KADOKAWA DWANGO CORPORATION

9468 Tokyo Stock Exchange First Section

16-Jan.-17

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Full Fiscal Year Results Forecasts Have Been Upwardly Revised Following a Major Increase in Profits in the Mainstay Publication Business

KADOKAWA DWANGO CORPORATION <9468> (hereafter, also “the Company”) was formed in October 2014 from the merger of major publishing house KADOKAWA CORPORATION and DWANGO Co., Ltd, which manages one of Japan’s largest video community services, “niconico.” The Company is a comprehensive media provider with capability of mega-content publisher and digital content platformer. It has a wide range of businesses, including books and e-books; magazines and advertising; motion picture planning, production, and distribution; video services; mobile content distribution; game software planning, development, and sales; and the provision of online learning services and the operation of vocational schools.

In the FY3/17 1H (April to September) consolidated results, net sales increased 6.2% y-o-y to ¥99,795mn, operating income rose 26.1% to ¥4,419mn, and net income attributable to the owners of the parent company climbed 57.8% to ¥3,020mn, for higher sales and double-digit increases in profits. The main factor was the major increase in profits in the Publication business in addition to favorable performances of e-books and magazines. Paper books exceeded expectations due to recovery in graphic novels, continuous good performance in media-mix titles, and strong sales of the books related to the movie *Your Name* (Japanese title *Kimi no na wa*).

The 1H results exceeded the Company’s expectations, particularly for paper books, and the Company upwardly revised its initial forecasts for both sales and profits for FY3/17 (which were net sales of ¥200,000mn, operating income of ¥3,100mn, and net income attributable to the owners of the parent company of ¥1,750mn), to net sales of ¥202,000mn (up 0.5% y-o-y), operating income of ¥6,000mn (down 34.2%), and net income attributable to the owners of the parent company of ¥4,000mn (down 41.6%).

At FISCO, we think that the Company’s forecasts are conservative in consideration of the following factors. 1) although the delay of a new service for smartphones until FY3/18 is a negative factor in the Web Services business, growth in numbers of monthly fee-paying members for niconico Channel will quicken, and the effects of the renewal of niconico (e.g., higher picture quality) will be realized In the Web Services business; 2)KADOKAWA’s one-company system will stably maintain the high level of profitability in the Publication business; 3)as well as the extra distribution income from the movie *Your Name* becoming a long-running hit, media-mix titles such as *Kantai Collection KanColle* and the TV anime *Bungo Stray Dogs* will contribute in Q3 (October to December) in the Video and Game business.

The Company set the target in its Medium-term Vision of achieving operating income of ¥18bn to ¥20bn in FY3/19. At FISCO, we evaluate that the one-company system stably maintains a high level of profitability in the Publication business, and also that synergies from the management integration are progressing steadily as can be seen from the growth in the novel posting site “Kakuyomu” from which titles will be published, and that the number of onsite and online visitors to “Game Party 2016” exceeded the previous year contributing to the further expansion of the Japanese game market. These developments will coincide with the effects of the active investment to launch new businesses and to change the categories of existing businesses. We think the Company will accelerate its growth, and continue to pay attention to the progress of its active investment.

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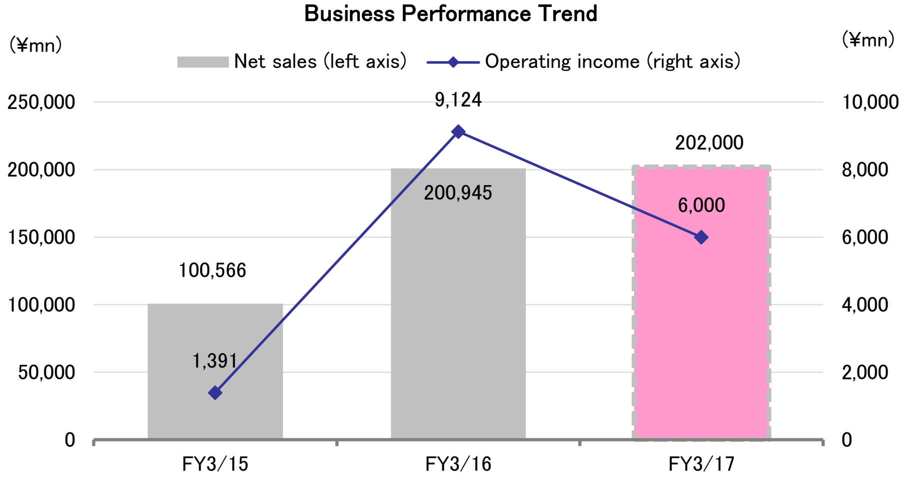
Check Point

- In the FY3/17 1H results, the Publication business recorded a major increase in profits, including the contribution from books related to the movie *Your Name*
- Synergies from the integration are being realized, as can be seen in the novel posting site "Kakuyomu" and "Game Party"
- Although the launch of a new service for smartphones has been delayed in the Web Services business, active investment to launch new businesses and to change the categories of existing businesses is progressing steadily in general.



Note: FY3/15 are provisional calculations for 6 months

Company Profile

Integration of a major publisher and a video service operating company

(1) Company profile

The Company is a joint holding company established on October 1, 2014, through a share transfer. It aims to create and grow new businesses in the fields of game information portals, e-books, and the education business through leveraging synergies with the major publisher KADOKAWA and DWANGO, which is the operator of the leading Japanese video service "niconico." The Company's strengths lie in its ability to create unique services, including editing capabilities honed in the fields of publishing and videos, expertise in developing unique content across multimedia formats to maximize earnings, the generation of original network services based on advanced networking technologies, and the integration of these services with real-world events. It has a wide range of businesses, including books and e-books; magazines and advertising; motion picture planning, production, and distribution; video services; mobile content distribution; game software planning, development, and sales; and the provision of online learning services and operation of vocational schools.

