

Summary of Financial Results for the Second Quarter Ended February 28, 2018 [Japan GAAP] (Consolidated)

April 12, 2018

Company **Watts Co., Ltd.** Listed on the TSE
 Stock Code 2735 URL: <http://www.watts-jp.com>
 Representative Fumio Hiraoka, President and CEO
 Contact Hidehito Mori, Executive Managing Director, Head of Corporate Planning Office T E L: +81-6-4792-3280
 Expected date of filing of quarterly report: April 12, 2018 Expected starting date of dividend payment: -
 Preparation of quarterly supplementary financial document: Yes
 Quarterly results briefing: Yes (for institutional investors)

(Rounded down to million yen)

1. Consolidated business results for the six months ended February 2018

(September 1, 2017 through February 28, 2018)

(1) Consolidated results of operations (% change from the previous corresponding period)

	Sales		Operating profit		Recurring profit		Net income attributable to owners of parent	
	Million yen	%	Million yen	%	Million yen	%	Million yen	%
Six months ended Feb. 2018	23,886	1.7	593	-7.9	602	-13.4	379	-22.5
Six months ended Feb. 2017	23,484	2.6	643	9.9	695	18.9	489	41.0

(Note) Comprehensive income

Six months ended February 2018: 373 million yen (-25.9%)

Six months ended February 2017: 503 million yen (93.6%)

	Net income per share	Diluted net income per share
	Yen	Yen
Six months ended Feb. 2018	28.00	-
Six months ended Feb. 2017	36.13	-

(2) Consolidated financial position

	Total assets	Net assets	Shareholders' equity ratio
	Million yen	Million yen	%
As of Feb. 2018	19,717	10,042	51.6
As of Aug. 2017	20,084	9,873	49.7

(Reference) Shareholders' equity:

As of February 2018: 10,181 million yen

As of August 2017: 9,974 million yen

2. Dividends

	Annual dividend				
	End of 1Q	End of 2Q	End of 3Q	Year-end	Total
	Yen	Yen	Yen	Yen	Yen
Year ended Aug. 2017	-	0.00	-	15.00	15.00
Year ending Aug. 2018	-	0.00	-	-	-
Year ending Aug. 2018 (forecast)	-	-	-	15.00	15.00

(Note) Revisions to dividend forecast for the current quarter: None

3. Forecast of consolidated business results for the fiscal year ending August 2018

(September 1, 2017 through August 31, 2018)

(% change from the previous corresponding period)

	Sales		Operating profit		Recurring Profit		Net income attributable to owners of parent		Net income per share
	Million yen	%	Million yen	%	Million yen	%	Million yen	%	Yen
Year ending Aug. 2018	49,600	4.4	1,450	19.9	1,520	19.5	925	10.2	68.28

(Note) Revisions to business forecast for the current quarter: None

***Notes**

(1) Changes in significant subsidiaries during the period (changes in specified subsidiaries accompanying changes in the scope of consolidation): None

(2) Application of accounting procedures specific to preparation of the consolidated quarterly financial statements:
None

(3) Changes in accounting policies, accounting estimates and restatement

- | | |
|--|--------|
| ① Changes in accounting policies associated with revision of accounting standards: | : None |
| ② Changes in accounting policies other than ① | : None |
| ③ Changes in accounting estimates | : None |
| ④ Restatement | : None |

(4) Shares outstanding (common stock)

① Number of shares outstanding at the end of period (treasury stock included)

As of February 2018 13,958,800 shares

As of August 2017 13,958,800 shares

② Treasury stock at the end of period

As of February 2018 410,874 shares

As of August 2017 410,874 shares

③ Average number of stock during period (quarterly cumulative period)

Six months ended February 2018 13,547,926 shares

Six months ended February 2017 13,547,926 shares

(Note) The number of treasury stock at the end of period includes the Company's shares held by the share issuance trust for directors (FY8/18 2Q: 60,000 shares, FY8/17 2Q: 60,000 shares). In addition, the Company's shares owned by the share issuance trust for directors are included in treasury stock deducted for calculation of the average number of shares during period (FY8/18 2Q: 60,000 shares, FY8/17 2Q: 9,282 shares).

