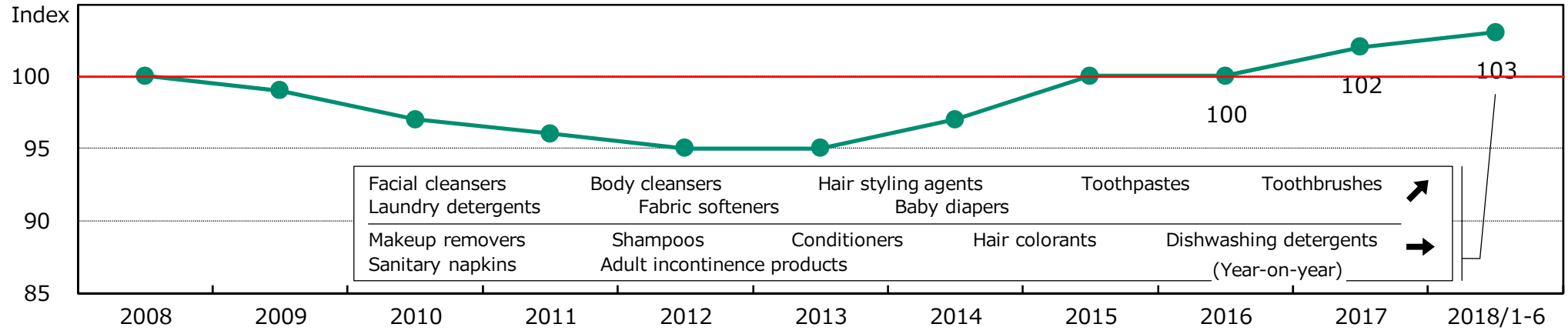
(Source: SRI POS data & SCI survey by INTAGE Inc.)

Growth of cosmetics market[2]



(Source: SRI POS data & SLI survey by INTAGE Inc. based on Kao's definition)
(Survey does not include inbound demand)

Consumer purchase price for 15 major household and personal care categories[4]



(Source: SRI POS data by INTAGE Inc.)

1. 82 major household and personal care product categories
2. 26 cosmetics product categories
3. SRI: Estimates based on POS data from approx. 4,000 retail outlets nationwide / SCI: Purchasing data from approx. 50,000 consumer monitors nationwide / SLI: Purchasing data for cosmetics, skin care and hair care products from approx. 40,000 female monitors
4. Index with January to December 2008 as 100

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Highlights of Consolidated Financial Results

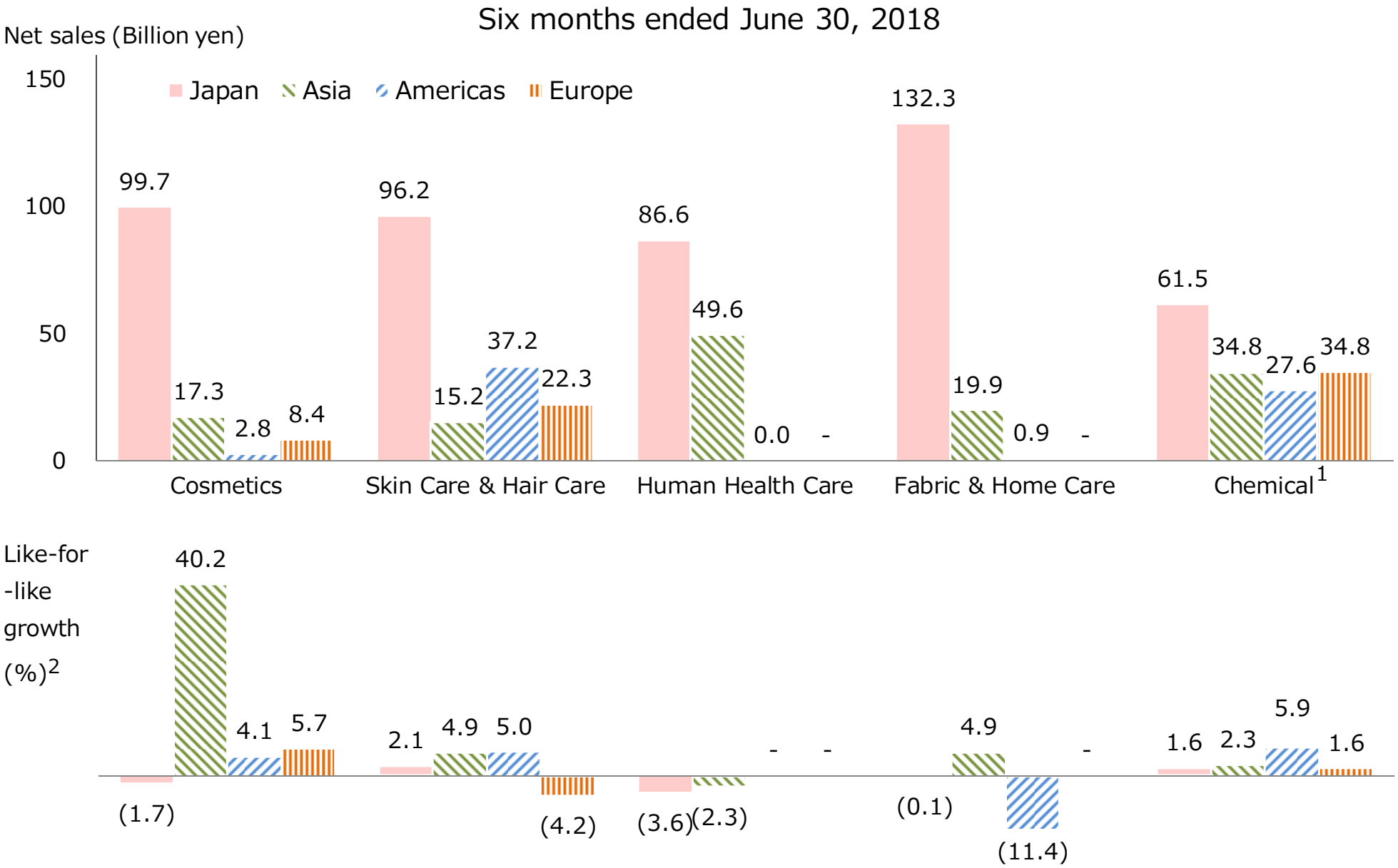
Consolidated Operating Results (Six months ended June 30)				
(Billion yen)	FY2017	FY2018	Growth %	Change
Net sales	717.3	729.0	+1.6	+11.7
Effect of currency translation[1]			+0.6	+4.4
Like-for-like, excluding effect of currency translation			+1.0	+7.3
Operating income	87.4	90.8	+3.9	+3.4
Operating margin	12.2%	12.4%		
Income before income taxes	86.7	89.9	+3.7	+3.2
Net income	56.9	63.5	+11.5	+6.5
Net income attributable to owners of the parent	56.5	62.8	+11.2	+6.3
EBITDA (Operating income + Depr. & amort.)	113.9	120.2	+5.6	+6.3
Basic earnings per share (yen)	114.56	127.76	+11.5	+13.20
Cash dividends per share (yen)	54.00	60.00		+6.00