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(2) Company history

The history up to the management integration goes back to October 2010, when KADOKAWA GROUP HOLDINGS, INC. and DWANGO Co., Ltd. formed a comprehensive business alliance for e-books and the distribution of various contents. In May 2011, the relationship progressed to a capital alliance, and in November 2011, they began providing the "KADOKAWA niconico A" service. The relationship between the two companies quickly became closer and they established an advertising joint venture, smiledge Co., Ltd. in March 2013 (liquidated in July 2015) and went as far as the integration in October 2014. On October 1, 2015, the Company name was changed to Kadokawa Kabushiki-kaisha*1 to emphasize management integration both internally and externally (but the English name remains KADOKAWA DWANGO CORPORATION).

In May 2016, the Company acquired equity of 51% of Yen Press, LLC (hereafter, Yen Press)*2, which publishes translations of Japanese manga and graphic novels, and made it a consolidated subsidiary, with the aim of maximizing the growth potential of Japanese content in the North American market.

*1 KADOKAWA is a combination of the Japanese sounds in names of the Group's constituent companies, KADOKAWA and DWANGO ("KA" from KADOKAWA, followed by "DO" from DWANGO, which is pronounced "Do-wan-go" in Japanese, followed by "KA" from KADOKAWA, and "WA" from DWANGO.)

*2 Yen Press is the English language publishing business of manga, graphic novels, and other publications that was spun-off by the Hachette Book Group, a major North American publishing company, in order to establish a joint venture with the Company.

History

	Event
October 2010	DWANGO and KADOKAWA GROUP HOLDINGS entered into a comprehensive business alliance relating to digital books and the distribution of various contents.
May 2011	A capital alliance was concluded between KADOKAWA GROUP HOLDINGS and DWANGO.
November 2011	The KADOKAWA niconico A comic service, collaboration between niconico Douga and BOOK ☆ WALKER was launched.
March 2013	The advertising joint venture smiledge Co., Ltd. was established.
October 2014	KADOKAWA and DWANGO established the joint holding company KADOKAWA DWANGO through a joint share transfer.
October 2015	The Company name was changed in Japanese to Kadokawa Kabushiki-kaisha.
May 2016	Yen Press, LLC (Delaware, the United States) was consolidated (the Company's investment ratio, 51%)

Source: prepared by FISCO based on the Company's website.

History of KADOKAWA

	Event
November 1945	Kadokawa Shoten was founded.
September 1982	The magazine *Weekly the Television* was launched.
March 1990	The magazine *Tokyo Walker* was launched.
November 1998	KADOKAWA SHOTEN was listed on the Second Section of the Tokyo Stock Exchange.
April 2003	KADOKAWA HOLDINGS was established by an incorporation-style company split through the holding-company method.
September 2004	KADOKAWA HOLDINGS was listed on the first section of the Tokyo Stock Exchange.
July 2006	KADOKAWA HOLDINGS changed its corporate name to KADOKAWA GROUP HOLDINGS.
October 2010	Entered a comprehensive business alliance with DWANGO for e-books and the distribution of various contents.
June 2011	Received a third-party allocation of shares of DWANGO for a capital increase.
June 2013	KADOKAWA GROUP HOLDINGS changed its corporate name to KADOKAWA CORPORATION.
May 2014	Concluded an integration agreement with DWANGO.

Source: prepared by FISCO based on the Company's securities report

History of DWANGO

	Event
August 1997	DWANGO was established to plan, develop, operate, and support network game systems, as well as to provide consultations.
April 2001	Established Composite Inc. with the objective of planning, developing, and managing content services for mobile phones.
November 2002	Made Composite Inc. a wholly owned subsidiary to strengthen the cooperation framework for content services for mobile phone users.
July 2003	Listed on the Tokyo Stock Exchange Mothers Market.
September 2004	Listing was transferred to the Tokyo Stock Exchange First Section.
April 2005	Made CHUNSOFT Co., Ltd. a subsidiary
February 2006	Entered into a business and capital alliance with Avex Group Holdings Inc.
May 2008	Collaborated with Yahoo Japan Corporation on "niconicoDouga," a video community service.
October 2010	Entered into a comprehensive business alliance with KADOKAWA GROUP HOLDINGS, INC. for digital books and the distribution of various contents.
June 2011	Conducted a third party allocation of new shares to KADOKAWA GROUP HOLDINGS, INC.
July 2013	Entered a business alliance with Nippon Telegraph and Telephone Corporation.
May 2014	Concluded an integration agreement with KADOKAWA.
December 2014	Made the education business operator Vantan Inc. a wholly owned subsidiary.

Source: prepared by FISCO based on the Company's securities report

Strengths and Business Risks

Realizing integration synergies to maximize profits by developing unique content across multimedia formats

(1) Strengths

The Company's strengths include its ability to create unique services, including editing capabilities honed in the fields of publishing and videos, expertise in developing unique content across multimedia formats to maximize earnings, the generation of original network services based on advanced networking technologies, and the integration of these services with real-world events.

In the Web Services business, various UGC (User Generated Content) is being created on niconico, and its contents-centered community is always active, focused on the users. In addition, in recent years the Company has been using the niconico Channel to enhance its content-development capabilities.

In the Publication business, the Company has a system able to produce publications efficiently from the editing capabilities it has accumulated over many years and also its highly precise marketing and promotions capabilities, while in e-books, it is achieving growth to the extent that BOOK☆WALKER, which it manages itself, has been positioned as the industry platform. Further, the novel posting site "Kakuyomu" has a total number of page views (PV) of approximately 117 million*, and 28,766 titles* have been posted on it. Of these posted titles, 52 are scheduled to be published within the fiscal year, and in such ways, synergies from the management integration are being realized.

