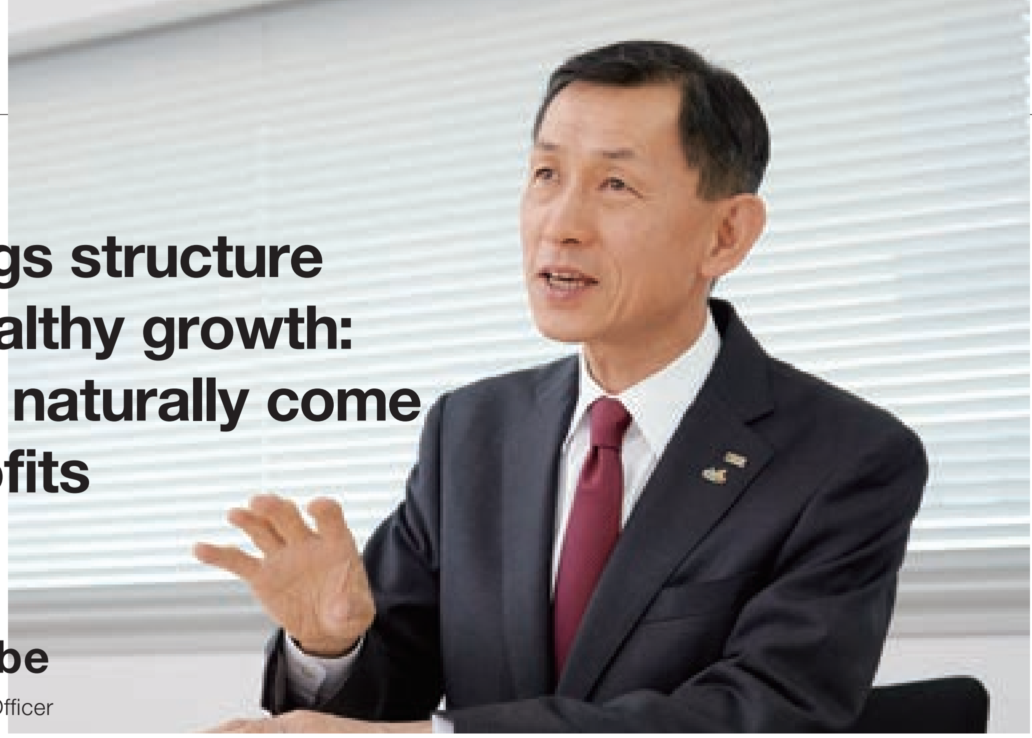
Reform earnings structure and aim for healthy growth: Stronger sales naturally come with better profits



Yoshihide Watanabe
Director & Senior Managing Executive Officer

Review of the First Mid-Term Management Plan (2016-2018)

Overview

The domestic processed food business managed to produce great results thanks to earnings structure reforms. The biggest contributor to its sales growth was the Yasai Seikatsu 100 Smoothie. The product tapped into demand for "filling snacks" and created a new market. Its success was largely credited to the successful launch of the Green Smoothie first and foremost, then the popularity of the 330ml size carton with a cap, and the successful proposal of a new drinking scenario which tapped into demand among consumers who prefer to have their breakfast at their office desks.

An initiative that contributed significantly to profit growth was a review of unprofitable products based on a top-down approach. In-store consumer products require physical shelves, which means that products that do not sell inevitably end up being eliminated. However, institutional and industrial products are free from physical shelves that limit the number of items. Consequently, the number of items tended to increase regardless of sales trends. Roughly speaking, our revenue structure is such that consumer products account for around 20% of the total number of items and around 80% of total net sales and institutional and industrial products account for around 80% of the total number of items and around 20% of total net sales. Due to industrial and institutional products that made a relatively minor contribution in terms of net sales, our plant production system was sometimes overstretched. Inventories of these products then led to waste because they had to be destroyed if there were no orders before the shipping deadline and we used to have several products with negative marginal income. To address this situation, we conducted a review of unprofitable products, coming up with various ideas such as consolidating similar products in consideration of customers. As a result, profitability improved significantly. Whilst always putting the customer first, we carefully examined our unprofitable operations. This led to a reduction in the volume of operations, which was also helpful for work style reforms.

Meanwhile, earnings structure reforms in the domestic agri-business and international business lagged behind. The agri-business performed fairly well in 2016. In hindsight, tomato prices remained high in that year, which drove up profits. We misjudged that higher profits were attributable to Kagome's capability and that a larger supply of tomatoes would lead to better earnings. This is why we suffered from our lackluster performance in 2017 and 2018. When market conditions subsequently declined and tomato prices fell, the agri-business also fell into the red. We concluded that this slump was a cyclical problem in 2017. And honestly, in 2018, we had groundless optimism in our company, assuming that we should make some efforts to help ourselves but prices would turn around. The essence of the problem is that we were slow in preparing for the worst and when we should have been carrying out fundamental checks, including checking up on the state of our competitors, we neglected to do so.

Also, the agri-business performance had been driven by Kagome's strong sales capability underpinned by the strength of our relationships with mass retailers all over Japan. We should have considered that the great results in 2016 came as marketing activities leveraging the sales capability culminated in the year.

With this kind of approach, we will not be able to respond to future market trends. We have been constantly engaged in the development of fresh tomatoes for 20 years, but only recently have we recognized the necessity to tackle issues that should have been addressed in the past two decades, such as developing more tasty tomatoes and controlling supply and demand. When goods increase in volume, consumer needs become more sophisticated. We have been doing things right in front of us but have been underprepared in the longer term, failing to ask ourselves "what do we do next?"

In 2014, we launched an initiative to stabilize earnings by branching out into baby leaf lettuce in addition to our tomato business. The question of how to put the baby leaf lettuce business on track whilst preparing for the future poses a major challenge.