Cash flow	Free cash flow[2]	(21.1)	billion yen
	Payments of cash dividends[3]	28.0	billion yen
	Purchase of treasury shares[4]	50.0	billion yen

1. Exchange rates: 108.76 yen/USD, 131.66 yen/Euro, 17.08 yen/Yuan
2. Free cash flow = Net cash flows from operating activities + Net cash flows from investing activities
3. Includes payments of cash dividends to non-controlling interests
4. Excludes share repurchases of less than one trading unit

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Consolidated Net Sales by Segment/Geographic Area



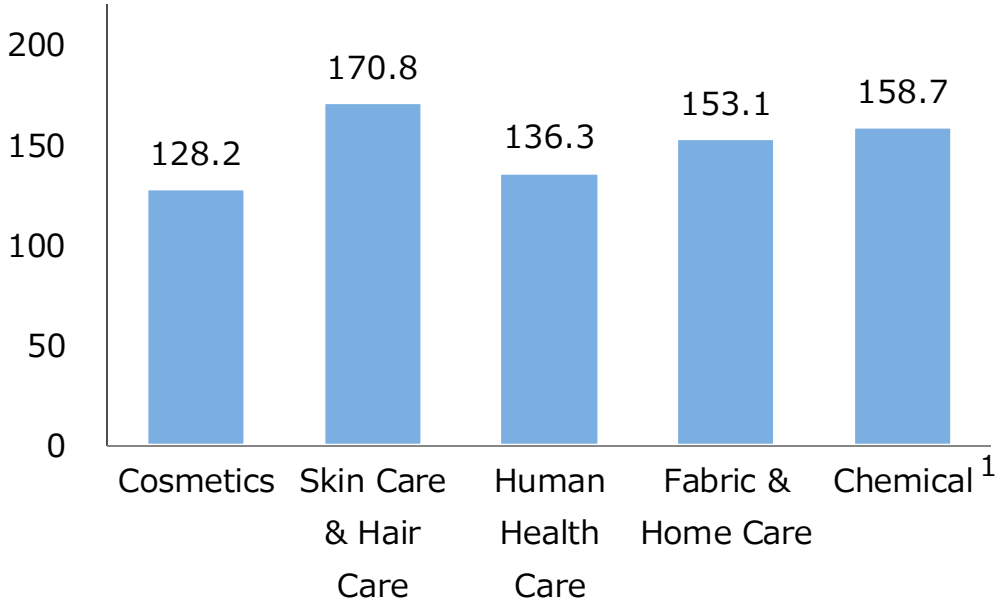
1. Net sales of the Chemical Business include intersegment transactions
2. Excluding the effect of currency translation

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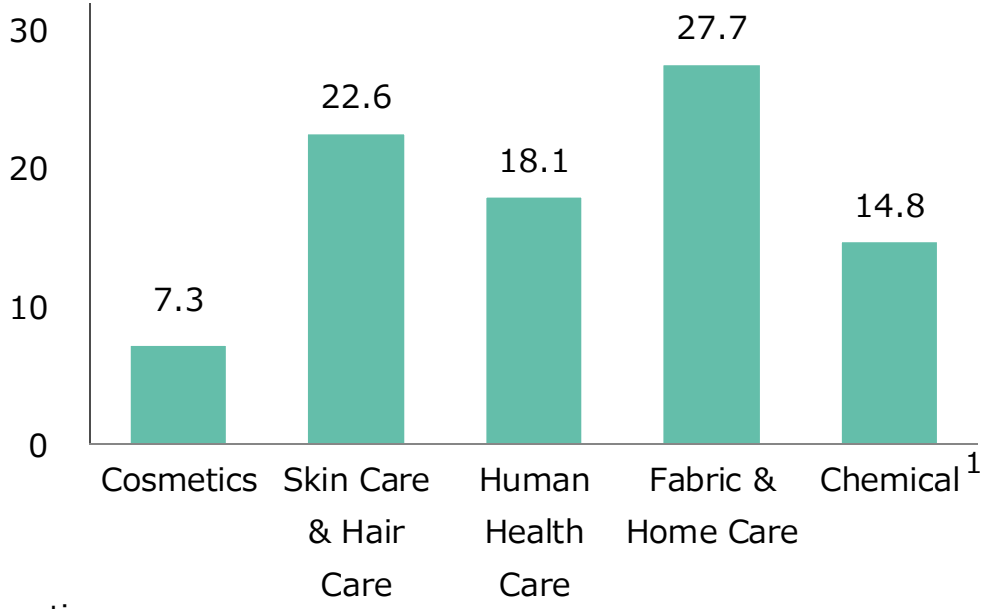
Consolidated Results by Segment

Six months ended June 30, 2018

Net sales (Billion yen)



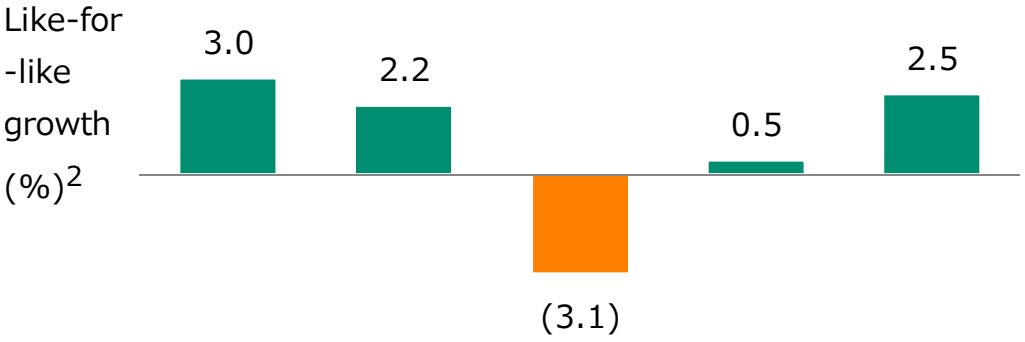
Operating income (Billion yen)



