Consolidated Financial Results for the Fiscal Year Ended December 31, 2016 [IFRS]

February 2, 2017

Company name: Kao Corporation
Tokyo Stock Exchange in Japan
Stock code: 4452
(URL: http://www.kao.com/jp/en/corp_ir/investors.html)
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Scheduled starting date of the dividend payments: March 22, 2017
Supplementary documents of the financial results: Yes
Holding financial results information meeting: Yes (for institutional investors and analysts)

(Millions of yen, except per share amounts)
(Amounts less than one million yen are rounded)

1. Consolidated financial results for the fiscal year ended December 31, 2016 (from January 1, 2016 to December 31, 2016)

(1) Consolidated operating results

(Percentages indicate year-on-year changes)

	Fiscal year ended December 31, 2016	%	Fiscal year ended December 31, 2015	%
Net sales	1,457,610	(1.1)	1,474,550	-
Operating income	185,571	10.9	167,318	-
Income before income taxes	183,430	10.5	166,038	-
Net income	127,889	20.7	105,952	-
Net income, attributable to owners of the parent	126,551	20.3	105,196	-
Comprehensive income	94,129	2.1	92,151	-

	Fiscal year ended December 31, 2016	Fiscal year ended December 31, 2015
Basic earnings per share (Yen)	253.43	209.82
Diluted earnings per share (Yen)	253.18	209.53
Ratio of net income to equity attributable to owners of the parent	18.6%	16.1%
Ratio of income before income taxes to total assets	13.8%	13.1%
Ratio of operating income to net sales	12.7%	11.3%
(Reference) Share of profit/loss in investments accounted for using the equity method	1,894	1,517

(2) Consolidated financial position

	December 31, 2016	December 31, 2015
Total assets	1,338,309	1,311,064
Total equity	691,463	691,987
Equity attributable to owners of the parent	679,842	680,996
Ratio of equity attributable to owners of the parent to total assets	50.8%	51.9%
Equity attributable to owners of the parent per share (Yen)	1,379.37	1,358.03

(3) Consolidated cash flows

	Fiscal year ended December 31, 2016	Fiscal year ended December 31, 2015
Net cash flows from operating activities	184,307	181,672
Net cash flows from investing activities	(88,639)	(74,124)
Net cash flows from financing activities	(95,043)	(20,773)
Cash and cash equivalents at the end of the year	303,026	309,922

2. Dividends

	Year ending December 31, 2017 (Forecast)	Year ended December 31, 2016	Year ended December 31, 2015
Annual cash dividends per share (Yen)			
1st quarter end	-	-	-
2nd quarter end	54.00	46.00	38.00
3rd quarter end	-	-	-
Fiscal year end	54.00	48.00	42.00
Total	108.00	94.00	80.00
Total dividend payment amount		46,787	40,158
Payout ratio (consolidated)	38.6%	37.1%	38.1%
Ratio of dividends to equity attributable to owners of the parent (consolidated)		6.9%	6.1%

3. Forecast of consolidated operating results for the fiscal year ending December 31, 2017 (from January 1, 2017 to December 31, 2017)

(Millions of yen, except per share amounts)
(Percentages indicate year-on-year changes)

	Six months ending June 30, 2017	%	Year ending December 31, 2017	%
Net sales	700,000	0.1	1,470,000	0.9
Operating income	82,000	1.1	200,000	7.8
Income before income taxes	82,000	6.3	199,000	8.5
Net income, attributable to owners of the parent	52,000	4.0	138,000	9.0
Basic earnings per share (Yen)	105.51	-	280.00	-

Note: From the fiscal year ending December 31, 2017, the Kao Group plans to adopt IFRS 15, “Revenue from Contracts with Customers” early in tandem with a revision of its sales system for the Consumer Products Business in Japan. As a result, certain items formerly treated as expenses will be deducted from net sales. Calculating net sales for the previous year using the same standard, growth rates in the forecast of consolidated business results would be 4.5% for the interim period and 5.3% for the full fiscal year.

4. Others

(1) Changes in significant subsidiaries during the year (changes in specified subsidiaries resulting in change in scope of consolidation): None

(2) Changes in accounting policies and changes in accounting estimates

1) Changes in accounting principles required by IFRS: None
2) Changes in accounting principles due to reasons other than 1): None
3) Changes in accounting estimates: Yes

For details, please refer to "2. Items Related to Summary Information (Notes), (2) Changes in accounting principles and changes in accounting estimates".