* As of the end of September 2016

(2) Business and other risks

Business and other risks can be considered to include the fact that the shrinkage of the paper-based book market or slowdown of rapid growth of e-book market may exceed the Company's expectations in the Publication business, currently its largest earnings pillar.

In addition, if the Company were to lose market share due to the market entry of new players in the Web Services business, expected to be an earnings driver in the future, it could have a negative impact on its earnings.

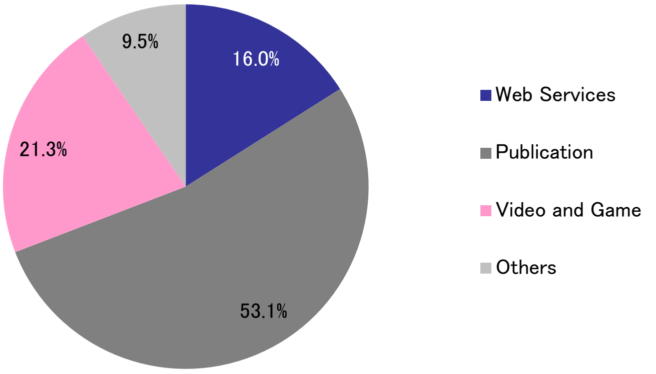
Business Operations

Revised segment classifications in order to clarify the Group's business pillars. Publication and Web Services are the mainstay businesses.

As of the end of September 2016, the Company Group was comprised of 44 consolidated subsidiaries, including KADOKAWA and DWANGO that conduct their businesses under the Company, which is the holding company, and 13 equity-method affiliates. The Group has three business segments, the Web Services business conducted by DWANGO, which mainly involves the provision of the "niconico" video service; the Publication business conducted by KADOKAWA for books, magazines, and other publications; and the Video and Game business for package sales of DVDS and other goods, planning production, and distribution of movies and other broadcasting programs, and also development and sales of games. It also classifies its operations into the Other business segment that includes product sales and the education business*. The percentage of total net sales by segment (to external customers) in FY3/17 1H, is: Web Services 16.0%, Publication 53.1%, Video and Game 21.3%, and Others 9.5%.

* In order to clearly indicate the main business pillars in the Group, from FY3/17 the Company changed its reporting segments to "Web Services" (formerly Portal Business, Live Business, and Mobile Business), "Publication" (Books and IP Business, Information Media Business), "Video and Game" (Video and IP Business, and Game Business), and "Others" (Others and some businesses in Information Media)

Percentage of Net Sales by Segment (FY3/17 1H)



Source: prepared by FISCO based on the Company's financial results summary

(1) Web Services business

Setting DWANGO's video service "niconico" as the core, this business is comprised of live business of planning and operating various kinds of events and leasing event venues, often as a way to promote "niconico," and also a music distribution business for mobile devices.

The Company provides various services on its mainstay "niconico" website, including niconico Video Community, niconico Live, and niconico Channel. Sales include revenues from premium memberships that enable members to watch videos and live feeds comfortably, advertising revenues from website banners and so forth, and also revenues from points used to watch pay-to-view videos. As of the end of September 2016, it had issued IDs to 60.06 million people (66% to males, 34% to females) and it had 2.56 million premium members. Usage conditions in Q2 (July to September) were that there were 9.54 million MAU (monthly active users) and 3.65 million DAU (daily active users). In addition, the "niconico Channel," which is a platform on which companies, organizations, and users can deliver video and live broadcasts, had a total of 7,458 channels, of which 1,056 were monthly-fee channels, and the number of monthly fee-paying members has steadily increased to reach 560,000 people.

In businesses other than "niconico," the Company plans and manages live events such as "niconico Chokaigi,"*1 "Game Party"*2, "Animelo Summer Live," and "niconico Choparty"*3. It also operates the live music venue "nicofarre," a new entertainment format that realizes a fusion of the Internet and the real world, and the niconico showroom "niconico Honsha"*4, which had its grand renewal opening in Ikebukuro, Tokyo, in October in 2014, operating collaboration cafes for limited periods and live game events.

In the music distribution business, although member numbers are trending downward due to the decline in feature phone users and the shift to smartphones, it remains a highly profitable business for the Company. This business operates "dwango.jp," which distributes single songs, ring tones®, and so forth, as well as "animelo (songs from popular anime)."

(2) Publication business

In this business, which is KAGOKAWA's mainstay business, the Company publishes and sells paper-based books, including separate volumes, pocket editions including graphic novels, and comics, as well as e-books. In addition to magazines including Weekly the Television (TV information magazine), Walker Series (Town information magazine), Weekly Famitsu (Game information magazine), and Lettuce Club (Lifestyle Information magazine), and mooks (magazine style books), in this business, the Company also produces custom media such as Weekly Georgia and Hikari TV Guide, as well as selling magazine and Internet advertising.

The paper-based book business is a strong background for developing related products through its media mix strategy, and the Company is an industry leader in graphic novels. It has considerable experience in working to achieve appropriate production and shipping based on marketing, and the rate of product returns in FY3/16 was 35.0%, which was lower than the industry average*5 of 36.9%.

Conversely, the Company sells e-books directly on BOOK☆WALKER, its own e-book distribution platform, also focusing on expanding sales in external e-book stores, such as the Amazon Kindle store, by conducting the "niconico Kadokawa Festival" sales promotion*6 and by releasing new publications in both paper and e-book formats simultaneously.