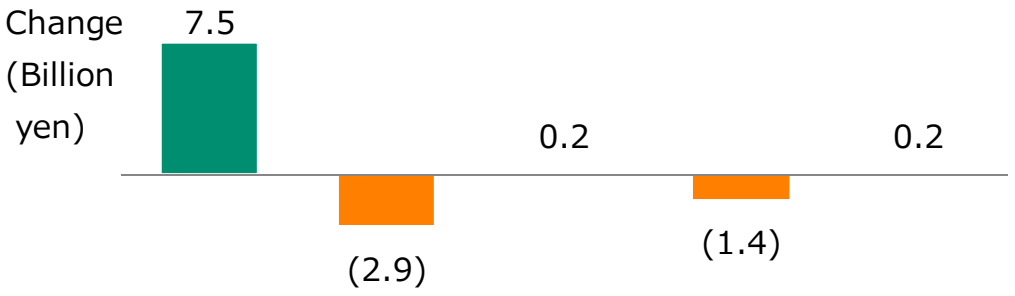
Operating margin (%)

Cosmetics	Skin Care & Hair Care	Human Health Care	Fabric & Home Care	Chemical
5.7	13.3	13.3	18.1	9.3

Like-for-like growth (%)[2]



Change (Billion yen)



1. Net sales and operating income of the Chemical Business include intersegment transactions
2. Excluding the effect of currency translation

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Consumer Products Business

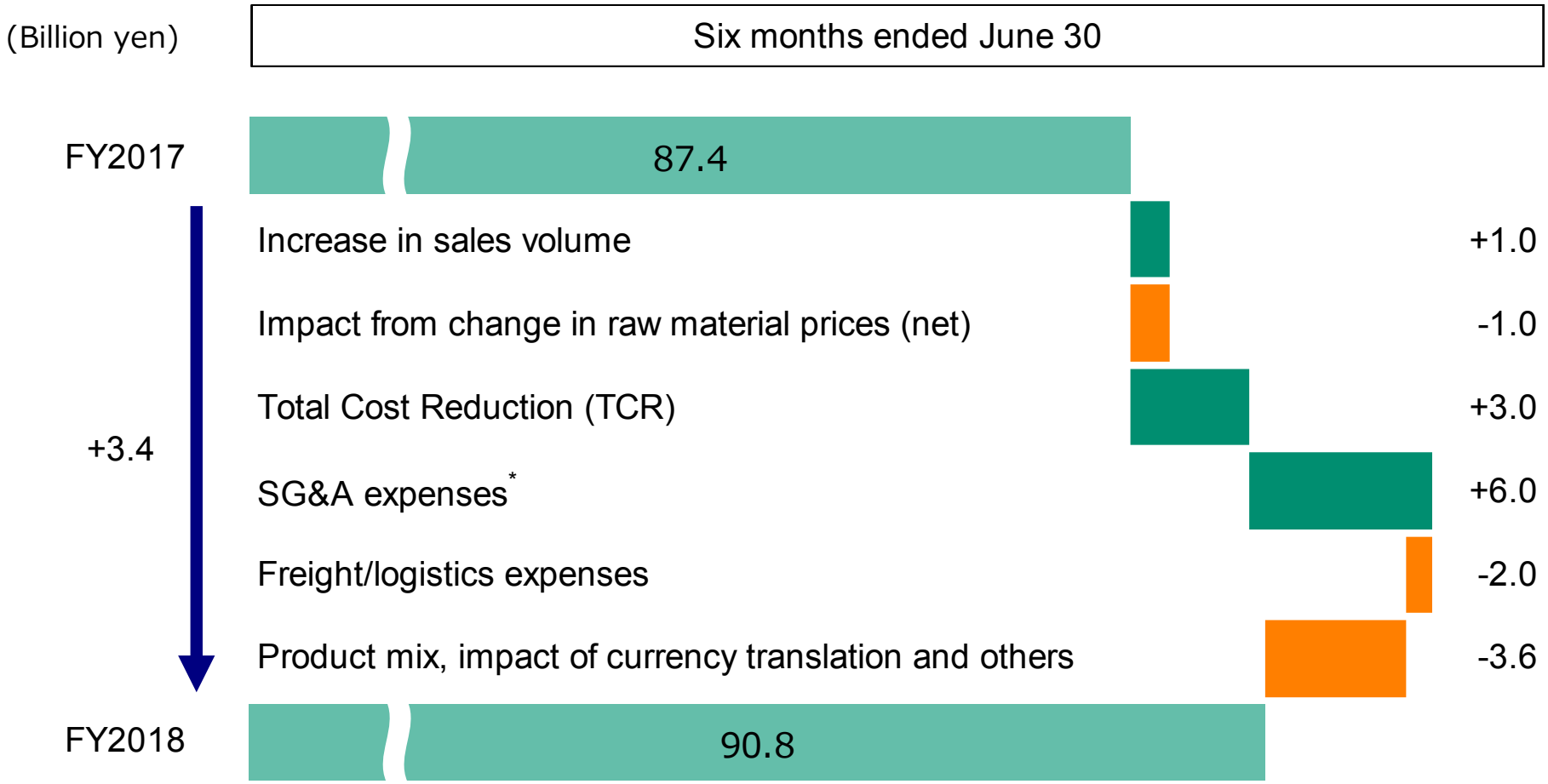
Six months ended June 30									
(Billion yen)	Net sales				Operating income			Operating margin %	
	FY2017	FY2018	Growth %	Like-for-like %[1]	FY2017	FY2018	Change	FY2017	FY2018
Japan	417.9	414.8	(0.7)	(0.7)	58.4	58.0	(0.4)	14.0	14.0
Asia	95.4	102.0	6.9	5.6	8.7	15.9	7.2	9.2	15.6
Americas	40.4	41.0	1.5	4.6	3.9	2.7	(1.2)	9.7	6.5
Europe	29.0	30.6	5.7	(1.7)	1.3	(0.9)	(2.2)	4.5	(2.9)
Consumer Products Business	582.6	588.4	1.0	0.6	72.4	75.7	3.3	12.4	12.9

Net sales growth rates of major countries and regions (Like-for-like %)	China:	5%[2]	Taiwan:	(2)%	Vietnam:	7%
	Indonesia:	8%	Thailand:	4%	Hong Kong:	15%