***Quarterly financial summary is not subject to auditing procedures by certified public accountants or auditing firms.**

***Explanation regarding appropriate use of business forecasts and other special instructions**

(Caution concerning forward-looking statements)

The forward-looking statements regarding future performance in this material are based on information currently available to the company and certain assumptions that the company deems to be reasonable at the time this report was prepared. Therefore, the company does not make promises about the achievements. Actual results may differ significantly from the forecasts due to various factors.

Please refer to “(3) Future forecast information including consolidated business forecasts” of “1. Results of operations” on page 5 for the suppositions that form the assumptions for business forecasts and cautions concerning the use of business forecasts.

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1. Results of Operations

(1) Analysis of operating results

During the six months ended February 2018, the Japanese economy expanded over 63 months, and real GDP grew for the eight consecutive quarters, mainly due to strong exports from the corporate sector and strong capital investment. As for the household sector, the number of permanent employees continued to increase owing to the gradual economic recovery. However, the growth in real income was limited, and consumer spending remained weak despite the continued improvement in consumer sentiment. This period was difficult especially for the retail industry, as there were two large typhoons and long rains in October, and heavy snowfall caused by strong cold waves from January onward.

Given this environment, in addition to the 100-Yen shop business in Japan, the Company, which operates the “Watts”, “Watts with”, “meets.”, “silk”, etc., has been working on diversifying its revenue sources by undertaking other domestic businesses, centering on the sale of interior goods and life-style goods, as well as overseas business.

As for the domestic 100-Yen shop business, the Company has been striving to achieve both greater customer satisfaction and higher earnings at shop by developing and selling ranges of private brand items under the “WATTS SELECT” brand consisting of reasonably priced, best value-for-money products, mostly daily-use household items, and carrying out low-cost opening and closing of shops and low-cost shop operations. At the same time, in order to create new brand value to meet diversifying customer needs, the Company is making further improvements through the business model restructuring which carries out a complete revision of the shop image and product mix, etc. As specific measures, the Company is currently undertaking sales promotional campaign that each store displays and features specific items along with a theme for each month to revitalize its sales floors and the development of “WATT'S new” sales proposal corners that make it easy for customers to imagine and visualize realistic lifestyle scenes. The Company will strive to further strengthen its sales promotion led by the headquarters. In addition, the Company is also proceeding with the optimization of product lineups on the basis of sales data acquired by POS systems. The Company has also introduced a reordering support system, for the purpose of preventing the unnecessary opportunity losses in sales caused by stock out, to improve the accuracy of its targeting in this regard. Furthermore, the Company has been steadily opening Watts branded shops, which were launched in February 2015, and the efforts have made it possible to open in good locations, such “Namba Marui” and “Kobe Marui” shops opened in March 2018.

As of the end of the second quarter, the number of “Watts” and “Watts with” 100-Yen shops increased by 95 to 352. In the 100-Yen shop business in Japan, the Company has already opened 81 shops, against the full-year plan of 108 shops, although there were many relatively small size shops. There were 32 shop closings (including 8 franchised shop), including certain unprofitable shops and unpredictable closing of shops where the Company’s shops were located in. As a result, the total number of 100-Yen shops at the end of the second quarter was 1,136, which includes 1,102 directly managed shops (net increase of 57), and 34 franchised/other shops (net decrease of 8).

As for the number of the other shops at the end of the second quarter, “Buona Vita,” a life-style goods shop offering comfortable life, was 21 shops (net decrease of 4). Buona Vita did not open any new shops during 1H, but the Company will focus on improving the profitability of existing shops. ‘Value-100,’ the fresh-foods supermarket collaboration, continues with 1 shop. In addition, “Søstrene Grene”, a Denmark’s life-style variety shop, opened “PRIME TREE AKAIKE” shop as the first opening in Tokai region, totaling 4 shops. The Company will make efforts to raise its brand recognition by dispatching products and shop information using SNS and increasing media

exposure.

Regarding the overseas operation, the Company operates “KOMONOYA”, a fixed-price shop mainly in Southeast Asia. At the end of 1H, “KOMONOYA” operates 33 shops in Thailand (net increase of 2), 4 shops in Malaysia (net decrease of 1), 12 shops in Vietnam (net decrease of 2), and 9 shops in Peru (net increase of 2). In China, a fixed price shop “小物家园” (KOMONOKAEN) closed 5 shops (1 Chinese style franchised shop) and resulted in 4 shops (1 Chinese style franchised shop). The total number of own-brand shops “KOMONOYA” and “小物家园” (KOMONOKAEN) was 62 (net decrease of 4). The numbers of local shops with sales floors consisting of the Company’s products are gradually increasing and expanding particularly in Myanmar, Mongolia, and Mexico. The total number of shops, in addition to our group shops, exceeds 100 shops. The Company added new product supply locations such as the Philippines, which are expected to achieve medium-to-long-term economic growth, the share of overseas sales in consolidated sales increased by 0.8 percentage points YoY to 5.4%.