The international business is basically in a similar situation to the agri-business. The frameworks optimized in the domestic processed food business could not be applied to the international business without modification and there were also issues with the decision-making framework. In particular, there is room for improvement in terms of the management structure, i.e., the management exercised by Kagome's head office in Japan. We should sincerely reflect on the fact that we ended up showing too much respect for local autonomy and created a situation that prevented head office from providing sufficient guidance. Our overseas subsidiaries carry out preliminary processing of agricultural raw materials locally but we failed to give local businesses sufficient guidance and advice in areas such as financial considerations, including profitability, and quality assurance, i.e., food safety and security.

To address these issues, we need to strengthen collaboration between overseas subsidiaries and the head office, gain a real time understanding of their situation and instruct them to adopt a multifaceted approach. One such measure is our initiative where we are dispatching finance and accounting personnel from the head office and ensuring compliance with global quality management standards to strengthen monitoring and control by head office. If we successfully manufacture high quality products through these initiatives, our sales and profits are sure to grow.

For the future development of the international business, it is important to ensure quality that meets customer requirements. In our manufacturing activities, we will pursue quality products tailored to various needs of consumers in regions around the world.

Strategies for improving profit in the domestic processed food business

Progress is being made as planned in terms of the management of marginal income and the breakeven point ratio, which was a focus of our efforts in our earnings structure reforms. We are focusing on the efficient use of sales promotion costs and advertising expenses and on the reduction of logistics costs by expanding the joint delivery framework at five domestic food companies as part of our review of freight charges. Logistics needs are becoming more and more sophisticated, and while the "logistics style reform" including two-day delivery and regular delivery is necessary, we are cutting back on the logistics costs of individual companies through the joint delivery system. In our review of unprofitable products, we decide on the number of product items to be discontinued at the beginning of the year, and fewer unprofitable products set the bar higher year after year. We are, therefore, taking action to improve total productivity, in other words, we are not simply reducing products with negative marginal income but also improving the operational level and operating rate of our plants.

Balance Sheet Changes

ROE stood at 11.3% for the fiscal year ended December 31, 2018. A breakdown of the figure shows that the income ratio was 5.49%, the total asset turnover ratio was 1.08, and the financial leverage ratio was 1.91. The total asset turnover ratio has exceeded 1.0 for the last three years and the financial leverage ratio has improved compared with the previous level of over 2.0.

In terms of asset efficiency, in-house manufacturing and outsourced manufacturing affect the balance sheet in different ways. Given that in-house manufacturing is also necessary because of its advantages in terms of profitability, etc., we intend to proceed systematically with a certain level of capital investment. This may cause the total asset turnover ratio to fall temporarily but our intention is to increase ROE by improving profitability.

As for inventory, there is still room to improve efficiency. Due to our business structure, tomatoes to sell the following year pile up from August through October and we tend to have too much inventory at the end of the fiscal year. There are two types of tomato inventory: inventory for use as raw materials in Japan and inventory for sale overseas. We are in the process of strengthening our sales capabilities to sell out inventory at overseas bases and are examining introducing Vendor-Managed Inventory in Japan. The way we stock inventory can be improved in terms of types of contracts with customers.

Investment securities decreased significantly from 22.4 billion yen at the end of the fiscal year 2017 to 10.4 billion yen at the end of the fiscal year 2018. As specified in our Corporate Governance Report, we have established clear standards. The clear standards get rid of unnecessary discussions and lead us to a conclusion automatically, which also benefits the work style reform.

Financial Strategies under the Second Mid-Term Management Plan (2019-2021)

Our Goal

Based on the policies of "reforming our earnings structure" and "taking on the challenge of entering new businesses and domains," we are acutely aware of "healthy sales growth." Over the past few years, our sales have been treading water at around 200 billion yen. To achieve sales of 250 billion yen, developing the ability to sell out all our products is essential, and it is important to translate capital investment and research and development expenses into sales. Our net sales target for fiscal year 2019 is conservative. For fiscal year 2020 and fiscal year 2021, we have strategically set ourselves a target compound annual growth rate of 5% or more. Given that the compound annual growth rate of our net sales over the past five years is 1.7%, this 5% target is extremely ambitious.

Whilst our profit target for fiscal year 2021 in our domestic processed food business is modest, I believe that there is still room for improvement through marginal income-based management. As the marginal income-based management of individual customers is being implemented, the number of success stories is also increasing, and we are also sharing best practices internally. Meanwhile, we plan to pass along higher logistics expenses, raw materials prices and other costs to selling prices where necessary and we have already decided to raise prices of certain products from July 1. However, this alone will not be enough. To persuade customers to continue choosing Kagome products out of many products available, we will continue focusing on enhancement of product value and product development.

On the other hand, our profit targets for the agri-business and international business are aggressive but, in my view, achievable provided we succeed in realizing our intrinsic capabilities. It is also true, though, that I am still slightly unsure about achieving the targets, judging from the past progress. I intend to ensure the targets are met through increased monitoring granularity in precision and frequency as well as through meticulous and bold business execution.

Our Approach on Investment

Our current Mid-Term Management Plan will see expanded capital investment. However, this investment is mainly to upgrade outdated facilities in Japan and is necessary for better production efficiency. Our target for return on investment is set at a payback period of four years for capital investment and IRR exceeding the hurdle rate for business investment. The hurdle rate is set at 10%, a combination of our WACC calculated at 4 to 5% and a risk premium. The hurdle rate also takes country risk into consideration. Whilst exceeding the rate is one standard, at the same time we also attach importance to the potential of business plans, and striking a balance is important.

We are also considering adopting a policy on the allocation and prioritization of investments in property, plant and equipment, and intangible assets as well as adopting KPIs for measuring their impact and progress. Vital for this are management's views on important issues (materiality). We are in the process of identifying important issues (materiality) and our Mid-Term Management Plan is being reviewed on a rolling basis every year. In the meantime, we will continue with the identification of important issues (materiality) toward 2020 and also organize our views on the allocation of investments to intangible assets.

Uses of Free Cash Flow and Shareholder Returns

We are currently reviewing the way in which we use free cash flow and our views on shareholder returns. Over the three years of the Mid-Term Management Plan (2019-2021), we will make available for dividend the cash flows from operating activities less capital investment. While maintaining stable dividends, we will also examine shifting to an approach that shows greater awareness of the total return ratio, including examining share buybacks if we have surplus free cash flow.