1. Excluding the effect of currency translation
2. 14% growth rate excluding the impact of initial shipments in the first quarter of fiscal 2017 following a distribution channel change as part of structural reforms of sales

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Analysis of Change in Consolidated Operating Income



* Excluding the effect of currency translation

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Future Initiatives and Forecasts

- In the Cosmetics Business, aim to achieve an operating margin of over 6% in 2018 and net sales of 300 billion yen with an operating margin of 10% in 2020 through cultivation by means of focused investment in strategic brands and structural reforms in the mid- and high-price ranges.
- Strengthen the positioning of *Bioré* in the Americas with new category extensions. Premiumize *John Frieda* hair care by customizing it according to the needs of each country in Europe. In Japan, strengthen high-value-added offerings with the launch of *Guhl Laboratory* plant-based hair care from *Guhl*, a brand that has been esteemed for many years in Europe. In the mass category, improvements to *Essential* are planned.
- For *Merries*, continue measures to maintain the brand's premium status. In China, aim for growth by addressing the rapidly growing pants-type category. Also, address retailing in regions and channels that are becoming borderless. Aim to maintain the strong performance of *Laurier* and *MegRhythm* in Japan and elsewhere in Asia.
- In fabric care products, although the competitive environment for laundry detergents is severe in Japan, work to maintain and expand market share by strengthening antibacterial-type products, for which there are high needs in the market.
- In the Chemical Business, stabilize profitability and aim for the fourth consecutive year of record high operating income with more high-value-added products.

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Major Assumptions for FY2018 Forecast

- Year-on-year growth rate of household and personal care market size in value (yen) in Japan
- Year-on-year growth rate of cosmetics market size in value (yen) in Japan

Slightly higher than previous year

		Growth
■ Net sales	¥1,540.0 billion	+3.4%
Effect of currency translation	+¥2.6 billion	+0.2%
Like-for-like, excluding effect of currency translation	+¥48.0 billion	+3.2%

		Estimated impact on income
■ Impact from change in raw material prices	Gross impact	-¥4.0 billion
	Net impact	-¥5.0 billion
■ Total Cost Reduction (TCR) activities		+¥6.0 billion
■ Capital expenditures/depreciation and amortization	Capital expenditures	¥90.0 billion
	Depreciation and amortization	¥60.0 billion

Exchange rate assumptions

- 110 yen/USD (FY2017 actual exchange rate [average] 112.18 yen/USD)
  135 yen/Euro (FY2017 actual exchange rate [average] 126.68 yen/Euro)
  17.0 yen/Yuan (FY2017 actual exchange rate [average] 16.60 yen/Yuan)

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Consolidated Operating Results Forecast for FY2018

Fiscal year (January 1 to December 31)

(Billion yen)	FY2017	Growth %	FY2018 (Forecast)	Growth %	Change
Net sales	1,489.4	+2.2	1,540.0	+3.4	+50.6
Effect of currency translation*				+0.2	+2.6
Like-for-like, excluding effect of currency translation				+3.2	+48.0
Operating income	204.8	+10.4	215.0	+5.0	+10.2
Operating margin	13.7%	-	14.0%	-	-
Income before income taxes	204.3	+11.4	215.0	+5.2	+10.7
[% of Net sales]	13.7%	-	14.0%	-	-
Net income attributable to owners of the parent	147.0	+16.2	152.0	+3.4	+5.0
[% of Net sales]	9.9%	-	9.9%	-	-
EBITDA (Operating income + Depr. & amort.)	259.3	+9.6	275.0	+6.1	+15.7
ROE	19.8%	-	18.5%	-	-
Basic earnings per share (yen)	298.30	+17.7	312.36	+4.7	+14.06
Cash dividends per share (yen)	110.00	-	120.00	-	+10.00

* Exchange rate assumptions: 110 yen/USD, 135 yen/Euro, 17.0 yen/Yuan

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Sales Forecast for FY2018

Consolidated Net Sales (Year ending December 31)

FY2018 (Forecast) (Billion yen)	Japan		Consolidated	
		Growth (%)		Like-for-like growth (%)[1]
Cosmetics Business	217.0	0.9	280.0	4.6
Skin Care and Hair Care Business	201.0	4.7	351.0	5.5
Human Health Care Business	185.0	0.3	286.0	1.5
Fabric and Home Care Business	302.0	2.4	344.0	2.5
Consumer Products Business	905.0	2.1	1,261.0	3.5
Chemical Business[2]			315.0	1.1
Consolidated			1,540.0	3.2

	Consolidated	
		Like-for-like growth (%)[1]
Japan	997.0	1.9
Asia	273.0	6.4
Americas	138.0	8.1
Europe	132.0	1.0
Consolidated	1,540.0	3.2

1. Excluding the effect of currency translation
2. Net sales of the Chemical Business include intersegment transactions

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Use of Cash Flow* and Shareholder Returns

Use steadily generated cash flow effectively from an EVA standpoint as shown below toward further growth.

- Investment for future growth (capital expenditures, M&A, etc.)
- Steady and continuous cash dividends (40% payout ratio target)
- Share repurchases and early repayment of interest-bearing debt including borrowings

* Net cash flows from operating activities

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ESG Initiatives to Enhance Corporate Value

Resource Recycling

- **Reducing Plastic through Refill and Replacement Products**
  Kao introduced refill and replacement products in Japan in 1991 to promote reduction of the amount of plastic used in packaging.
- **High Evaluation of *Smart Holder & Raku-raku Eco Pack* for Consideration of the Environment and Ease of Use**
  Received First Prize at the Ministry of Economy, Trade and Industry's 57th Japan Packaging Competition
- **Proposing the New Concept of RecyCreation® to Local Communities**
  Kao conducts research activities that create value through resource upcycling by collecting used refill packs and reprocessing them into interlocking blocks for use by local communities.



Using the easily replaceable *Raku-raku Eco Pack* with its special *Smart Holder*



Children using the blocks to make a bas relief of the official character of Onagawa Town

Cleanliness and Hygiene

- **Educational Programs in Japan and elsewhere in Asia to Establish Hygiene Habits**
  Kao conducts classes in Japan, Thailand, Taiwan, Indonesia and elsewhere to help children learn how to wash their hands properly.
- **Opening of a Website with Information on Cleanliness during Disasters**
  Kao opened a website presenting information to keep in mind on cleanliness that is useful for both disaster preparedness and during disasters.