With the conversion of existing paper media to the Internet and digital formats, revenue from magazine sales has slumped, and the associated decline in advertising sales continues in the industry. To deal with this harsh environment, the Company is streamlining its operations while actively taking steps to transition media from paper-based to digital. In FY3/16, the magazine return rate was 32.7%, lower than the industry average*5 of 41.8%, the same as with books.

(3) Video and Game business

This business includes sales of package software; the planning, production, and distribution of movies; sales of the copyrights to overseas versions of anime; and video distribution. In addition, Kadokawa Daiei Studio Co.and Glovision Inc. are developing studio business. The Company is focusing on visualizing the Group IP generated in the Publication business and the Video and Game business and on producing and distributing live-action films and anime titles. It has also recently been working on video distribution and sales of anime copyright overseas

In this business, the Company's five consolidated subsidiaries, FromSoftware, Inc., Spike Chunsoft Co., Ltd., KADOKAWA GAMES, LTD., MAGES. Inc., and KADOKAWA CORPORATION carry out the planning, development, and sales of packaged game software, network games, and app games. Previous hit titles include Dark Souls, Bloodborne (FromSoftware), Kantai Collection, Derby Stallion GOLD (KADOKAWA GAMES), Kenka Bancho, Danganronpa, Shiren the Wanderer (Spike Chunsoft), and Steins;Gate (MAGES).

(4) Others

Others comprises businesses such as e-commerce sales of character merchandise and pop idol CDs, copyright revenues and sales of CDs featuring content created from anime or "niconico". It also includes an education business involving the operation of schools providing training to work in creative fields inside and outside of Japan, and also online learning services at N high school and other educational facilities.

*1 The largest "niconico" event held at Makuhari Messe with the concept of "recreating everything of 'niconico' on site." All the participating users are the "lead actors" in the various events that integrate the Internet and the real world. The "2016 niconico Chokaigi" event was held on April 29 and 30, 2016, with 152,561 visitors to the venue and a total of 5.548,583 online visitors.

*2 Japan's largest "user participation" game event that features games from analogue to digital and old and new games from the East and West. It was held on January 30 and 31, 2016, at Makuhari Messe, and has grown to a scale of 47,588 site visitors and 6,878,290 online visitors (the 2015 Game Party had 35,786 site visitors and 5,746,338 online visitors), and it is contributing to the expansion of the Japanese game market.

*3 A large-scale stage event for niconico, which is Japan's premium video service. It is niconico's largest live event where popular users on niconico in genres such as "I tried to sing" and "I tried to dance," and also famous artists, gather together and perform. It was held for the fifth time on November 3, 2016, at the Saitama Super Arena, and was attended by approximately 15,000 people.

*4 At the "niconico" pilot shop, a facilities complex of nicocafe, an event space, the nicobukuro studio, and the niconico shop. The grand opening was in Harajuku in April 2011, then transferred to Ikebukuro and renewed.

*5 The sources of the industry indicators are the Publishing Monthly Report and Publishing Yearbook published by the All Japan Magazine and Book Publisher's and Editor's Association and Research Institute for Publications.

*6 It was first held in October 2014 to commemorate the management integration of KADOKAWA and DWANGO, and it has been held every fall since then. Various promotions linking KADOKAWA's contents and niconico's services are implemented, and in addition in 2016 (from October 1 to October 31), a large scale campaign linked to the online shop was carried out.

Results Trends

The Publication business recorded a major increase in profits from the strong performances of e-books and also paper books

(1) Overview of the FY3/17 1H consolidated results

In the FY3/17 1H (April to September) consolidated results, net sales increased 6.2% y-o-y to ¥99,795mn, operating income rose 26.1% to ¥4,419mn, and net income attributable to the owners of the parent company climbed 57.8% to ¥3,020mn, for an increase in sales and double-digits increases in profits.

FY3/17 1H consolidated results overview

(¥mn)

	FY3/16		FY3/17		
	1H result	Sales ratio	1H result	Sales ratio	y-o-y Change
Net sales	93,926	-	99,795	-	6.2%
Cost of sales	66,000	70.3%	70,591	70.7%	7.0%
Gross profit	27,926	29.7%	29,203	29.3%	4.6%
SG&A expenses	24,421	26.0%	24,783	24.8%	1.5%
Operating income	3,505	3.7%	4,419	4.4%	26.1%
Ordinary income	4,203	4.5%	4,011	4.0%	-4.6%
Net income attributable to the owners of the parent company	1,914	2.0%	3,020	3.0%	57.8%

Source: prepared by FISCO based on the Company's financial results summary

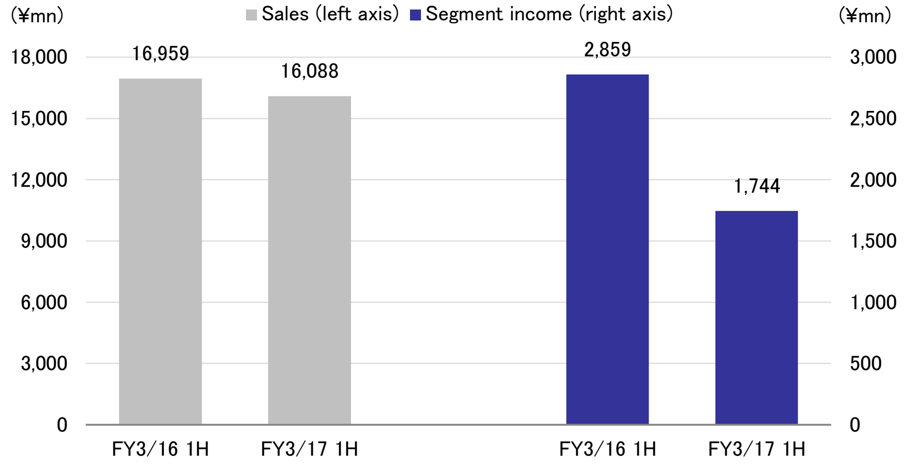
The reasons for the y-o-y increase in net sales were that results trended favorably in the Publication business from the continued strong sales of e-books, e-magazines and media-mix titles, and also the steady performance of the Video and Game business with license revenues from favorable sales of DARK SOULS III in Europe and the United States. Gross profit rose by 4.6% to ¥29,203mn due to the increase in net sales. The Company succeeded in keeping down the increase in SG&A expenses to 1.5% y-o-y, to ¥24,783mn, from the effects of the rationalization from the introduction of the one-company system in the Publication business. The SG&A expenses ratio fell from 26.0% to 24.8%. As a result of the above, a y-o-y increase of 26.1% in operating income was secured and the operating income margin improved by 0.7 of a percentage point to 4.4%. Ordinary income fell 4.6% to ¥4,011mn because of negative factors including donations of ¥749mn and a foreign exchange loss of ¥399mn due to the appreciation of the yen. Tax expenses were kept down by appropriating for tax purposes the loss brought forward from the previous fiscal year, and net income attributable to the owners of the parent company increased 57.8% to ¥3,020mn.