(3) Number of issued shares outstanding at the end of the year (ordinary shares)

	December 31, 2016	December 31, 2015
Number of issued shares including treasury shares	504,000,000	504,000,000
Number of treasury shares	11,137,654	2,541,816

	Fiscal year ended December 31, 2016	Fiscal year ended December 31, 2015
Weighted average number of shares outstanding during the year	499,355,189	501,351,849

Notice regarding execution of audit procedures

This financial results report is exempt from audit procedures based on the Financial Instruments and Exchange Law of Japan. At the time of disclosure of this report, audit procedures for financial statements are in progress.

Explanation regarding the appropriate use of forecast of operating results and other special items

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

Please refer to "1. Analysis of Operating Results and Financial Condition" for the suppositions that form the assumptions for earnings forecasts and cautions concerning the use of earnings forecasts.

Adoption of International Financial Reporting Standards (IFRS)

The Group has adopted International Financial Reporting Standards (IFRS) from the fiscal year ended December 31, 2016.
Presentation of figures in the consolidated financial statements for the previous year also conforms to IFRS.
For differences between IFRS and Japanese GAAP in the financial statements, see information on first-time adoption of IFRS in the Investor Relations section of the Company's website.

1. Analysis of Operating Results and Financial Condition

(1) Analysis of Operating Results

Operating Results for the Fiscal Year Ended December 31, 2016

The Kao Group has adopted International Financial Reporting Standards (IFRS) from the fiscal year ended December 31, 2016. In addition, financial figures for the previous fiscal year have been restated using IFRS for comparative analysis.

(Billions of yen, except per share amounts)

	2016	2015	Growth %
Net sales	1,457.6	1,474.6	(1.1)
Operating income	185.6	167.3	10.9
Operating margin (%)	12.7	11.3	-
Income before income taxes	183.4	166.0	10.5
Net income	127.9	106.0	20.7
Net income, attributable to owners of the parent	126.6	105.2	20.3
Basic earnings per share (Yen)	253.43	209.82	20.8

1) Trends in Overall Results for the Fiscal Year Ended December 31, 2016

During the fiscal year ended December 31, 2016, the global economy slowed in the first half due to factors including a trend toward normalization of monetary policy in the United States and Europe, sluggish economies in emerging nations and elsewhere, and a drop in the price of crude oil, but turned toward recovery in the second half, centered on the United States. The Japanese economy continued on a moderate recovery track, although delays in improvement have become apparent in some sectors. Moreover, it was a volatile year in foreign exchange markets. The household and personal care products market in Japan, a key market for the Kao Group, grew by 2% on a value basis and consumer purchase prices remained nearly flat compared with the previous fiscal year. The cosmetics market in Japan grew by 1%, excluding inbound demand (demand from visitors to Japan).

Under these circumstances, the Kao Group worked to launch and nurture products with high added value in response to changes in consumer needs based on its concept of "*Yoki-Monozukuri,"** which emphasizes research and development geared to customers and consumers. The Kao Group also conducted cost reduction activities and other measures.

* *The Kao Group defines* Yoki-Monozukuri *as a strong commitment by all members to provide products and brands of excellent value for consumer satisfaction. In Japanese,* Yoki *literally means "good/excellent," and* Monozukuri *means "development/manufacturing of products."*

To improve capital efficiency and increase shareholder returns, Kao Corporation resolved at a meeting of its Board of Directors held on August 25, 2016 to repurchase its own shares, and repurchased shares totaling 50.0 billion yen.

Net sales decreased 1.1% compared with the previous fiscal year to 1,457.6 billion yen. Excluding the effect of currency translation, net sales would have increased 3.2%. In the Consumer Products Business, sales increased in Japan due to factors including market growth, launches of new and improved products, and further enhancement of sales promotion activities. Outside Japan, sales in Asia increased, excluding the effect of currency translation. In the Chemical Business, sales increased compared with the previous fiscal year, excluding the effect of currency translation, as the Kao Group worked to adjust selling prices in response to rising costs for natural fats and oils, although sales were impacted by a decline in demand in some customer industries.

As for profits, due to the effect of increased sales in the Consumer Products Business in Japan and Asia, a decrease in the cost of petrochemical raw materials and other factors, operating income was 185.6 billion yen, an increase of 18.3 billion yen compared with the previous fiscal year, the operating margin was 12.7% and income before income taxes was 183.4 billion yen, an increase of 17.4 billion yen. Net income was 127.9 billion yen, an increase of 21.9 billion yen.