Image of the website

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External Evaluation

Overall ESG	■ Selected for inclusion in the global ESG investment indices Dow Jones Sustainability World Index (DJSI World) and Dow Jones Sustainability Asia/Pacific Index (DJSI Asia/Pacific) for the fourth consecutive year ■ Included in the global FTSE4Good ESG investment index for the 11th consecutive year ■ Selected for all three ESG indices adopted by Japan's Government Pension Investment Fund, one of the world's largest pension funds: FTSE Blossom Japan Index; MSCI Japan ESG Select Leaders Index; and MSCI Japan Empowering Women Index (WIN)
Environmental	■ Received a Climate Change 2017 score of A-, a Water 2017 score of A- and a Forests 2017 score of A- from UK-based non-profit environmental assessment organization CDP
Social	■ Selected as a Health and Productivity Management Brand for the fourth consecutive year ■ Received Nadeshiko Brand designation for the third time in recognition of Kao's efforts as an enterprise that encourages women's success ■ Received an award in the consumer-oriented activities section of the 3rd Association of Consumer Affairs Professionals (ACAP) Consumer-oriented Activities Awards
Governance	■ Named one of the World's Most Ethical Companies for the 12th consecutive year ■ Selected as the Grand Prize Company for the Corporate Governance of the Year award by the Japan Association of Corporate Directors



Left: Yoshihiko Miyauchi, Chairman of the Japan Association of Corporate Directors
Right: Michitaka Sawada, President and Chief Executive Officer of Kao Corporation

ESG Investment Indices and Evaluations from External Organizations

ESG indices for which Kao has been selected

MEMBER OF Dow Jones Sustainability Indices In Collaboration with RobecoSAM

FTSE4Good

FTSE Blossom Japan

MSCI 2018 Constituent MSCI ESG Leaders Indexes

MSCI 2018 Constituent MSCI Japan ESG Select Leaders Index

MSCI 2018 Constituent MSCI Japan Empowering Women Index (WIN)

included in ETHIBEL SUSTAINABILITY INDEX EXCELLENCE Global

member of the INVESTMENT REGISTER ETHIBEL PIONEER & EXCELLENCE

EURONEXT vigeo eiris INDICES WORLD 120

ECPI Sense in sustainability

TOP 100 COMPANY 2017 Thomson Reuters Diversity & Inclusion Index

MS-SRI

Evaluations from external organizations

CDP SUPPLIER ENGAGEMENT LEADER 2018

ROBECOSAM Sustainability Award Bronze Class 2018

Corporate Responsibility Prime rated by oekom research

2018 WORLD'S MOST ETHICAL COMPANIES® WWW.ETHISPHERE.COM

DBJ健康格付 2016

2018 健康経営銘柄 Health and Productivity

2018 健康経営優良法人 Health and productivity ホワイト500

DIVERSITY MANAGEMENT SELECTION 100 2013

NADESHIKO BRAND 2018

プラチナくるみん 子育てサポートしています

* ESG Investment: Investment that takes into consideration Environmental, Social and Governance factors
SRI: Socially Responsible Investment

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Appendices

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Business Segments and Main Product Categories

Consumer Products Business

Cosmetics Business

Counseling cosmetics, Self-selection cosmetics



Six months ended June 2018

Sales:	¥128.2 billion
Like-for-like growth:[1]	+3.0%
Share of net sales:	17.6%
Operating margin:	5.7%

Skin Care and Hair Care Business

Skin care (mass products), Hair care (mass products), Professional hair care products



Six months ended June 2018

Sales:	¥170.8 billion
Like-for-like growth:[1]	+2.2%
Share of net sales:	23.4%
Operating margin:	13.3%

Human Health Care Business

Beverages, Oral care, Sanitary products, Blood circulation enhancement products (incl. bath additives and thermal pads)



Six months ended June 2018

Sales:	¥136.3 billion
Like-for-like growth:[1]	(3.1)%
Share of net sales:	18.7%
Operating margin:	13.3%

Fabric and Home Care Business

Laundry detergents, Fabric treatments, Products for kitchen, bath, toilet and living room care



Six months ended June 2018

Sales:	¥153.1 billion
Like-for-like growth:[1]	+0.5%
Share of net sales:	21.0%
Operating margin:	18.1%

Chemical Business

Six months ended June 2018

Sales:	¥158.7 billion[2]
Like-for-like growth:[1]	+2.5%
Share of net sales:[3]	19.3%
Operating margin:	9.3%

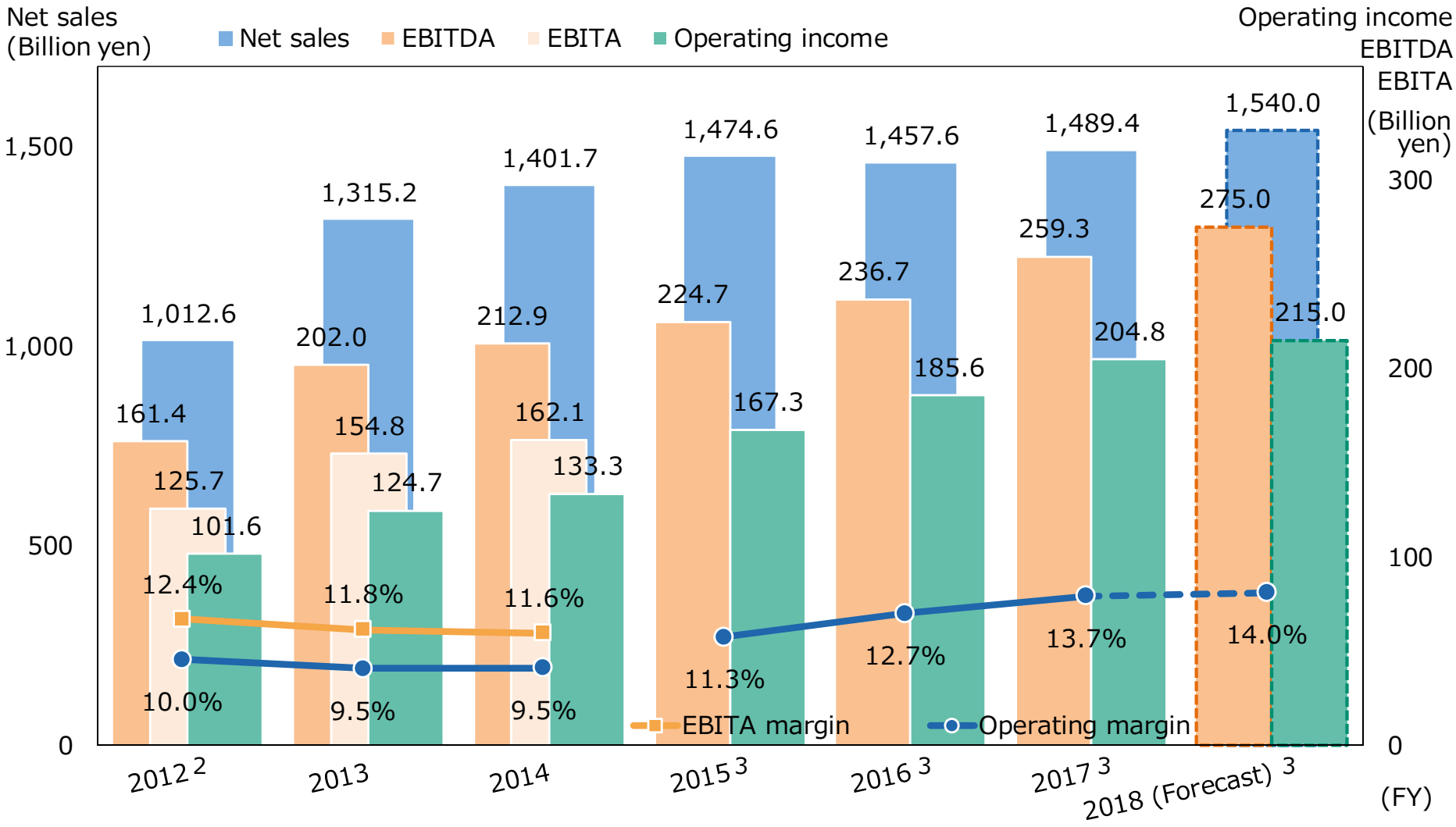
Oleo chemicals,
Performance chemicals,
Specialty chemicals,