(2) Trends by segment

a) Web Services business

In this business, revenue decreased 5.1% y-o-y to ¥16,088mn and operating income fell 39.0% to ¥1,744mn, for declines in both sales and profits. The main reason for the lower sales was the decline in member numbers in the mobile business, but this result was basically in line with the forecast. On the other hand, operating income declined because in addition to the reduction in income in the mobile business from the lower sales, profits in the portal business were down due to the investment to renew niconico*1 and the costs to develop apps, while profits also fell in the live business as the loss from "niconico Chokaigi 2016" increased. However, the live business achieved profitability in Q2 (July to September) from the contribution of Animelo Summer Live 2016 -TOKI-*2.

Web Services business net sales and segment income



Source: prepared by FISCO based on the Company's financial results briefing materials

b) Publication business

In this business, revenue rose 11.0% y-o-y to ¥53,744mn and operating income increased 304.2% to ¥3,884mn, for higher sales and profits. As planned, e-books and magazines maintained their strong performance from the provision of services tailored to the expansion of market scale, and the strong results in the Publication business drove both the higher revenue and operating income.

Kadokawa's graphic novels and comics performed strongly despite the market for paper books continuing to contract gradually. The main factors behind the improved sales and profits in the Publication Business were that media-mix titles such as *Re: Life in a different world from zero*, *Bungo Stray Dogs*, and *KONO SUBARASHII SEKAI NI SYUKUFUKU WO! (God's Blessing on This Wonderful World)* maintained their favorable results, while sales of books relating to the movie *Your Name* exceeded expectations. Conversely, for paper magazines, the Company is developing an incubation business utilizing the resources and the expertise it has cultivated in the magazine business so far, and it is currently in the process of converting the business structure.

*1 From August 18, the Company increased the maximum size of the video file that could be posted onto "niconico Video Community" from the previous 100MB (premium members) to 1.5GB. From November 1, it began offering the "New Delivery (β)" service, in which users can distribute and view high definition video of niconico live broadcasts at 1Mbps. In addition, it released the niconico live broadcast delivery app (from October) and the niconico channel app (from November 11).

*2 Held for 3 days, from August 26 to 28, at the Saitama Super Arena. The total number of site visitors over the 3 days was 81,000 people.

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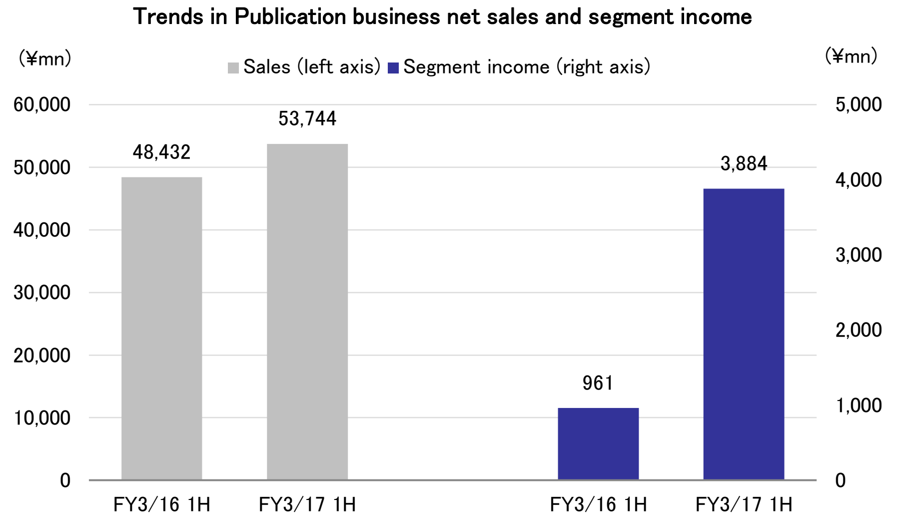
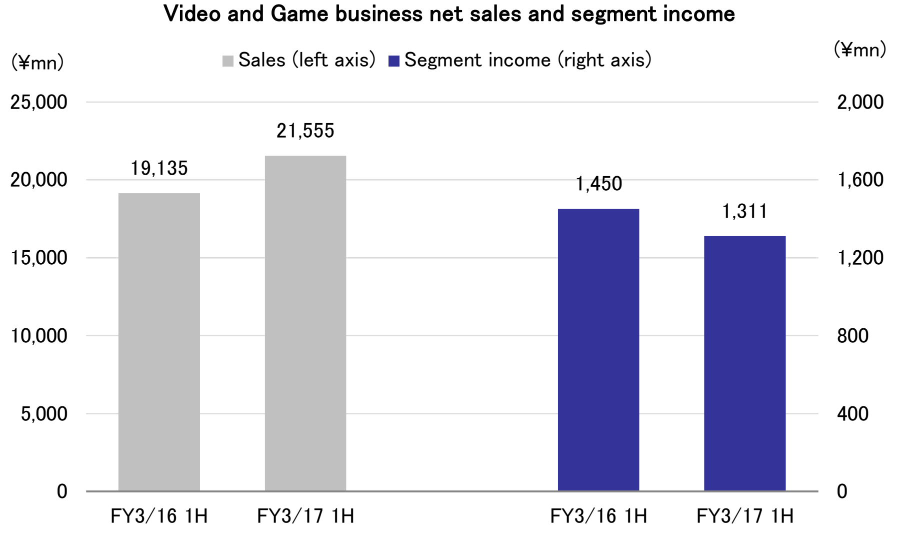