We now have all the pieces needed to complete the puzzle of "achievement of the long-term vision." What matters for Kagome's future management is where to start fitting these pieces into the puzzle.

Kagome values are autonomy and upfront characteristics.

Since we have never been a company where employees just do as they are told, we will continue moving forward as an "open company," both internally and externally.

Issues to Be Addressed and Measures in Fiscal Year 2019

One of the main factors that push down profits in the domestic processed food business is the negative effect of currency fluctuations. We import a great deal of raw materials from overseas and have traditionally hedged long-term currency exposures in some transactions in order to stabilize management and make forecasts. This fiscal year, hedges implemented when the yen weakened dramatically in the past will expire and this is expected to negatively impact on our performance compared with the previous fiscal year. We must also take such cost increases into consideration, but more significant than this issue is healthy sales growth. What matters is how we grow sales from those in 2019, and after we complete our earnings structure reform that lags one year behind in the agri-business and international business, sales will grow and profits will follow suit. Accomplishing this is one of the issues that needs to be addressed in the current fiscal year.

Importantly, the agri-business needs to make up for the first quarter and regain lost ground. We will do everything we can, including buying and selling tomatoes on the market, for example. In the international business, we are taking action to ensure that we attain the budget for the current fiscal year so as to turn overseas subsidiaries to profitability, while always preparing backup plans to take second and third steps just in case.

Financial Strategies for Achievement of the 2025 Targets

We now have all the pieces necessary to achieve our long-term vision. Likened to a jigsaw puzzle, the question of where we should start completing the puzzle is important. Kagome has only fit pieces into places next to already completed parts. This approach only allows for slow progress toward completing the puzzle. If we find a shiny piece, we should fit the piece even though it does not border the places already completed. This forms the core of highly profitable businesses. I believe that if we link the businesses we have now with these highly profitable businesses, everything will work out fine.

In our view, future M&A is just one of the means, not a premise, for growth, considering growth until 2025. If there is a brilliant company that fits our jigsaw, we will flexibly respond, examining whether we partner with the company in the form of M&A or alliance and how the partnership will benefit each other.

In addition, we have realized the importance of engagement through our IR activities. Listening to home truths from outside stops management from becoming complacent and enables us to see our true reflection in the mirror. The same holds true to engagement with External Directors. We have boosted our engagement activities out of a desire to share Kagome's appeal with institutional investors as well as individual investors, who already rate us highly. One manifestation of the autonomy which Kagome values is that we are upfront. In the future, we intend to continue moving forward as an "open company" both externally and internally.

Operating Results and Financial Analysis (Fiscal Year 2018)

Conditions of Earnings and Profits

Net sales

Net sales decreased by 4,344 million yen (a decrease of 2.0%), to 209,865 million yen, compared with 214,210 million yen for the previous consolidated fiscal year. Net sales for the previous consolidated fiscal year included net sales of 5,951 million yen of Preferred Brands International, Inc., which was sold in the previous consolidated fiscal year, and we failed to achieve sufficient revenue growth to offset the net decrease in the net sales of Preferred Brands International, Inc.

The domestic processed food business posted a sales increase of 83 million yen (an increase of 1.0%) year on year, reflecting strong sales in our core beverage business, including Yasai Seikatsu 100 Smoothie and tomato juice, and in our direct marketing business, which offset decreased sales of institutional and industrial consigned products.

Meanwhile, our domestic agri-business and international business saw lower-than-expected growth due to the delayed response to environmental changes.

Cost of sales and gross profit

The cost of sales for the consolidated fiscal year under review decreased by 2,521 million yen (a decrease of 2.1%), to 115,216 million yen, compared with 117,738 million yen for the previous consolidated fiscal year. The cost of sales ratio improved by 0.1 points, from 55.0% in the previous consolidated fiscal year to 54.9%. The cost of sales ratio worsened owing to a variety of factors: defects with manufacturing equipment newly introduced at Kagome Inc. (in the U.S.), a major subsidiary in the international business; a decline in the selling price of tomato paste at Holding da Industria Transformadora do Tomate, SGPS S.A. (in Portugal) due to sluggish market conditions; and detractors in the domestic agri-business such as weaker market prices throughout the first half, the peak period for our mainstay fresh tomatoes, than in the previous consolidated fiscal year as well as a slow response to market oversupply. However, the deteriorated cost of sales ratio was offset by the significant contribution of lower costs in the domestic processed food business, and consequently the cost of sales ratio improved from the previous consolidated fiscal year.

As a result, gross profit for the consolidated fiscal year under review was 94,649 million yen, decreasing 1,823 million yen (a decrease of 1.9%) compared with 96,472 million yen for the previous consolidated fiscal year.

Selling, general and administrative expenses and operating income

Selling, general and administrative expenses for the consolidated fiscal year under review decreased by 1,854 million yen (a decrease of 2.2%), to 82,648 million yen, compared with 84,503 million yen for the previous consolidated fiscal year. The ratio of selling, general and administrative expenses to net sales was 39.4%, unchanged from the previous consolidated fiscal year, reflecting the effective use of sales promotion costs, against a backdrop of strategic investment in advertising expenses and continued increase in freight costs and storage charges in Japan.

As a result, operating income for the consolidated fiscal year under review increased by 31 million yen (an increase of 0.3%), to 12,000 million yen, compared with 11,968 million yen for the previous consolidated fiscal year, achieving a record high for third consecutive year.

The ratio of operating income to net sales was 5.7%, improved by 0.1 points from 5.6% in the previous consolidated fiscal year.

Other income or loss and ordinary income

Other income for the consolidated year under review decreased by 505 million yen, to 1,053 million yen, compared with 1,559 million yen for the previous consolidated fiscal year. This was mainly because, in the previous consolidated fiscal year, we recorded a valuation gain of 391 million yen due to fluctuation in the market value of company-owned derivatives (compared with a valuation loss of 28 million yen in the consolidated fiscal year under review).