1. Excluding the effect of currency translation
2. Net sales of the Chemical Business include intersegment transactions
3. Share of net sales is calculated based on sales to customers

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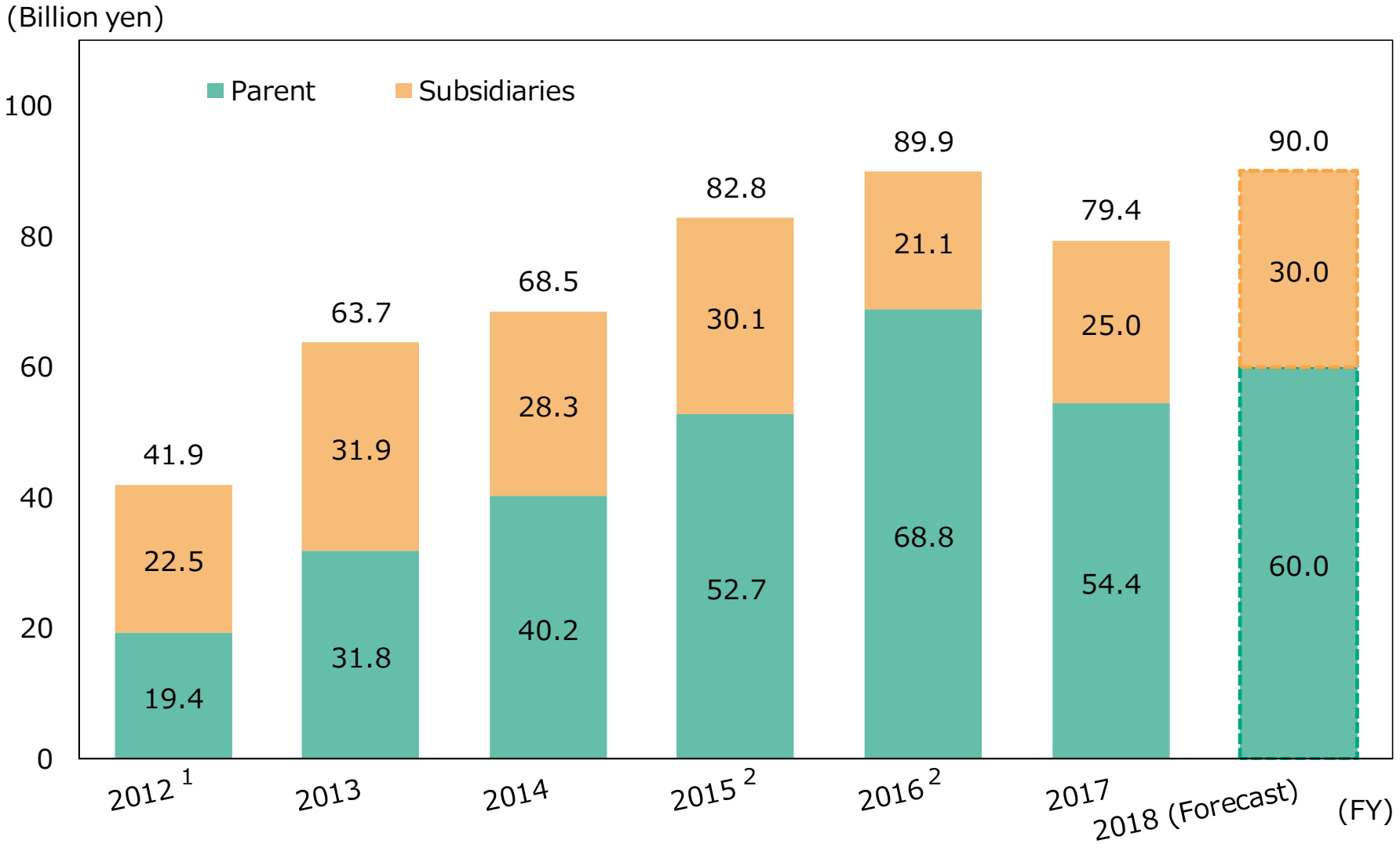
Consolidated Net Sales/EBITDA/EBITA[1]/Operating Income



1. Operating income before amortization of goodwill and intellectual property rights related to M&A
2. Fiscal year end is December 31 from FY2012 (Please refer to slide 2 for details)
3. IFRS adopted in FY2016. FY2015 figures are calculations based on IFRS. EBITA is not presented from FY2015 because amortization of goodwill has been discontinued under IFRS.