Basic earnings per share were 253.43 yen, an increase of 43.61 yen, or 20.8%, from 209.82 yen in the previous fiscal year.

Economic value added (EVA*), which the Kao Group uses as a management indicator, increased 14.8 billion yen compared with the previous fiscal year to 73.4 billion yen, due in part to an increase in net operating profit after tax (NOPAT) and efforts to reduce capital invested including the implementation of shareholder returns through a share repurchase.

** EVA is a registered trademark of Stern Stewart & Co.*

The main exchange rates used for translating the financial statement items (income and expenses) of foreign consolidated subsidiaries and affiliates were as shown below.

	First quarter Jan. – Mar.	Second quarter Apr. – Jun.	Third quarter Jul. – Sep.	Fourth quarter Oct. – Dec.
Yen/U.S. dollar	115.31 (119.15)	108.05 (121.33)	102.38 (122.23)	109.41 (121.43)
Yen/Euro	127.15 (134.43)	122.05 (134.14)	114.24 (135.91)	117.88 (132.99)
Yen/Chinese yuan	17.63 (19.11)	16.55 (19.56)	15.36 (19.41)	16.01 (19.00)

Note: Figures in parentheses represent the exchange rates for the same period of the previous fiscal year.

2) Trends by Segment during the Fiscal Year

Summary of Segment Information

Consolidated Results by Segment

(Billions of yen)

Fiscal year ended December 31	Net sales				Operating income			
	2016	2015	Growth %	Like-for-like*	2016	2015	Change	% of net sales
Beauty Care	601.6	608.6	(1.1)	2.9	51.1	37.9	13.2	8.5
Human Health Care	273.1	281.7	(3.1)	1.3	25.9	33.4	(7.4)	9.5
Fabric and Home Care	345.2	335.3	2.9	4.7	78.1	66.1	12.0	22.6
Total Consumer Products	1,219.8	1,225.6	(0.5)	3.0	155.1	137.4	17.7	12.7
Chemical	273.8	288.5	(5.1)	2.5	29.7	28.6	1.1	10.8
Total	1,493.6	1,514.1	(1.3)	2.9	184.8	166.0	18.8	12.4
Reconciliations	(36.0)	(39.5)	-	-	0.8	1.3	(0.5)	-
Consolidated	1,457.6	1,474.6	(1.1)	3.2	185.6	167.3	18.3	12.7

Note:
* Like-for-like growth rates exclude the currency translation effect related to translation of local currencies into Japanese yen.

Consolidated Net Sales Composition

(Billions of yen)

Fiscal year ended December 31	Net sales			
	2016	2015	Growth %	Like-for-like*
Beauty Care	425.3	412.3	3.2	3.2
Human Health Care	215.3	222.7	(3.3)	(3.3)
Fabric and Home Care	302.3	288.8	4.7	4.7
Total Japan	943.0	923.8	2.1	2.1
Asia	180.8	182.7	(1.1)	13.0
Americas	80.1	89.7	(10.7)	(0.5)
Europe	78.1	89.9	(13.1)	(0.8)
Eliminations	(62.2)	(60.5)	-	-
Total Consumer Products	1,219.8	1,225.6	(0.5)	3.0
Japan	124.0	130.0	(4.6)	(4.6)
Asia	103.8	105.8	(1.9)	12.4
Americas	44.6	48.2	(7.4)	7.8
Europe	59.4	64.8	(8.3)	2.4
Eliminations	(58.0)	(60.3)	-	-
Total Chemical	273.8	288.5	(5.1)	2.5
Total	1,493.6	1,514.1	(1.3)	2.9
Reconciliations	(36.0)	(39.5)	-	-
Consolidated	1,457.6	1,474.6	(1.1)	3.2

Note:
* Like-for-like growth rates exclude the currency translation effect related to translation of local currencies into Japanese yen.

Reference: Consolidated Results by Geographic Area[1]

(Billions of yen)

Fiscal year ended December 31	Net sales				Operating income			
	2016	2015	Growth %	Like-for-like[2]	2016	2015	Change	% of net sales
Japan	1,035.7	1,019.8	1.6	1.6	145.1	127.8	17.4	14.0
Asia	281.5	284.8	(1.1)	13.0	22.8	20.9	2.0	8.1
Americas	124.7	137.8	(9.6)	2.4	7.2	7.8	(0.6)	5.8
Europe	137.2	154.4	(11.1)	0.5	9.4	12.1	(2.7)	6.8
Total	1,579.1	1,596.8	(1.1)	3.6	184.6	168.5	16.1	11.7
Reconciliations	(121.5)	(122.2)	-	-	1.0	(1.1)	2.2	-
Consolidated	1,457.6	1,474.6	(1.1)	3.2	185.6	167.3	18.3	12.7

Notes:
1. Information on consolidated results by geographic area is for reference.
2. Like-for-like growth rates exclude the currency translation effect related to translation of local currencies into Japanese yen.