As described above, the opening of 100-Yen shops was favorable, but same-store sales were weak mainly due to abnormal weather. As a result, for the second quarter of the fiscal year ending August 2018, sales were 23,886 million yen (up 1.7% YoY, 97.5% to the plan), operating profit was 593 million yen (down 7.9% YoY, 82.4% to the plan), recurring profit was 602 million yen (down 13.4% YoY, 80.3% to the plan). Net income attributable to owners of parent was 379 million yen (down 22.5% YoY, 82.5% to the plan) due to the recording of income taxes-deferred resulting from the impact of reorganization in the same period of the previous fiscal year. (*Year on year: comparison with the results for the previous fiscal year. Ratio to plan: ratio to the business forecasts for the second quarter of the fiscal year ending August 2018 which were announced in the Summary of Financial Results on October 12, 2017.)

Since the Group operates under a single segment consisting of the operation of 100-Yen shops associated business, segment information is omitted.

(2) Analysis of financial position

a. Assets, liabilities and net assets

(Assets)

As of the end of the second quarter of the current fiscal year, current assets stood at 14,717 million yen, a decrease of 559 million yen compared with the end of the previous fiscal year. This is mainly because notes and accounts receivable-trade decreased by 289 million yen, and cash and deposits increased by 253 million yen.

Fixed assets stood at 4,999 million yen, an increase of 191 million yen compared with the end of the previous fiscal year. This is mainly because tools, furniture and fixtures increased by 61 million yen, and buildings and structures increased by 58 million yen, and investment securities increased by 33 million yen, and guarantee deposits increased by 27 million yen.

As a result, total assets stood at 19,717 million yen, a decrease of 367 million yen compared with the end of the previous fiscal year.

(Liabilities)

As of the end of the second quarter of the current fiscal year, current liabilities stood at 8,269 million yen, a decrease of 554 million yen compared with the end of the previous fiscal year. This is mainly because accrued consumption taxes decreased by 165 million yen, and deposits included in other current liabilities decreased by 158 million yen, and income taxes payable decreased by 108 million yen.

Fixed liabilities stood at 1,404 million yen, an increase of 18 million yen compared with the end of the previous fiscal year. This is mainly because liabilities relating to retirement benefits increased by 11 million yen.

As a result, total liabilities stood at 9,674 million yen, a decrease of 536 million yen compared with the end of the previous fiscal year.

(Net assets)

As of the end of the second quarter of the current fiscal year, net assets stood at 10,042 million yen, an increase of 168 million yen compared with the end of the previous fiscal year. This is mainly because retained earnings increased by 175 million yen. As a result, the equity ratio was 51.6% (49.7% at the end of the previous fiscal year).

b. Cash flows

Cash and cash equivalents (hereinafter referred to as “cash”) at the end of the second quarter of the current fiscal year amounted to 5,473 million yen, a decrease of 253 million yen compared with the previous fiscal year.

Details and breakdown of each cash flow in the second quarter are as follows.

(Cash flows from operating activities)

Net cash provided by operating activities was 344 million yen (588 million yen was provided in the same period of the previous fiscal year). Cash was provided mainly by income before income taxes of 591 million yen, and decrease in accounts receivable-trade of 291 million yen. Cash was used mainly for income taxes paid of 329 million yen and increase in inventory assets of 160 million yen.

(Cash flows from investing activities)

Net cash used in investing activities was 391 million yen (259 million yen was used in the same period of the previous fiscal year). As for the breakdown, cash was used mainly for property, plant and equipment of 320 million yen for opening of new shops, and for payments for lease and guarantee deposits of 78 million yen.

(Cash flows from financing activities)

Net cash used in financing activities was 197 million yen (0 million yen was provided in the same period of the previous fiscal year). As for the breakdown, there were proceeds from long-term loans payable of 400 million yen, repayment of long-term loans payable of 394 million yen, and dividend paid of 203 million yen.