Other expenses for the consolidated fiscal year under review increased by 92 million yen, to 1,002 million yen, compared with 910 million yen for the previous consolidated fiscal year.

As a result, ordinary income for the consolidated fiscal year under review decreased by 566 million yen (a decrease of 4.5%), to 12,051 million yen, compared with 12,618 million yen for the previous consolidated fiscal year.

The ratio of ordinary income to net sales was 5.7%, a deterioration of 0.2 points from 5.9% for the previous consolidated fiscal year.

Extraordinary gain or loss

Extraordinary gain for the consolidated fiscal year under review increased by 1,466 million yen, to 6,056 million yen, compared with 4,590 million yen for the previous consolidated fiscal year. We recorded a gain on sales of fixed assets of 1,482 million yen because, in the consolidated fiscal year under review, we sold the site of our Shizuoka plant and the site of our Komaki warehouse as part of efforts to improve corporate governance including asset efficiency. We also recorded a gain on sales of investment securities of 4,574 million yen as a result of the sale of shares including shares of Asahi Group Holdings, Ltd. and shares of Nissin Foods Holdings Co., Ltd. in line with our basic policy to dispose of and reduce cross-shareholdings of little significance.

Extraordinary loss for the consolidated fiscal year under review increased by 581 million yen, to 2,179 million yen, compared with 1,598 million yen for the previous consolidated fiscal year.

Our subsidiary Kada Greenfarm Co., Ltd. severely suffered from Typhoons No. 20 and No. 21 in August and September 2018 and was dissolved with effect on November 30, 2018 based on the judgment that any resumption of its business in the future was impossible. As a result, we recorded a loss on disaster of 1,271 million yen in the consolidated fiscal year under review. Additionally, in our international business, a laggard in responding to environmental changes, we made a start on structural reforms, focusing on the seed business, and recorded business structure improvement expenses of 471 million yen, including the closure of unprofitable sales bases and the disposal of inventories based on a review of sales strategies.

Income taxes and profit attributable to shareholders of parent

Total income taxes for the consolidated fiscal year under review decreased by 311 million yen, to 4,921 million yen compared with 5,232 million yen for the previous consolidated fiscal year. The actual effective tax rate after application of deferred tax accounting was 30.9%, which edges the effective statutory tax rate in Japan, 30.7%, reflecting the impact of amortization of goodwill, among other factors.

Profit attributable to shareholders of parent for the consolidated fiscal year under review after deducting profit attributable to non-controlling interests from net income increased by 1,426 million yen, to 11,527 million yen, compared with 10,100 million yen for the previous consolidated fiscal year.

Accordingly, for the consolidated fiscal year under review, net sales were 209,865 million yen, down 2.0% year on year, operating income was 12,000 million yen, up 0.3% year on year, ordinary income was 12,051 million yen, down 4.5% year on year, and profit attributable to shareholders of parent was 11,527 million yen, up 14.1% year on year.

Analysis of Financial Condition

Assets

Kagome's total assets at the end of the consolidated fiscal year under review decreased by 2,124 million yen from the end of the previous consolidated fiscal year.

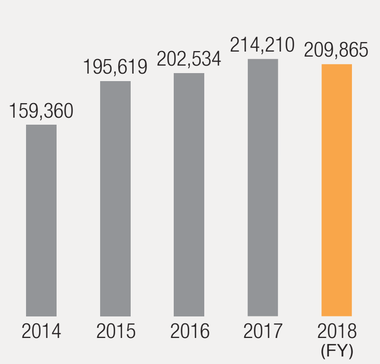
Current assets increased by 7,653 million yen from the end of the previous consolidated fiscal year. This was due to an increase of 8,441 million yen in "cash and deposits" due mainly to the sale of investment securities.

Fixed assets decreased by 9,778 million yen from the end of the previous consolidated fiscal year.

"Property, plant and equipment" increased by 3,351 million yen from the end of the previous consolidated fiscal year.

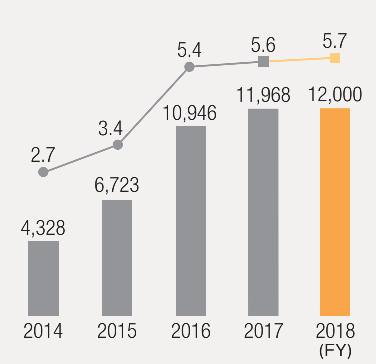
Net Sales

(Unit: Millions of Yen)



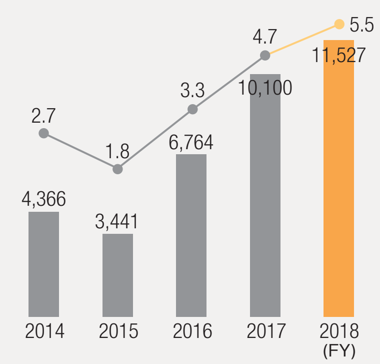
Operating Income / Operating Income to Net Sales

(Unit: Millions of Yen / %)



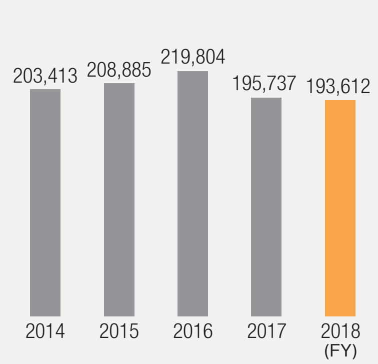
Profit Attributable to Shareholders of Parent / Return on Sales

(Unit: Millions of Yen / %)



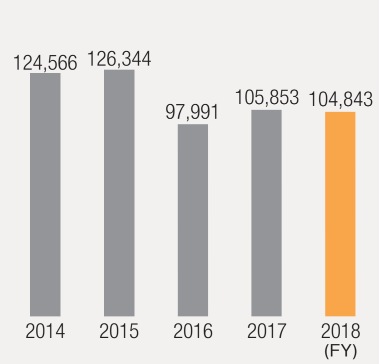
Total Assets

(Unit: Millions of Yen)



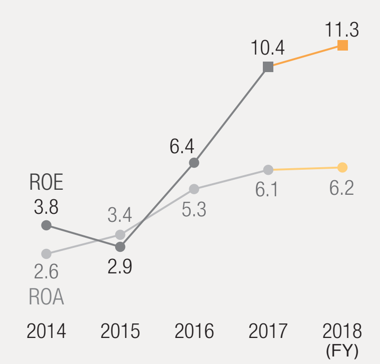
Total Net Assets

(Unit: Millions of Yen)



ROA (Return on Assets) / ROE (Return on Equity)

(Unit: %)



One major source of increase was 11,366 million yen in fixed investments due mainly to the renewal of Kagome's manufacturing equipment.