Source: prepared by FISCO based on the Company's financial results briefing materials

c) Video and Game business

In this business, revenue increased 12.6% y-o-y to ¥21,555m, but operating income decreased 9.6% to ¥1,311mn. The reasons for the higher sales were mainly 1) continuous licensing income from the strong sales of *DARK SOULS III* in Europe and the United States in games 2) expansion of overseas license business including anime video distribution, and 3) increase in program-production sales. Segment income declined because the sizes of the video-package hit titles were small compared to those in the previous fiscal year.



Source: prepared by FISCO based on the Company's financial results briefing materials

d) Others

In this business, revenue fell 8.6% to ¥9,925mn and the operating loss was ¥587mn (compared to operating income of ¥71mn in the previous fiscal year). In addition to the slump in sales of trading cards, the amount invested in new businesses, including the inbound demand business and the education business seemed to be the reason for the negative operating income.

List of results by segment

(¥mn)

	FY3/16 1H results		FY3/17 1H results		Change		Change (%)	
	Revenue	Operating income	Revenue	Operating income	Revenue	Operating income	Revenue	Operating income
Consolidated total	93,926	3,505	99,795	4,419	5,868	914	6.2%	26.1%
Web Services	16,959	2,859	16,088	1,744	-871	-1,115	-5.1%	-39.0%
Publication	48,432	961	53,744	3,884	5,312	2,923	11.0%	304.2%
Video and Game	19,135	1,450	21,555	1,311	2,419	-139	12.6%	-9.6%
Others	10,858	71	9,925	-587	-933	-658	-8.6%	-
Corporate / eliminations	-1,459	-1,837	-1,517	-1,933	-58	-96	-	-

Source: the Company's financial results briefing materials

The equity ratio has been maintained at around 40% despite an increase in long-term borrowing

(3) Financial position

Looking at the balance sheet, at the end of September 2016, total assets were up ¥31,990mn compared to the end of the previous fiscal year to ¥233,599mn. Breaking this down, current assets increased ¥29,562mn to ¥161,389mn and non-current assets also rose ¥2,429mn to ¥72,210mn. The increase in current assets was because cash and deposits climbed by ¥35,834mn due to income from the long-term debt although accounts receivable fell by ¥5,775mn. Non-current assets were higher, mainly due to an increase in intangible non-current assets of ¥1,719m from a rise in goodwill of ¥647mn following Yen Press being made into a consolidated subsidiary.

Total liabilities were up ¥30,135mn compared to the end of the previous fiscal year to ¥127,218mn. This was because although current liabilities decreased ¥9,387mn to ¥52,027mn, non-current liabilities increased ¥39,523mn to ¥75,146mn. Current liabilities were down, mainly due to decreases in trade debt of ¥3,819mn and a provision for returned goods of ¥1,315mn. Conversely, non-current liabilities increased because long-term debt rose ¥38,960mn from the end of the previous fiscal year after the Company conducted long-term borrowing in August*.

Net assets were up ¥1,854mn compared to the end of the previous fiscal year to ¥106,381mn. This was because the negative factors, of decreases in the capital surplus of ¥1,186mn due to dividend payments, and in the other comprehensive income accumulated total of ¥397mn from a fall in the foreign currency-adjustment account on the appreciation of the yen, was exceeded by the positive factor, of the increase in retained earnings of ¥2,795mn on the recording of net income attributable to the owners of the parent company.

Looking at cash flow conditions, at the end of September cash and cash equivalents had increased ¥35,791mn from the end of the previous fiscal year to ¥87,966m. Cash flow from operating activities was ¥2,081mn, as although there were negative factors, including decreases in purchase liabilities of ¥3,707mn and advances received of ¥2,477mn, these were offset by the positive factors, including a reduction in accounts receivable of ¥5,728mn and the recording of net income before income taxes of ¥4,002mn. Cash flow used in investing activities was ¥3,515mn due to spending to acquire tangible non-current assets (¥1,965mn) and intangible non-current assets (¥1,091mn), and also spending of ¥1,039mn to acquire equity in a subsidiary following a change in the scope of consolidation. Cash flow from financial activities was ¥37,998mn, mainly due to the income from the long-term borrowing.

Looking at the management indicators, the equity ratio, which indicates financial soundness, fell from 51.4% at the end of the previous fiscal year to 44.9% due to the long-term borrowing. But the current ratio improved, from 214.5% to 309.9%, as while current assets rose following the increase in cash and deposits from the long-term borrowing, current liabilities fell due to the decline in trade debt and other items. The D/E ratio also climbed, from 28.3% to 65.2%, due to the impact of the long-term borrowing, but this is not a level considered to be a problem. Conversely, the operating income margin, which indicates profitability, improved from 3.7% to 4.4%, reflecting the favorable 1H results following the strong performance of the Publication business.