(3) Future forecast information including business forecasts

The Company made no revisions to its business forecasts announced in the summary of financial results on October 12, 2017.

2. Quarterly Consolidated Financial Statements

(1) Quarterly Consolidated Balance Sheets

	(Thousands of yen)	
	Previous fiscal year (August 31, 2017)	Current second quarter (February 28, 2018)
Assets		
Current assets		
Cash and deposits	5,727,607	5,473,644
Notes and accounts receivable-trade	2,201,021	1,911,752
Merchandise and finished goods	6,506,142	6,684,344
Raw materials and supplies	28,606	21,902
Deferred tax assets	303,936	270,346
Consumption taxes receivable	127,273	56,839
Other	404,956	320,313
Allowance for doubtful accounts	-22,621	-21,407
Total current assets	15,276,922	14,717,736
Noncurrent assets		
Property, plant and equipment		
Buildings and structures	1,454,655	1,545,295
Accumulated depreciation and impairment loss	-771,545	-803,675
Buildings and structures, net	683,109	741,619
Vehicles	11,236	11,264
Accumulated depreciation and impairment loss	-4,250	-5,102
Vehicles, net	6,985	6,162
Tools, furniture and fixtures	3,087,382	3,243,984
Accumulated depreciation and impairment loss	-2,496,759	-2,592,098
Tools, furniture and fixtures, net	590,623	651,885
Land	257,800	257,800
Total property, plant and equipment	1,538,518	1,657,468
Intangible assets		
Other	78,543	75,953
Total intangible assets	78,543	75,953
Investments and other assets		
Investment securities	453,085	486,723
Deferred tax assets	119,561	128,673
Guarantee deposits	2,488,108	2,515,435
Other	131,260	139,722
Allowance for doubtful accounts	-1,488	-4,563
Total investments and other assets	3,190,527	3,265,992
Total noncurrent assets	4,807,588	4,999,414
Total assets	20,084,510	19,717,150

(Thousands of yen)

	Previous fiscal year (August 31, 2017)	Current second quarter (February 28, 2018)
Liabilities		
Current liabilities		
Notes and accounts payable-trade	6,325,286	6,288,626
Short-term loans payable	100,000	100,000
Current portion of long-term loans payable	648,434	653,160
Income taxes payable	349,322	241,199
Accrued consumption taxes	252,300	86,783
Provision for bonuses	168,421	161,493
Provision for directors' bonuses	11,475	—
Other	969,451	738,496
Total current liabilities	8,824,690	8,269,761
Noncurrent liabilities		
Long-term loans payable	771,503	772,695
Liabilities relating to retirement benefits	187,594	199,045
Provision for directors' retirement benefits	12,405	13,751
Provision for directors' stock-based benefits	16,206	20,693
Asset retirement obligations	114,621	117,516
Other	283,836	281,078
Total noncurrent liabilities	1,386,168	1,404,780
Total liabilities	10,210,858	9,674,541
Net assets		
Shareholders' equity		
Capital stock	440,297	440,297
Capital surplus	1,637,636	1,637,636
Retained earnings	8,029,585	8,204,812
Treasury stock	-137,991	-137,991
Total shareholders' equity	9,969,528	10,144,755
Accumulated other comprehensive income		
Valuation difference on available-for-sale securities	26,277	32,793
Foreign currency translation adjustment	-21,377	3,466
Total accumulated other comprehensive income	4,900	36,259
Non-controlling interests	-100,776	-138,406
Total net assets	9,873,652	10,042,608
Total liabilities and net assets	20,084,510	19,717,150

(2) Quarterly Consolidated Statements of Income and Statements of Comprehensive Income
(Quarterly Consolidated Statements of Income)
(Second quarter)