Net sales outside Japan were 33.8% of net sales compared with 35.2% for the previous fiscal year. Excluding the effect of currency translation, net sales outside Japan would have been 36.6% of net sales.

Consumer Products Business

Sales decreased 0.5% compared with the previous fiscal year to 1,219.8 billion yen. Excluding the effect of currency translation, sales would have increased 3.0%.

In Japan, sales increased 2.1% to 943.0 billion yen. The Kao Group made efforts that included working to respond to the changing lifestyles and diversifying preferences of consumers, and social issues such as the environment, health, the aging society and hygiene, by launching numerous high-value-added products and enhancing proposal-oriented sales activities.

In Asia, sales decreased 1.1% to 180.8 billion yen. Excluding the effect of currency translation, sales would have increased 13.0%. Growth continued as the Kao Group worked in areas such as launching and nurturing products targeting the middle-class consumer segment, collaborating with retailers, utilizing wholesale channels and expanding sales regions.

In the Americas, sales decreased 10.7% to 80.1 billion yen. Excluding the effect of currency translation, sales would have decreased 0.5%. Although sales of skin care products and professional hair care products grew, sales of hair care products decreased compared with the previous fiscal year.

In Europe, sales decreased 13.1% to 78.1 billion yen. Excluding the effect of currency translation, sales would have decreased 0.8%. Although sales of professional hair care products were nearly flat, sales of hair care products decreased compared with the previous fiscal year.

Operating income increased 17.7 billion yen compared with the previous fiscal year to 155.1 billion yen due to factors including the effect of increased sales in the Fabric and Home Care Business in Japan, increased sales in Asia, a decrease in the cost of raw materials and the completion of amortization of trademarks.

Note: The Kao Group's Consumer Products Business consists of the Beauty Care Business, the Human Health Care Business, and the Fabric and Home Care Business.

Beauty Care Business

Sales decreased 1.1% compared with the previous fiscal year to 601.6 billion yen. Excluding the effect of currency translation, sales would have increased 2.9%.

Sales of cosmetics were on a par with the previous fiscal year at 255.0 billion yen. Excluding the effect of currency translation, sales would have increased 2.8%. In Japan, sales increased due to factors including good performance by new products launched in 2015 and enhanced in-store sales promotion activities. Major reforms in the cosmetics business started in September 2016 and sales of the *SOFINA iP* series, for which sales channels have expanded, and of the new global brand *KANEBO* were steady. In counseling cosmetics, the *ALBLANC* skin brightening brand and the *RMK* brand performed strongly, and in self-selection cosmetics, sales of *KATE* and *media* makeup grew. Sales increased outside Japan, due in part to strong performance in China and Taiwan.

Sales of skin care products increased. In Japan, sales increased due to growth in sales of *Bioré* facial cleanser and UV care as well as *Curél* derma care products. Sales also grew in Asia and in the Americas as *Bioré* sold strongly.

Sales of hair care products decreased. In Japan, the Kao Group conducted a complete renewal of *Essential* shampoos and conditioners and other measures, but sales were flat due to intensifying competition. The Kao Group also launched new easy-to-use, environmentally conscious refill products, which gained the support of consumers. Outside Japan, sales decreased as severe conditions continued.

Operating income increased 13.2 billion yen compared with the previous fiscal year to 51.1 billion yen, due to the effect of increased sales in Japan, the completion of amortization of trademarks related to Kanebo Cosmetics, and an impairment loss and other items recorded in the previous fiscal year.

Human Health Care Business

Sales decreased 3.1% compared with the previous fiscal year to 273.1 billion yen. Excluding the effect of currency translation, sales would have increased 1.3%.

For food and beverage products, signs of recovery became apparent as the Kao Group strengthened its promotion of the function of highly concentrated tea catechins in *Healthya Green Tea,* a functional drink that enhances the body's ability to metabolize fat and facilitates reduction of body fat, and worked to cultivate new users.