* The Company utilized the low interest rate environment, in which interest payments are lower than the fees for the commitment line agreement, to conduct borrowing of ¥15,000mn (loan period, 7 years, interest rate: base rate + spread) so that it could secure long-term working capital. In addition, KADOKAWA also reviewed its existing borrowing of ¥10,000mn and commitment line agreement (upper-limit amount, ¥15,000mn), and with the aim of reducing monetary expenses, carried out prepayment and cancellation of the commitment line agreement and conducted borrowing of ¥25,000mn (same conditions as the Company).

Balance Sheet, Cash Flow Statement, and Management Indicators

• Consolidated Balance Sheets (¥mn)

	FY3/15	FY3/16	FY3/17 1H	Change	Change factor
Current assets	131,200	131,827	161,389	29,562	Cash and deposits +35,834, Inventory assets +172, Accounts receivable -5,775
Non-current assets	74,473	69,781	72,210	2,429	Tangible non-current assets +670, Other investment assets +41, Intangible non-current assets +1,719 (of which, goodwill +647)
Total assets	205,673	201,609	233,599	31,990	
Current liabilities	63,316	61,459	52,072	-9,387	Short-term debt +176, Trade debt -3,819, Provision for returned goods -1,315
Non-current liabilities	38,108	35,623	75,146	39,523	
Total liabilities	101,425	97,082	127,218	30,135	Long-term debt +38,960
(Interest-bearing debt)	31,598	29,376	68,439	39,063	
Net assets	104,248	104,526	106,381	1,854	Retained earnings +2,795, Capital Surplus -1,186, Other comprehensive income accumulated total -397
Total liabilities and net assets	205,673	201,609	233,599	31,990	

• Cash Flow Statement

	FY3/15	FY3/16	FY3/17 1H	Change
Cash flow from operating activities	7,765	6,733	2,081	
Cash flow from investing activities	-9,049	-4,673	-3,515	
Cash flow from financing activities	24,385	-8,775	37,998	
Cash and cash equivalents	59,201	52,175	87,966	35,791

• Management indicators

	FY3/15	FY3/16	FY3/17 1H
Stability			
Current ratio	207.2%	214.5%	309.9%
Equity ratio	50.2%	51.4%	44.9%
D/E ratio	30.6%	28.3%	65.2%
Profitability			
ROE	22.5%	6.6%	-
ROA	2.1%	5.0%	-
Operating income margin	1.4%	4.5%	4.4%

Source: prepared by FISCO based on the Company's securities report

Results forecasts have been upwardly revised, reflecting the strong performance of the Publication business in 1H

(4) FY3/17 Outlook

a) Overview of the Company targets

The 1H results exceeded the Company's expectations, particularly for paper books, and based on this it upwardly revised its initial forecasts for both sales and profits for FY3/17 (which were net sales of ¥200,000mn, operating income of ¥3,100mn, and net income attributable to the owners of the parent company of ¥1,750mn), to net sales of ¥202,000mn (up 0.5% y-o-y), operating income of ¥6,000mn (down 34.2%), and net income attributable to the owners of the parent company of ¥4,000mn (down 41.6%).

Overview of the FY3/17 Company Targets

(¥mn)

	FY3/16		FY3/17				
	Result	Sales ratio	Initial target	Revised target	Sales ratio	y-o-y Change (%)	vs. initial target
Net sales	200,945	-	200,000	202,000	-	0.5%	101.0%
Cost of sales	141,144	70.2%	-	-	-	-	-
Gross profit	59,801	29.8%	-	-	-	-	-
SG&A expenses	50,676	25.2%	-	-	-	-	-
Operating income	9,124	4.5%	3,100	6,000	3.0%	-34.2%	193.5%
Ordinary income	10,189	5.1%	3,300	5,800	2.9%	-43.1%	175.8%
Net income attributable to the owners of the parent company	6,845	3.4%	1,750	4,000	2.0%	-41.6%	228.6%

Source: prepared by FISCO based on the Company's financial results summary

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The main reasons why the Company upwardly revised its forecasts for net sales by ¥2,000mn and operating income by ¥2,900mn were that the 1H results exceeded its expectations, with the driving force being the strong performance of paper books, including the favorable sales of media-mix titles. In 2H, although there will be reversals in each segment for both sales and profits, taken as a whole the values have been basically kept unchanged from the targets at the beginning of the period.

Active investment for continued growth in the future, which will be a factor reducing results in FY3/17, was progressing basically as planned in 1H, and there has been no change to the plan of annual new investment of ¥4,650mn (the amount that will impact the income statement; increased ¥3,380mn y-o-y). The specific content of the investment will be the following seven; 1) the renewal of "niconico" (to display high definition images and reconstruct infrastructure), 2) a new service for smartphones, 3) conversion of business model in magazines, 4) the inbound-demand business, 5) a game information portal, 6) online learning services, and 7) enhancing the UGC-type novel posting website.

b) The revisions to the Company targets by segment

Looking specifically at the revisions to the Company targets by segment, in the Web Services business, the initial target of revenue of ¥32,000mn (down 3.4% y-o-y) has been left unchanged, while the operating income has been revised to ¥2,500mn (down 46.1%), which is a downward revision of ¥200mn compared to the initial target. This was as a result of the Company considering both the negative factors, delay of the release of a new service for smartphones until FY3/18 and the pessimistic outlook for sponsorship income in the live business, and the positive factor, a steady increase in the number of niconico Channel members (the total number of registered members of paid-for channels exceeded 500,000 at the end of May 2016 and had reached 560,000 by the end of September).