Main decreases were depreciation and amortization of 4,775 million yen, sale of real estate of 1,032 million yen, and impairment loss of 844 million yen.

"Investments and other assets" decreased by 13,125 million yen from the end of the previous consolidated fiscal year due mainly to the sale of investment securities.

Liabilities

Liabilities decreased by 1,114 million yen from the end of the previous consolidated fiscal year.

This resulted from a 2,802 million yen decrease in deferred tax liabilities due mainly to the sale of investment securities, offsetting a 1,514 million yen increase in "Other payable" (including long-term accounts payable).

Net assets decreased by 1,009 million yen from the end of the previous consolidated fiscal year.

This was attributable to a decrease of 9,321 million yen in "Accumulated other comprehensive income," reflecting the sale and market value decline of investment securities and yen appreciation, which offset an increase of 9,105 million yen in shareholder's equity resulting from an increase of 11,527 million yen in "Retained earnings" due to "Profit attributable to shareholders of parent" and a decrease of 2,668 million yen due to distribution of surplus money.

As a result, the shareholder equity ratio was 52.5% and net assets per share was 1,146.85 yen.

Analysis of Status of Consolidated Cash Flows

Cash and cash equivalents as of December 31, 2018 amounted to 30,112 million yen, an increase of 8,562 million yen compared to December 31, 2017.

The status of respective cash flows is as follows:

Net cash provided by operating activities was 10,130 million yen (compared to net cash provided of 16,598 million yen for the previous fiscal year). This mainly reflects profit before income taxes of 15,928 million yen, depreciation and amortization of 5,194 million yen (the above were net cash inflows), gain on sales of investment securities of 4,517 million yen, gain on sales and disposal of fixed assets of 1,254 million yen, and income taxes paid of 5,500 million yen (the above were net cash outflows).

Net cash used in investing activities was 299 million yen (compared to net cash provided of 17,271 million yen for the previous fiscal year).

This was mainly attributable to inflows of 8,962 million yen due to sales of investment securities and 2,331 million yen due to the sales of fixed assets and outflows of 10,718 million yen due to the acquisition of fixed assets and 801 million yen due to purchases of investment securities.

Net cash used in financing activities was 1,083 million yen (compared to net cash used of 40,761 million yen for the previous fiscal year).

Major factors were inflows of 7,726 million yen due to long-term borrowings and 2,301 million yen due to increase (decrease) in short-term borrowings and outflows of 8,497 million yen due to repayments of long-term borrowings and 2,668 million yen due to dividends paid.

Capital Resources and Capital Liquidity

The Kagome Group's basic policy is to ensure the capital liquidity and capital resources needed for its business operations. The Group's main capital resources are cash flows from operating activities and loans from financial institutions.

Long-term funding demand for capital investment, etc. is met mainly through the Group's own funds and long-term borrowings from financial institutions whilst short-term funding needs for working capital, etc. are met mainly through the Group's own funds.

As of December 31, 2018, cash and cash equivalents amounted to 30,112 million yen and interest-bearing debt amounted to 37,302 million yen.

Outlook for the Fiscal Year Ending December 31, 2019

Conditions in the domestic food industry are expected to remain uncertain in 2019, with contraction of the market due to population decline, higher consumption tax, rising prices for imported raw materials and increased logistics expenses, and changes in the global situation. In this environment, Kagome launched a three-year Mid-term Management Plan starting from the fiscal year ending December 31, 2019, aiming to "become a strong company capable of sustainable growth, using food as a means of resolving social issues" and to realize its long-term vision of transforming from a "tomato company" to a "vegetable company."

	Revenue (million yen) Note 2	Core operating income (million yen) Note 3	Operating income (million yen)	Profit attributable to owners of parent (million yen)	Basic earnings per share (yen)
Fiscal year ending December 31, 2019 (Forecast)	189,000	12,600	13,600	9,500	107.10

Note 1. The above consolidated financial results forecast has been prepared in accordance with International Financial Reporting Standards (IFRS) because Kagome decided to voluntarily adopt IFRS starting from the fiscal year ending December 31, 2019.

Note 2. Revenue is presented net of sales rebates and discounts, which were previously presented in selling, general and administrative expenses.

Note 3. Core operating income is a profit index that measures constant business performance by deducting cost of sales and selling, general and administrative expenses from revenue plus share of loss (profit) of entities accounted for using equity method.