Sales of sanitary products increased. Sales of the *Laurier* brand of sanitary napkins grew steadily. In Japan, a high-value-added scented version of *Laurier Slim Guard*, which offers both high absorbency and comfort, was launched and sales increased. In Asia, sales of high-value-added products increased strongly. Sales of *Merries* baby diapers were nearly flat excluding the effect of currency translation. In Japan, amid a decline in demand for purchasing with the purpose of resale in China compared with the previous fiscal year, the Kao Group began full-scale efforts for cross-border e-commerce for the Chinese market, but sales decreased. In addition, the Kao Group has mostly resolved prolonged shortages in stores, and resumed marketing activities. Market share is recovering, supported by the June 2016 launch of an improved product with even better breathability, among other factors. In China, where market growth continues, sales increased even as the Kao Group conducted a transformation of its sales structure. In Indonesia, sales of locally produced *Merries* targeting the middle-class consumer segment were favorable.

Sales of personal health products increased. Sales of oral care products increased with good performance by *Pure Oral* toothpaste and mouthwash. Sales of bath additives increased. Although sales of *MegRhythm* steam thermo sheets decreased due to a decline in inbound demand, the product is on a recovery trend as a result of factors including enhanced in-store sales promotion activities and advertising.

Operating income decreased 7.4 billion yen compared with the previous fiscal year to 25.9 billion yen due to factors including the effect of aggressive marketing expenditures, an increase in depreciation, the effect of exchange rate fluctuations and a decrease in inbound demand.

Fabric and Home Care Business

Sales increased 2.9% compared with the previous fiscal year to 345.2 billion yen. Excluding the effect of currency translation, sales would have increased 4.7%.

Sales of fabric care products increased compared with the previous fiscal year. In Japan’s fiercely competitive market environment, both sales and market share increased from responding to the larger-sized products category and the contribution of new and improved products. Sales of laundry detergents increased, centered on ultra-concentrated liquid laundry detergent *Ultra Attack Neo* and the rest of the *Neo* series, as well as conventional-type *Attack Antibacterial EX Super Clear Gel*. For fabric softeners, as the market for high-value-added products expanded, the Kao Group launched a new *Flair Fragrance* product that features a new fragrance release function, and *Flair Fragrance IROKA*, a premium fabric softener, and sales increased. *Humming Fine*, which has a strong deodorizing effect, sold strongly. Sales also increased in Asia compared with the previous fiscal year. In particular, sales were strong for *Attack Jaz1*, a powder detergent for hand washing targeting the middle-class consumer segment in Indonesia.

Sales of home care products increased. In Japan, for *CuCute* dishwashing detergent, the Kao Group launched *CuCute CLEAR Foam Spray*, a new foam spray type product. In response to the conventional notion that a sponge is used with dishwashing detergent, the product created a new market with the entirely new concept of “spraying away residue from places a sponge can’t reach.” Sales of *Magiclean* household cleaners for the bath, toilet, kitchen and other areas grew with value-added offerings such as deodorizing, disinfecting and anti-staining. In addition, sales of *Resesh* clothing, fabric and air refresher and *Quickle* household cleaning mop kit grew steadily. Sales grew in Asia as *Magiclean*, a high-value-added household cleaner that responds to lifestyles in each country for use in various daily life settings, performed strongly in Thailand and elsewhere.

Operating income increased 12.0 billion yen compared with the previous fiscal year to 78.1 billion yen due to factors including the effect of increased sales and a decrease in the cost of raw materials.

Chemical Business

Sales decreased 5.1% compared with the previous fiscal year to 273.8 billion yen. Excluding the effect of currency translation, sales would have increased 2.5%.

In Japan, sales were impacted by a trend toward a decrease in demand in some customer industry markets, including construction materials. Outside Japan, excluding the effect of currency translation, sales increased despite the negative effects from the decrease in demand among customer industries, as the Kao Group worked to expand sales and adjust the selling prices of oleo chemicals.

Sales of oleo chemicals continued to increase as the Kao Group worked to adjust selling prices in line with the continuing rise of raw material prices. In performance chemicals, the Kao Group worked to develop and expand sales of high-value-added products with a reduced environmental footprint, but was impacted by worsening conditions in the construction materials and other markets. Sales of specialty chemicals decreased due to ongoing sluggish demand and structural changes in the personal computer market.

Operating income increased 1.1 billion yen compared with the previous fiscal year to 29.7 billion yen as the Kao Group promoted high-value-added products, worked to adjust selling prices and conducted other measures in response to rising costs for natural fats and oils in a severe business environment.

In June 2016, the Kao Group announced the acquisition of ink companies in the United States and Europe to accelerate the development of its water-based pigment inkjet ink, which contributes to reducing environmental footprint, and the global rollout of the business. The company in the United States became a consolidated subsidiary in July 2016.