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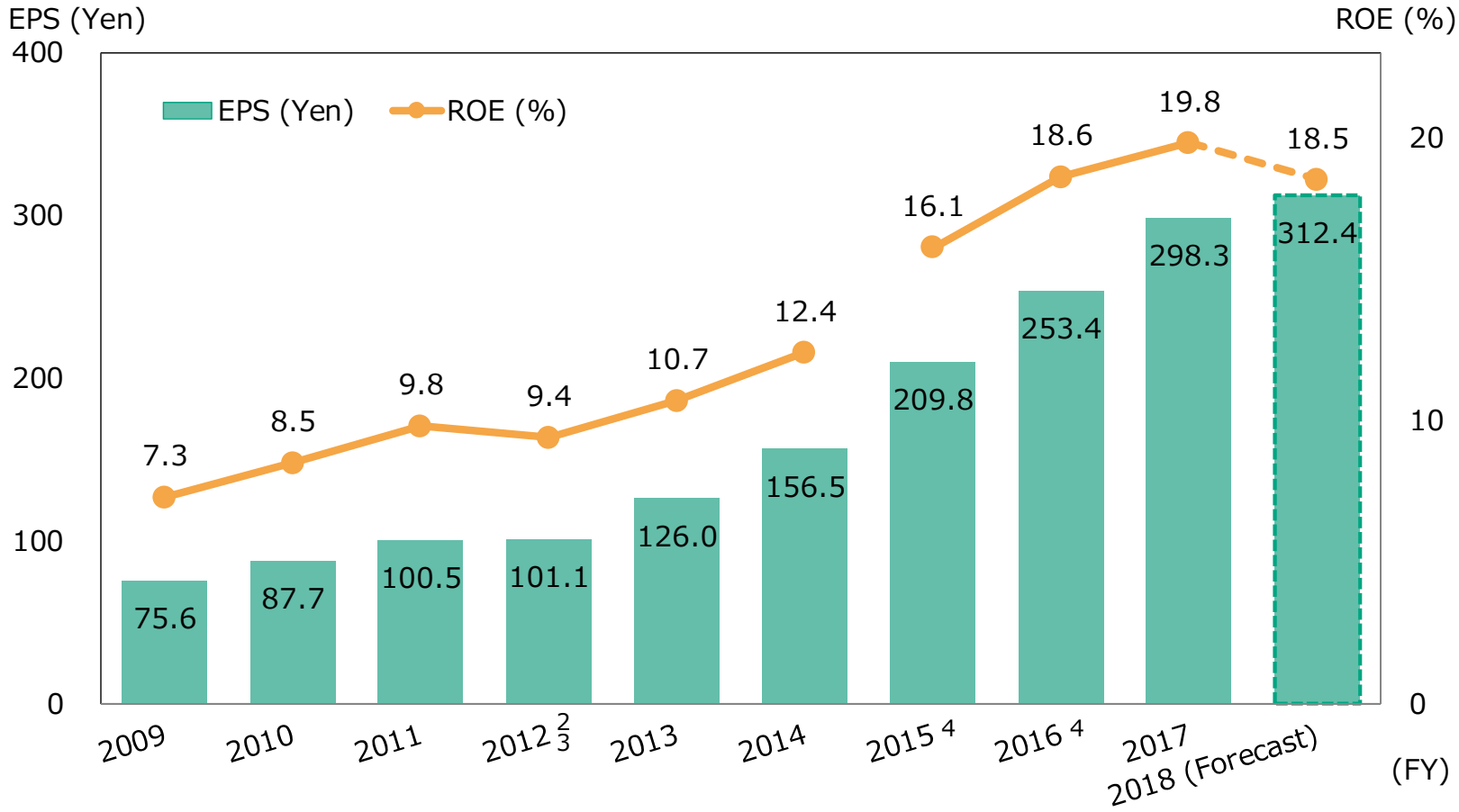
Capital Expenditures



1. Fiscal year end is December 31 from FY2012 (Please refer to slide 2 for details)
2. IFRS adopted in FY2016. FY2015 figures are calculations based on IFRS.

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ROE & EPS[1]