Consolidated Financial Statements

Consolidated Balance Sheets

	Millions of Yen As of Dec. 31, 2017	Millions of Yen As of Dec. 31, 2018	Thousands of U.S. dollars As of Dec. 31, 2018
Assets			
Current assets:			
Cash and deposits	22,150	30,591	275,595
Notes and accounts receivable	36,042	35,893	323,360
Merchandise and finished goods	21,143	19,705	177,523
Work in process	919	896	8,072
Raw material and supplies	19,636	20,674	186,252
Deferred tax assets	506	1,014	9,135
Derivatives	2,568	195	1,757
Other current assets	7,051	8,631	77,757
Allowance for doubtful accounts	(351)	(281)	(2,532)
Total current assets	109,667	117,321	1,056,946
Fixed assets:			
Property, plant and equipment:			
Buildings and structures	43,867	44,482	
Accumulated depreciation	(25,042)	(24,984)	
Buildings and structures, net	18,824	19,497	175,649
Machinery, equipment and vehicles	70,864	73,364	
Accumulated depreciation	(53,042)	(53,627)	
Machinery, equipment and vehicles, net	17,821	19,736	177,802
Tools and furniture	6,276	6,190	
Accumulated depreciation	(5,334)	(5,109)	
Tools and furniture, net	942	1,081	9,739
Land	12,874	11,532	103,892
Lease assets	3,369	3,384	
Accumulated depreciation	(2,518)	(2,567)	
Lease assets, net	851	817	7,360
Construction in progress	1,935	3,937	35,468
Property, plant and equipment, net	53,250	56,602	509,928
Intangible assets:			
Goodwill	503	55	495
Software	1,426	1,872	16,865
Other intangible assets	266	264	2,378
Total intangible assets	2,196	2,192	19,748
Investments and other assets:			
Investment securities	22,364	10,413	93,811
Long-term loans receivable	1,581	1,238	11,153
Deferred tax assets	95	132	1,189
Other assets	6,663	5,783	52,099
Allowance for doubtful accounts	(82)	(71)	(640)
Total investments and other assets	30,621	17,496	157,622
Total fixed assets	86,069	76,291	687,306
Total assets	195,737	193,612	1,744,252

	Millions of Yen As of Dec. 31, 2017	Millions of Yen As of Dec. 31, 2018	Thousands of U.S. dollars As of Dec. 31, 2018
Liabilities			
Current liabilities:			
Notes and accounts payable	16,554	16,472	148,396
Short-term borrowings	21,218	22,306	200,955
Current portion of long-term borrowings	1,447	1,719	15,486
Other payable	12,039	13,166	118,613
Income taxes payable	3,918	3,620	32,613
Deferred tax liabilities	14	13	117
Accrued bonuses for employees	1,251	1,316	11,856
Accrued bonuses for directors	105	79	712
Derivatives liabilities	2	4	36
Other current liabilities	3,158	3,862	34,793
Total current liabilities	59,710	62,563	563,631
Long-term liabilities:			
Long-term borrowings	14,154	12,910	116,306
Deferred tax liabilities	3,882	1,079	9,721
Net defined benefit liability	5,045	5,454	49,135
Provision for loss on guarantees	190	185	1,667
Other	6,900	6,576	59,243
Total long-term liabilities	30,173	26,206	236,090
Total liabilities	89,883	88,769	799,721
Net Assets			
Shareholder's equity:			
Common stock	19,985	19,985	180,045
Capital surplus	22,362	22,362	201,459
Retained earnings	74,303	83,162	749,207
Treasury stock	(26,985)	(26,739)	(240,892)
Total shareholder's equity	89,665	98,771	889,829
Accumulated other comprehensive income:			
Unrealized gain on available-for-sale securities	8,971	2,892	26,054
Deferred gains or losses on derivatives under hedge accounting	2,420	457	4,117
Foreign currency translation adjustments	1,754	606	5,459
Remeasurements of defined benefit plans	(864)	(995)	(8,964)
Total accumulated other comprehensive income	12,283	2,961	26,676
Subscription rights to shares	106	202	1,820
Non-controlling interests	3,798	2,908	26,198
Total net assets	105,853	104,843	944,532
Total liabilities and net assets	195,737	193,612	1,744,252

Consolidated Statements of Income

	Millions of Yen		Thousands of U.S. dollars
	Fiscal year ended December 31, 2017	Fiscal year ended December 31, 2018	Fiscal year ended December 31, 2018
Net sales	214,210	209,865	1,890,676
Cost of sales	117,738	115,216	1,037,982
Gross profit	96,472	94,649	852,694
Selling, general and administrative expenses	84,503	82,648	744,577
Operating income	11,968	12,000	108,108
Other income			
Interest income	409	258	2,324
Dividend income	341	360	3,243
Gain on valuation of derivatives	391	-	-
Other	417	434	3,910
Total other income	1,559	1,053	9,486
Other expenses			
Interest expense	477	410	3,694
Share of loss of entities accounted for using equity method	44	72	649
Foreign exchange losses	41	88	793
Other	346	430	3,874
Total other expenses	910	1,002	9,027
Ordinary income	12,618	12,051	108,568
Extraordinary gain			
Gain on sales of fixed assets	354	1,482	13,351
Gain on sales of investment securities	1,721	4,574	41,207
Gain on sales of shares of subsidiaries and associates	2,171	-	-
Gain on transfer of business	330	-	-
Compensation income for expropriation	11	-	-
Total extraordinary gain	4,590	6,056	54,559
Extraordinary loss			
Loss on disposal of non-current assets	195	228	2,054
Impairment loss	1,337	136	1,225
Loss on disaster	-	1,271	11,450
Business structure improvement expenses	-	471	4,243
Other	64	71	640
Total extraordinary loss	1,598	2,179	19,631
Profit before income taxes	15,610	15,928	143,495
Income taxes - current	4,688	4,990	44,955
Income taxes - deferred	544	(69)	(622)
Total income taxes	5,232	4,921	44,333
Net income	10,377	11,006	99,153
(Breakdown)			
Profit attributable to shareholders of parent	10,100	11,527	103,847
Profit (loss) attributable to non-controlling interests	276	(521)	(4,694)

Consolidated Statements of Comprehensive Income

	Millions of Yen		Thousands of U.S. dollars
	Fiscal year ended December 31, 2017	Fiscal year ended December 31, 2018	Fiscal year ended December 31, 2018
Other comprehensive income			
Unrealized gain on available-for-sale securities	2,484	(6,079)	(54,766)
Deferred gains or losses on derivatives under hedge accounting	(1,850)	(1,975)	(17,793)
Foreign currency translation adjustments	656	(1,430)	(12,883)
Remeasurements of defined benefit plans	435	(131)	(1,180)
Share of other comprehensive income of an affiliate by the equity method	(2)	0	0
Total other comprehensive income	1,723	(9,617)	(86,640)
Comprehensive income	12,100	1,389	12,514
(Breakdown)			
Comprehensive income attributable to shareholders of parent	11,621	2,206	19,874
Comprehensive income attributable to non-controlling interests	479	(817)	(7,360)