Forecast of Business Results (Billions of yen, except per share amounts)

	2017	2016	Growth %
Net sales	1,470.0	1,457.6	0.9*
Operating income	200.0	185.6	7.8
Operating margin (%)	13.6	12.7	-
Income before income taxes	199.0	183.4	8.5
Net income, attributable to owners of the parent	138.0	126.6	9.0
Basic earnings per share (Yen)	280.00	253.43	10.5

** From fiscal 2017, the Kao Group plans to adopt IFRS 15, "Revenue from Contracts with Customers" early in tandem with a revision of its sales system. Calculating net sales for the previous fiscal year using the same standard, the above growth rate would be an increase of 5.3% (an increase of 4.7% excluding the effect of currency translation).*

1) Forecast of Overall Business Results for the Fiscal Year Ending December 31, 2017

Expectations for the global economy are spreading in the United States and worldwide, but on the other hand, as anti-globalization and protectionist trends are starting to become conspicuous, there are concerns about a downturn in business conditions due to trends in government policies and financial markets in each country, as well as fluctuations in exchange rates and geopolitical risks. In Japan, amid continuing improvement in conditions for employment and income, the economy is expected to recover moderately, due in part to the effects of various economic measures, but there is also a possibility of impact from an economic downturn overseas, and the outlook for the operating environment remains unclear.

Amid these circumstances, the Kao Group will accurately respond to various changes in the operating environment of the Consumer Products Business and aims for sustained "profitable growth" globally by increasing the added value of its products from the consumer's perspective. In the Chemical Business, the Kao Group will carry out measures such as developing high-value-added products that are unaffected by trends in raw material prices and enhancing eco-chemical products with a reduced environmental impact. The fiscal year ending December 31, 2017 is the initial year of the Kao Group Mid-term Plan "K20," which will span the four-year period to 2020. The Kao Group will steadily implement the various strategies incorporated in the plan, one by one.

From the first quarter of 2017, the Kao Group plans to adopt IFRS 15, "Revenue from Contracts with Customers" early in tandem with a revision of its sales system for the Consumer Products Business in Japan. As a result, the Kao Group forecasts that net sales will increase 0.9% year on year to 1,470.0 billion yen due to the deduction from net sales of certain items formerly treated as expenses. Calculating net sales for the fiscal year ended December 31, 2016 using the same standard, the increase in net sales would be 5.3% (4.7% excluding the effect of currency translation). The Kao Group will work to stimulate the market with new product launches and other measures inside and outside Japan, and expects an increase in sales volume.

Overall, the Kao Group expects higher raw material prices compared with the previous fiscal year, with prices for natural oils and fats forecast to remain at a high level and market prices for petrochemicals forecast to rise somewhat. In addition, the Kao Group will continue to conduct cost reduction activities and other measures.

Based on these assumptions, the Kao Group forecasts a 7.8% increase in operating income to 200.0 billion yen, an operating margin of 13.6%, an 8.5% increase in income before income taxes to 199.0 billion yen, and a 9.0% increase in net income, attributable to owners of the parent to 138.0 billion yen.

Economic value added (EVA) is forecast to increase due to an increase in net operating profit after tax (NOPAT).

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2) Forecast by Segment for the Fiscal Year Ending December 31, 2017

For the growth rates for each business segment below, sales for the previous fiscal year have been calculated using the same standard as for fiscal 2017.

In the Consumer Products Business in Japan, the market for household and personal care products is projected to grow slightly on a value basis. The cosmetics market is expected to remain flat. In overseas markets, growth is expected to continue in Asia, and a moderate recovery is projected in the Americas and Europe. In this situation, the Kao Group will work to create strong brands based on a high level of safety and reliability.

In the Beauty Care Business, the Kao Group will work to revitalize the market by adding greater value to products and proposing the Group's own originality and appeal while assessing changes in consumer attitudes toward beauty and lifestyle habits. In Japan, the Kao Group will promote initiatives including launches and cultivation of distinctive new products tailored to changes in consumer needs and reform of marketing activities and sales methods to meet changes in consumer purchasing behavior.

For cosmetics, the Kao Group will further aggressively promote the reform of Kao Sofina and Kanebo Cosmetics, brighten up their brand identities by accentuating the features of their respective products, and strive to restore their luster in the market. Outside Japan, the Kao Group will work to develop high-value-added products that incorporate its original technologies and nurture and strengthen core brands.