	(Thousands of yen)	
	Previous second quarter (from September 1, 2016 to February 28, 2017)	Current second quarter (from September 1, 2017 to February 28, 2018)
Sales	23,484,918	23,886,905
Cost of sales	14,616,096	14,679,892
Gross profit	8,868,822	9,207,012
Selling, general and administrative expenses	8,224,927	8,613,979
Operating profit	643,895	593,033
Non-operating revenues		
Rent income	11,002	10,742
Equity in earnings of affiliates	15,465	10,863
Foreign exchange gains	26,032	—
Other	13,831	22,905
Total non-operating income	66,332	44,511
Non-operating expenses		
Interest expenses	2,595	2,757
Early-withdrawal penalty	5,507	20,540
Cost of lease revenue	5,430	5,400
Exchange loss	—	1,087
Other	803	5,438
Total non-operating expenses	14,335	35,224
Recurring profit	695,891	602,320
Extraordinary income		
Gain on sales of fixed assets	—	1,034
Surrender value of insurance	287	—
Total extraordinary income	287	1,034
Extraordinary loss		
Loss on retirement of fixed assets	4,680	843
Loss on sales of fixed assets	84	—
Impairment loss	41,649	11,508
Total extraordinary losses	46,414	12,352
Income before income taxes and minority interests	649,765	591,002
Income taxes-current	281,944	230,057
Income taxes-deferred	-73,704	19,228
Total income taxes	208,240	249,286
Net income	441,525	341,715
Net loss attributable to non-controlling interests	-47,923	-37,629
Net income attributable to owners of parent	489,449	379,345

(Quarterly Consolidated Statements of Comprehensive Income)

(Second quarter)

(Thousands of yen)

	Previous second quarter (from September 1, 2016 to February 28, 2017)	Current second quarter (from September 1, 2017 to February 28, 2018)
Net income	441,525	341,715
Other comprehensive income		
Valuation difference on available-for-sale securities	7,592	6,515
Foreign currency translation adjustment	30,164	8,962
Share of other comprehensive income of associates accounted for using equity method	23,889	15,881
Total other comprehensive income	61,646	31,359
Comprehensive income	503,172	373,075
(Breakdown)		
Comprehensive income attributable to owners of parent	551,096	410,705
Comprehensive income attributable to non-controlling interests	-47,923	-37,629

(3) Quarterly Consolidated Statements of Cash Flows

(Thousands of yen)

	Previous second quarter (from September 1, 2016 to February 28, 2017)	Current second quarter (from September 1, 2017 to February 28, 2018)
Net cash provided by (used in) operating activities		
Income before income taxes and minority interests	649,765	591,002
Depreciation and amortization	170,035	169,232
Impairment loss	41,649	11,508
Increase (decrease) in allowance for doubtful accounts	6	1,860
Increase (decrease) in provision for bonuses	11,443	-6,927
Increase (decrease) in provision for directors' bonuses	—	-11,475
Increase (decrease) in liabilities relating to retirement benefits	7,617	11,450
Increase (decrease) in provision for directors' retirement benefits	-78,685	1,345
Increase (decrease) in provision for directors' stock-based benefits	3,908	4,486
Interest and dividends income	-1,293	-2,036
Interest expenses	2,595	2,757
Loss on retirement of fixed assets	4,680	843
Decrease (increase) in accounts receivable-trade	233,803	291,584
Decrease (increase) in inventories	-230,102	-160,888
Increase (decrease) in notes and accounts payable-trade	-14,455	2,433
Increase (decrease) in accrued consumption taxes	106,732	-95,206
Other	-141,119	-204,511
Subtotal	766,582	607,461
Interest and dividends income received	1,266	1,986
Interest expenses paid	-2,072	-1,800
Income taxes paid	-177,494	-329,405
Income taxes refund	—	65,913
Net cash provided by (used in) operating activities	588,282	344,155
Net cash provided by (used in) investing activities		
Purchase of property, plant and equipment	-181,084	-320,812
Proceeds from sales of property, plant and equipment	1,338	1,034
Payments for lease and guarantee deposits	-63,199	-78,283
Proceeds from collection of lease and guarantee deposits	61,434	45,519
Payments for asset retirement obligations	—	-865
Purchase of investment securities	-48,745	—
Other	-29,135	-38,018
Net cash provided by (used in) investing activities	-259,390	-391,425
Net cash provided by (used in) financing activities		
Proceeds from long-term loans payable	599,450	400,000
Repayment of long-term loans payable	-396,418	-394,082
Cash dividends paid	-202,562	-203,144
Net cash provided by (used in) financing activities	469	-197,226
Effect of exchange rate change on cash and cash equivalents	14,825	-9,466
Net increase (decrease) in cash and cash equivalents	344,187	-253,963
Cash and cash equivalents at beginning of period	5,030,891	5,727,607
Cash and cash equivalents at end of period	5,375,078	5,473,644

(4) Notes to consolidated financial statements

(Notes on going concern assumption)

None

(Notes if there is a significant change in the amount of shareholders' equity)

None