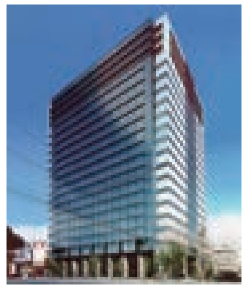
Consolidated Statements of Cash Flows

	Millions of Yen		Thousands of U.S. dollars
	Fiscal year ended December 31, 2017	Fiscal year ended December 31, 2018	Fiscal year ended December 31, 2018
Cash flows from operating activities:			
Profit before income taxes	15,610	15,928	143,495
Depreciation and amortization	5,813	5,194	46,793
Impairment loss	1,337	844	7,604
Amortization of goodwill	722	419	3,775
Interest and dividend income	(750)	(619)	(5,577)
Interest expense	477	410	3,694
Increase (decrease) in accrued bonuses	18	42	378
Increase (decrease) in other provisions	93	(71)	(640)
Increase (decrease) in net defined benefit liability	242	218	1,964
Share of loss (profit) of entities accounted for using equity method	44	96	865
Loss (gain) on sales of investment securities	(1,721)	(4,517)	(40,694)
Loss (gain) on sales of shares of subsidiaries and associates	(2,171)	-	-
Loss (gain) on sales and disposal of fixed assets-net	(158)	(1,254)	(11,297)
Loss (gain) on transfer of business	(330)	-	-
Compensation income for expropriation	(11)	-	-
Decrease (increase) in notes and accounts receivable	(2,993)	(192)	(1,730)
Decrease (increase) in inventories	(1,876)	(597)	(5,378)
Decrease (increase) in accounts receivable-other	(974)	(501)	(4,514)
Increase (decrease) in notes and accounts payable	3,113	(46)	(414)
Increase (decrease) in accounts payable-other	1,203	80	721
Proceeds from lease and guarantee deposits received	615	-	-
Decrease (increase) in other current assets	(260)	(269)	(2,423)
Increase (decrease) in other current liabilities	(255)	321	2,892
Other – Increase (decrease)-net	(51)	(9)	(81)
Subtotal	17,738	15,479	139,450
Cash received from interest and dividend income	772	555	5,000
Cash paid for interest expense	(449)	(404)	(3,640)
Income taxes paid	(1,474)	(5,500)	(49,550)
Proceeds from compensation for expropriation	11	-	-
Net cash provided by (used in) operating activities	16,598	10,130	91,261
Cash flows from investing activities:			
Disbursement for time deposits	(96)	(20)	(180)
Proceeds from withdrawal of time deposits	10,122	115	1,036
Purchases of marketable and investment securities	(682)	(801)	(7,216)
Proceeds from sales and redemption of securities	2,938	8,962	80,739
Acquisition of fixed assets	(9,202)	(10,718)	(96,559)
Proceeds from sales of fixed assets	1,830	2,331	21,000
Collection of loans receivable	263	65	586
Proceeds from transfer of business	868	-	-
Purchase of shares and capital of subsidiaries resulting in change in scope of consolidation	(90)	-	-
Purchase of shares of subsidiaries and associates	(48)	(121)	(1,090)
Proceeds from sales of shares of subsidiaries resulting in change in scope of consolidation	11,246	-	-
Other – Increase (decrease)-net	122	(112)	(1,009)
Net cash provided by (used in) investing activities:	17,271	(299)	(2,694)
Cash flows from financing activities:			
Increase (decrease) in short-term borrowings	(17,918)	2,301	20,730
Proceeds from long-term borrowings	8,634	7,726	69,604
Repayments of long-term borrowings	(29,277)	(8,497)	(76,550)
Repayments of finance lease obligations	(123)	(117)	(1,054)
Dividends paid	(2,180)	(2,668)	(24,036)
Proceeds from share issuance to non-controlling shareholders	0	0	0
Dividends paid to non-controlling interests	(69)	(74)	(667)
Decrease (increase) in treasury shares	173	246	2,216
Other	0	-	-
Net cash provided by (used in) financing activities	(40,761)	(1,083)	(9,757)
Foreign translation adjustment on cash and cash equivalents	377	(185)	(1,667)
Net increase (decrease) in cash and cash equivalents	(6,513)	8,562	77,135
Cash and cash equivalents at beginning of period	28,313	21,550	194,144
Increase (decrease) in cash and cash equivalents resulting from change of scope of consolidation	(249)	-	-
Cash and cash equivalents at end of period	21,550	30,112	271,279

Company Overview

Founded	1899
Established	1949
Head Office	3-14-15, Nishiki, Naka-ku, Nagoya, Aichi Phone: +81-52-951-3571 (Main) Fax: +81-52-968-2510
Tokyo Head Office	Nihonbashi-hamacho F-Tower, 3-21-1 Nihonbashi-hamacho, Chuo-ku, Tokyo Phone: +81-3-5623-8501 (Main) Fax: +81-3-5623-2331
Capital	19,985 million yen
Number of Employees	2,504 (consolidated)
Places of Business	Head Office, Tokyo Head Office, 1 division office, 8 branches, 6 plants, Innovation Division
Description of Business	Production and sales of food seasonings, preserved foods, beverages, and other food products; purchasing, production, and sales of seedlings, fruits, and vegetables


Head Office


Tokyo Head Office

Places of Business and Group Companies

Places of Business

Head Office
Tokyo Head Office
Innovation Division
Tokyo Laboratory

Business Office
- Hokkaido Branch
- Tohoku Branch
- Kita-Tohoku Business Office
- Tokyo Branch
- Kanagawa Branch
- Kanto Branch
- Nagoya Branch
- Shizuoka Business Office
- Hokuriku Business Office
- Osaka Branch
- Chu-Shikoku Branch
- Okayama Business Office
- Shikoku Business Office
- Kyusyu Branch
- Okinawa Business Office