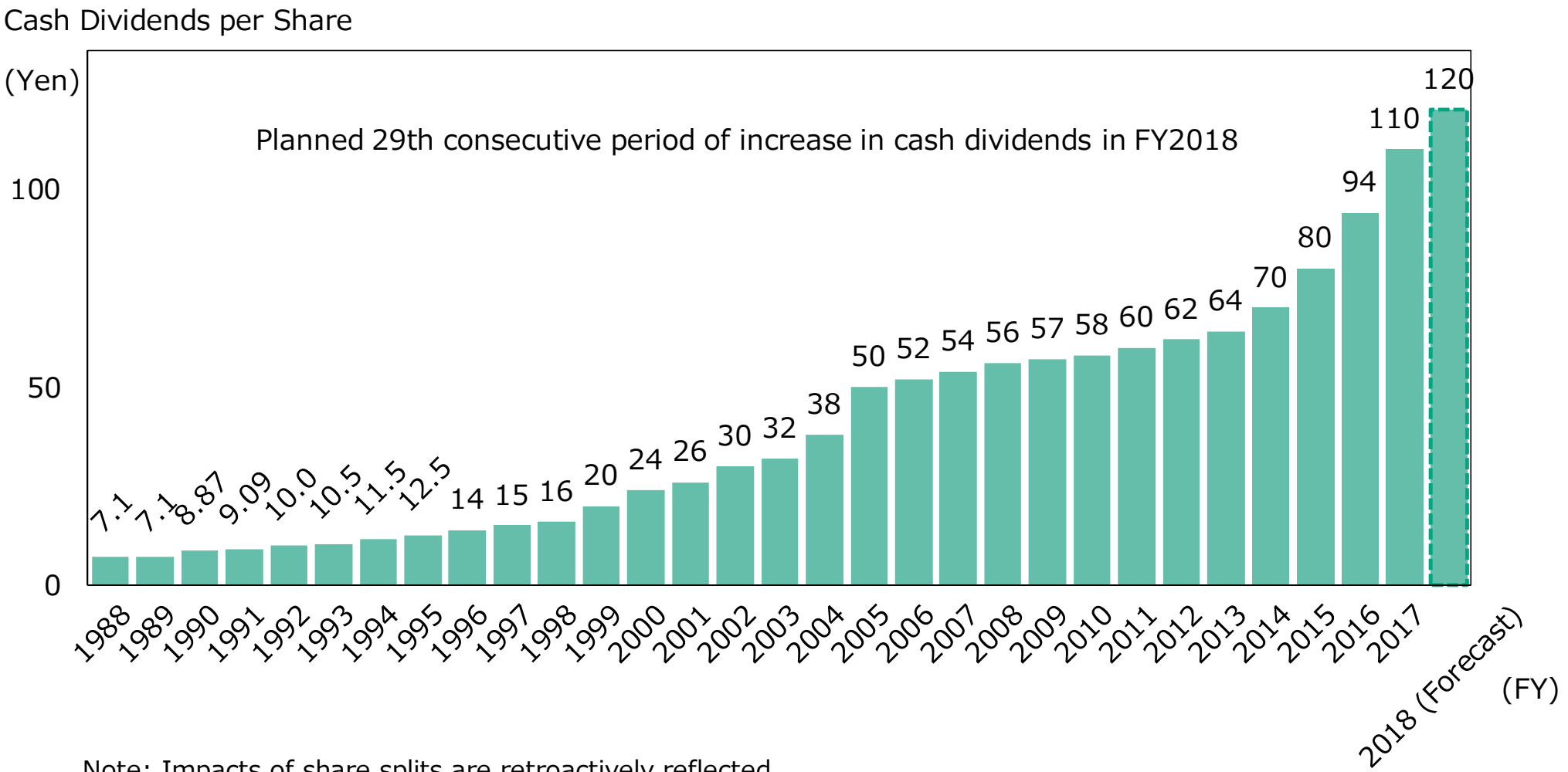


Weighted average number of shares outstanding (Million shares)	536.0	533.0	521.9	521.8	513.9	508.7	501.4	499.4	492.8	486.6
Net income [J-GAAP] / Net income attributable to owners of the parent [IFRS] (Billion yen)	40.5	46.7	52.4	52.8	64.8	79.6	105.2	126.6	147.0	152.0

1. Net income per share [J-GAAP] / Basic earnings per share [IFRS]
2. Fiscal year end is December 31 from FY2012 (Please refer to slide 2 for details)
3. ROE of FY2012 is for the transitional period connected with the change in fiscal year end
4. IFRS adopted in FY2016. FY2015 figures are calculations based on IFRS.

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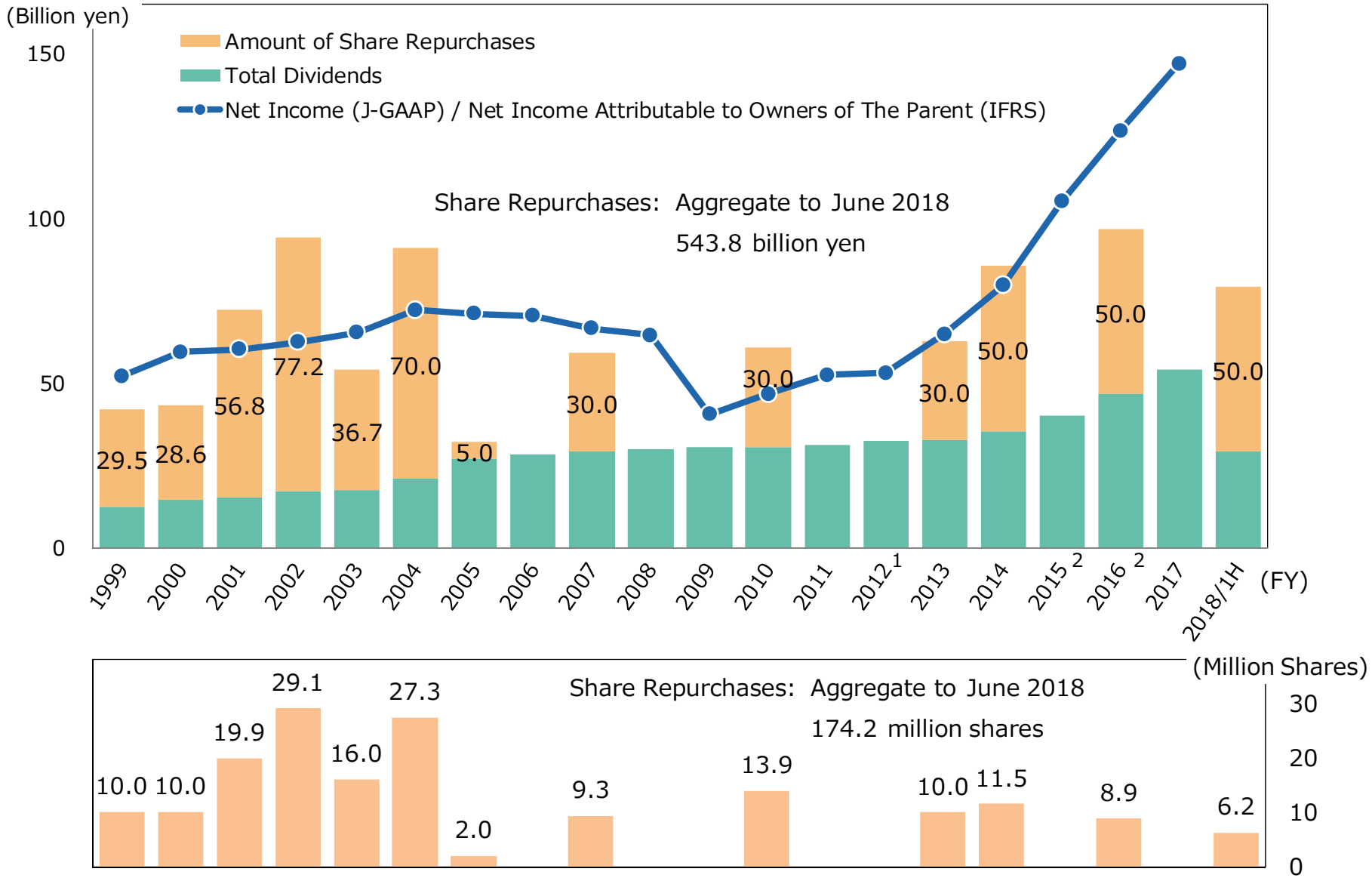
Cash Dividends per Share



Note: Impacts of share splits are retroactively reflected

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Shareholder Returns



1. Fiscal year end is December 31 from FY2012. Figures for FY2012 are for the period from January 1 to December 31, 2012. (Please refer to slide 2 for details.)
2. IFRS adopted in FY2016. FY2015 figures are calculations based on IFRS.

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