The Kao Group forecasts that sales in this business will increase 5.3% year on year to 601.0 billion yen.

The Human Health Care Business will promote product development focused on health care for both body and spirit. In food and beverage products, the Kao Group will capitalize on products approved as Foods for Specified Health Uses that are differentiated by their high level of functional health value, and enhance promotion of their functions while further expanding their base of loyal users. At the same time, the Kao Group will strengthen its health support solutions business in response to rising health consciousness as a result of mandatory special health examinations and specified health guidance in Japan. The Kao Group aims to create sanitary products that are gentle on skin and that offer greater comfort and a sense of confidence. In China, the Kao Group will strengthen the growing e-commerce channel and baby specialty store channel. In addition, the Kao Group will work to further enhance integration between its Japanese and overseas operations to meet the strong demand for Japanese-made baby diapers from outside Japan. In Indonesia, the Kao Group will expand its rollout of baby diapers produced locally targeting the middle-class consumer segment. The Kao Group will work to further raise the brand value of its personal health products by continuing to make original new proposals with products that can become healthy daily lifestyle habits.

The Kao Group forecasts that sales in this business will increase 8.7% year on year to 280.0 billion yen.

In the Fabric and Home Care Business, the Kao Group will strengthen its brands and offer proposals for enriched daily lives based on insights into changing consumer lifestyles, developing high-value-added products that offer cleanliness, comfort and enjoyment in various everyday situations. In collaboration with retailers, the Kao Group will further promote its "eco together" environmental statement with instructional activities that aim to reduce environmental impact throughout the entire lifecycle of products such as the *Neo* series, which includes *Ultra Attack Neo* ultra-concentrated liquid laundry detergent, and refill products for liquid and powder laundry detergents. The Kao Group will work to develop and nurture products that incorporate its technologies to meet local consumer needs in Asia and will expand its rollout of laundry detergent targeting the middle-class consumer segment in Indonesia.

The Kao Group forecasts that sales in this business will increase 2.9% year on year to 340.0 billion yen.

In the Chemical Business, the Kao Group will promote global supply of distinctive high-value-added chemical products that meet the diverse needs of a wide range of industries. In oleo chemicals, the Kao Group will stably supply high-quality products to meet increasing demand for fatty alcohols, fatty amines and higher-value-added derivatives made from natural oils and fats, mainly in Asia. In performance chemicals, growth is forecast in Asia, while the forecast for Japan includes an improved export environment for customer industries and demand for infrastructure. In specialty chemicals, the Kao Group will work to expand sales of products related to information materials and strive to offer products that anticipate customer trends.

In addition, the Kao Group will work to expand sales by opening up the markets of emerging nations, where growth is expected, while developing new materials using unique and environmentally conscious technologies in response to rising concern about global climate change.

As a result of the above, including adjustments in selling prices in response to fluctuations in raw material prices, the Kao Group forecasts that sales in this business will increase 3.9% year on year to 284.0 billion yen.

3) Underlying Assumptions of the Forecast for the Fiscal Year Ending December 31, 2017

The above forecast was made assuming translation rates of one U.S. dollar to 110 yen, one euro to 123 yen and one Chinese yuan to 16.8 yen.

Please note that although there is potential for volatility in prices of natural oils and fats and petrochemicals, assumptions for prices are based on information currently available to the Kao Group.

(2) Analysis of Financial Condition

Analysis of Assets, Liabilities, Equity and Cash Flows

1) Analysis of Assets, Liabilities, Equity and Cash Flows for the Fiscal Year Ended December 31, 2016

Summary of Consolidated Financial Position

(Billions of yen, except per share amounts)

	December 31, 2016	December 31, 2015	Incr./(Dcr.)
Total assets	1,338.3	1,311.1	27.2
Total liabilities	646.8	619.1	27.8
Total equity	691.5	692.0	(0.5)
Ratio of equity attributable to owners of the parent to total assets	50.8%	51.9%	-
Equity attributable to owners of the parent per share (Yen)	1,379.37	1,358.03	21.34
Bonds and borrowings	120.6	120.5	0.1

Summary of Consolidated Cash Flows

(Billions of yen)

	2016	2015	Incr./(Dcr.)
Net cash flows from operating activities	184.3	181.7	2.6
Net cash flows from investing activities	(88.6)	(74.1)	(14.5)
Free cash flow*	95.7	107.5	(11.9)
Net cash flows from financing activities	(95.0)	(20.8)	(74.3)

**Free cash flow is the sum of net cash flows from operating activities and net cash flows from investing activities.*

Total assets increased 27.2 billion yen from December 31, 2015 to 1,338.3 billion yen. The principal increases in assets were a 13.9 billion yen increase in inventories and a 32.8 billion yen increase in property, plant and equipment. The principal decreases in assets were a 6.9 billion yen decrease in cash and cash equivalents and a 14.2 billion yen decrease in other current assets.