For the Publication business, the Company revised targets incorporating the strong performance of e-books and magazines, and paper books exceeding the plan in 1H. Taking the profitability improvement from the effects of the integration of the publishing companies within the Group and the establishment of the one-company system into account additionally, it upwardly revised revenue target by ¥2,000mn to ¥109,000mn (up 3.6% y-o-y) and operating income target by ¥2,500mn to ¥6,900mn (up 9.3%).

In the Video and Game business, the initial revenue target of ¥44,000mn (down 0.6% y-o-y) has been left unchanged, but the operating income target has been upwardly revised ¥700mn to ¥3,200mn (down 11.5%). The main factors were that the movie *Your Name*, in which KADOKAWA invested as a member of the production committee, was a bigger hit than expected, and therefore the distribution income from the movie has increased as it became a long-running hit.

In Others, the initial target for revenue of ¥20,000mn (down 6.3% y-o-y) has been left unchanged, but the operating loss has been downwardly revised to ¥1,600mn. This is mainly because of the hampered sales of trading cards. In addition, in Corporate and Eliminations, expenses are expected to decrease in the general administrative department due to the progress made in rationalization, including the effects of the integration. Therefore, its target has been upwardly revised ¥200mn, from negative ¥5,200mn to ¥5,000mn.

Net sales and segment income targets by segment

(¥mn)

	FY3/16 Full-year results		FY3/17 Full-year results — initial forecasts		FY3/17 Full-year results — revised forecasts		Revised amount	
	Revenue	Operating income	Revenue	Operating income	Revenue	Operating income	Revenue	Operating income
Consolidated total	200,945	9,124	200,000	3,100	202,000	6,000	2,000	2,900
Web Services	33,136	4,638	32,000	2,700	32,000	2,500	-	-200
Publication	105,199	6,282	107,000	4,400	109,000	6,900	2,000	2,500
Video and Game	44,284	3,614	44,000	2,500	44,000	3,200	-	700
Others	21,340	-1,011	20,000	-1,300	20,000	-1,600	-	-300
Corporate / eliminations	-3,015	-4,399	-3,000	-5,200	-3,000	-5,000	-	200

Source: the Company's financial results briefing materials

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At FISCO, we think that the Company's forecasts are conservative in consideration of the following factors. 1) Although the delay of a new service for smartphones until FY3/18 is a negative factor in the Web Services business, the pace of growth is accelerating for the niconico Channel, and the effects of the renewal of niconico (e.g., higher image quality) will be realized; 2) in the Publication business, one-company system will continue to stably improve profitability; 3) in the Video and Game business, as well as the distribution income from the movie *Your Name* becoming a long-running hit, in Q3 (October to December), contributions to revenue can be expected from *Kantai Collection KanColle* and *Satoshi: A Move for Tomorrow*, and strong sales of media-mix titles, such as *Bungo Stray Dogs, Brave Witches*, and *BUBUKI/BURANKI: The Gentle Giants of the Galaxy* broadcasted as TV anime in the quarter.

■ Medium-term Vision

Aiming for operating income of ¥18,000mn to ¥20,000mn in FY3/19

In May 2015, the Company announced its Medium-term Management Plan (FY3/16−FY3/18 Medium-term Vision - Toward New Challenges and Growth Markets). In the plan, it positioned FY3/16 as a year to actively invest in new businesses and services, FY3/17 as a year to develop these investments, and FY3/18 as the year to recoup the investment, setting targets for this fiscal year of net sales of ¥230,000mn and operating income of ¥18,000mn to ¥20,000mn. Specifically, the plan has four basic strategies for business expansion; (1) growth of the Books and IP Business, (2) growth of the game information portal business, (3) growth of the Portal Business, and (4) entry into the educational business*.

* Changes to segments are not reflected

As a result of the active investment in FY3/17, the position of FY3/17 was changed from an investment-development period to a period to continue to actively invest in new businesses and services, the same as FY3/16. Therefore, the Company announced that it had changed the period to achieve the targets in the Medium-term Vision from FY3/18 to FY3/19, postponing the schedule by 1 year.

At FISCO, we evaluate the content of the current results that it is clear a high level of profitability is being stably maintained from the one-company system in the Publication business, and also that synergies from the management integration are progressing steadily, as can be seen from the growth in the novel posting site "Kakuyomu" and that the number of site visitors and online visitors to "Game Party" exceeded the previous year and it is contributing to the further expansion of the Japanese game market. These developments will coincide with the effects of the active investment to launch new businesses and to change the categories of existing businesses, and we think that the Company's pace of growth will accelerate. Therefore, we will continue to pay attention to the progress made in the active investment.

Returns to Shareholders

Considers returns to shareholders to be an important management issues and pays dividends in consideration of results in the fiscal period

The Company's first priority is to ensure the continuity of its business management by building up internal reserves to strengthen the corporate constitution and to prepare for future business development. It also considers it important to sustainably distribute profits to shareholders and other stakeholders, and recognizes that returning profits to shareholders is an important management issue. It takes into account the business performance of each period when deliberating on shareholder returns.

The Company plans to continue to pay a dividend of ¥20 per share in FY3/17, the same as in FY3/16 (for a dividend payout ratio of 33.9% compared to 20.2% in FY3/16). It has also introduced a shareholder reward system. Shareholders who hold 100 shares or more continuously for one year or more (shareholders listed at least three consecutive times in the shareholders' register) are given a gift of either three paperbacks, three comics, two separate volumes, two movie tickets, 3,000 e-book purchase points, a DVD or Blu-ray Disc, or one niconico item from one of the Company's subsidiaries. It has also introduced a system to reward long-term shareholders, with shareholders who have held their shares for three years or more (shareholders listed at least seven consecutive times in the shareholders' register) receiving an additional gift of either two paperbacks, two comics, one separate volume, one movie ticket, or 1,500 e-book purchase points from one of the Company's subsidiaries.

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