Plants
- Ueno Plant
- Kozakai Plant
- Fujimi Plant
- Nasu Plant
- Ibaraki Plant
- Komaki Plant

Main Group companies

Domestic Subsidiaries and Associates

- Hibikinada Greenfarm Co., Ltd. (Kitakyushu City, Fukuoka)
- Iwaki Onahama Greenfarm Co., Ltd. (Iwaki City, Fukushima)
- Kagome Axis Co., Ltd. (Nagoya City, Aichi)
- F-LINE Corp. (Chuo-ku, Tokyo)

Overseas Subsidiaries and Associates

- Kagome Inc. (California, U.S.A.)
- Ingomar Packing Company, LLC (California, U.S.A.)
- United Genetics Holdings LLC (California, U.S.A.)
- Holding da Industria Transformadora do Tomate, SGPS S.A. (HIT) (Palmela City, Portugal)
- Vegitalia S.p.A. (Calabria, Italy)
- Kagome Australia Pty Ltd. (Victoria, Australia)
- Taiwan Kagome Co., Ltd. (Tainan City, Taiwan)

Status of Shares

Number of shares outstanding	99,616,944 shares
(Note) 1.Total number of authorized shares	279,150,000 shares
2. Number of shares per unit	100 shares
Number of shareholders	186,959

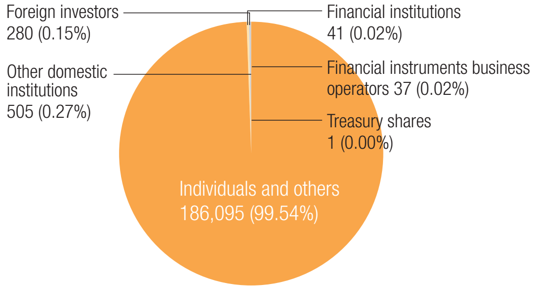
Major Shareholders

Names of Major Shareholders	Capital Contribution to the Company: Number of Shares Held (thousand shares)	Shareholding Ratio (%)
Japan Trustee Services Bank, Ltd. (account in trust)	9,029	10.14
The Master Trust Bank of Japan, Ltd. (account in trust)	5,351	6.01
Dynapac Co., Ltd.	4,399	4.94
Nissin Foods Holdings Co., Ltd.	1,559	1.75
Toshichika Kanie	1,412	1.58
JP MORGAN CHASE BANK 385151	1,251	1.40
Eikichi Kanie	1,110	1.24
Kagome Business Association	975	1.09
STATE STREET BANK WEST CLIENT - TREATY 505234	962	1.08
Shinichi Sano	957	1.07

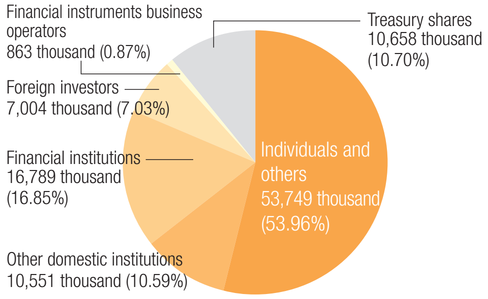
*The shareholding ratios were calculated without treasury shares (10,658 thousand shares). The treasury shares do not include 252 thousand shares of the Company owned by The Master Trust Bank of Japan, Ltd. (account in trust), which was established in the introduction of the employee incentive plan, "Employee Stock Ownership Plan (ESOP) Trust."

Status of Share Distribution

Distribution by Shareholder Type

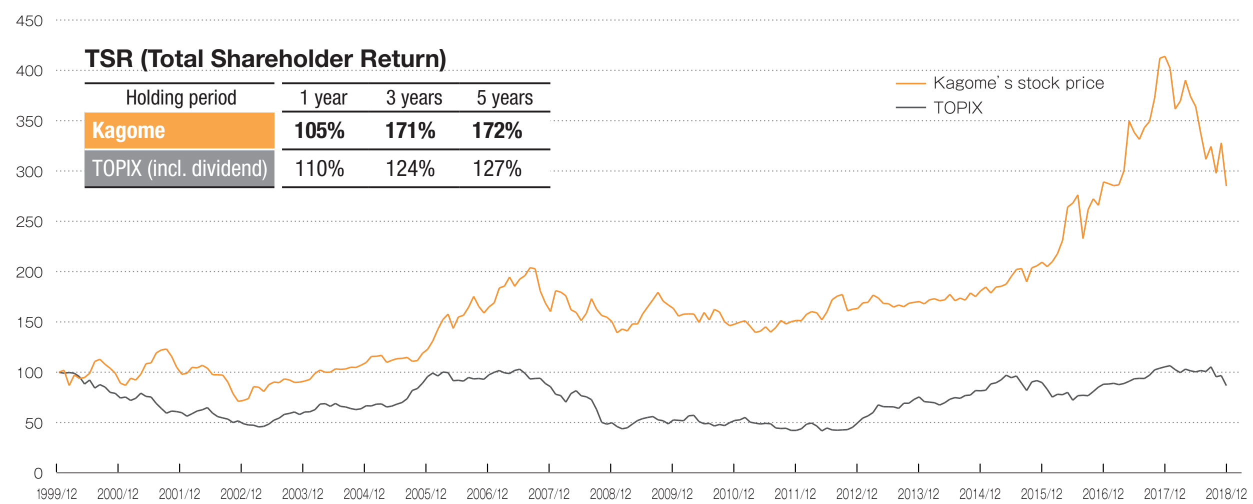


Distribution by Number of Shares



Stock Price Trend

Trends of the Company's stock price and Tokyo Stock Price Index (TOPIX)



TSR (Total Shareholder Return)

Holding period	1 year	3 years	5 years
Kagome	105%	171%	172%
TOPIX (incl. dividend)	110%	124%	127%

*Month-end stock prices relative to the stock price as of December 31, 1999, being 100.
*TSR is a total return assuming that dividends are re-invested at the closing price as of March 31, 2014, which is the end of the fiscal year in question.

Changes in Trading Volume (in yen)