Total liabilities increased 27.8 billion yen from December 31, 2015 to 646.8 billion yen. The principal increases in liabilities were a 10.1 billion yen increase in trade and other payables, a 5.7 billion yen increase in other current liabilities and a 19.1 billion yen increase in retirement benefit liabilities. The principal decrease in liabilities was a 9.3 billion yen decrease in provisions.

Total equity decreased 0.5 billion yen from December 31, 2015 to 691.5 billion yen. The principal increase in equity was net income totaling 127.9 billion yen. The principal decreases in equity were 50.0 billion yen due to purchase of treasury shares from the market, exchange differences on translation of foreign operations of 16.2 billion yen, remeasurements of defined benefit plans totaling 16.1 billion yen and dividends totaling 45.1 billion yen.

As a result of the above factors, the ratio of equity attributable to owners of the parent to total assets was 50.8% compared with 51.9% at December 31, 2015.

Net cash flows from operating activities totaled 184.3 billion yen. The principal increases in net cash were income before income taxes of 183.4 billion yen, depreciation and amortization of 51.1 billion yen and increase in retirement benefit liabilities of 20.0 billion yen. The principal decreases in net cash were increase in inventories of 17.4 billion yen, other, which includes accrued expenses, of 7.2 billion yen and income taxes paid of 48.7 billion yen.

Net cash flows from investing activities totaled negative 88.6 billion yen. This primarily consisted of payments into time deposits of 11.6 billion yen, purchase of property, plant and equipment of 74.6 billion yen and purchase of intangible assets of 5.1 billion yen.

Free cash flow, the sum of net cash flows from operating activities and net cash flows from investing activities, was 95.7 billion yen.

Net cash flows from financing activities totaled negative 95.0 billion yen. This primarily consisted of 50.0 billion yen for purchase of treasury shares and 45.1 billion yen for dividends paid to owners of the parent and non-controlling interests.

The balance of cash and cash equivalents at December 31, 2016 decreased 6.9 billion yen compared with December 31, 2015 to 303.0 billion yen, including the effect of exchange rate changes.

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2) Forecast of Assets, Liabilities, Net Assets and Cash Flows for the Fiscal Year Ending December 31, 2017

Net cash flows from operating activities are forecast to be approximately 190.0 billion yen, due in part to an increase in income before income taxes.

In net cash flows from investing activities, the Kao Group plans capital expenditures of approximately 75.0 billion yen, which will include aggressive investment for global expansion and capital investment for purposes such as increasing production capacity, promoting streamlining and improving distribution efficiency.

In net cash flows from financing activities, the Kao Group expects to pay cash dividends and to make other expenditures.

As a result of the above, the balance of cash and cash equivalents as of December 31, 2017 is forecast to increase approximately 60.0 billion yen from the previous fiscal year end to approximately 360.0 billion yen.

Cash Flow Indices

	2016	2015
Equity attributable to owner of the parent / Total assets (%)	50.8	51.9
Market capitalization / Total assets (%)	204.1	239.2
Interest-bearing debt / Operating cash flow (years)	0.7	0.7
Operating cash flow / Interest paid (times)	122.6	124.2

Notes:

1. *All figures are computed based on consolidated data.*
2. *Market capitalization is calculated based on the number of issued and outstanding shares less treasury shares.*
3. *Interest-bearing debt is all debt included in the consolidated statement of financial position on which interest is paid.*
4. *The Kao Group has applied IFRS from fiscal 2016, with a transition date of January 1, 2015. Accordingly, figures for fiscal 2014 and earlier are not presented.*

(3) Basic Policies Regarding Distribution of Profits and Dividends for the Fiscal Years Ended December 31, 2016 and Ending December 31, 2017

In order to achieve profitable growth, Kao Corporation (the Company) secures an internal reserve for capital investment and acquisitions from a medium-to-long-term management perspective and places priority on providing shareholders with steady and continuous dividends. In addition, the Company flexibly considers share repurchase and retirement of treasury shares from the standpoint of improving capital efficiency.

In accordance with these policies, the Company plans to pay a year-end dividend for fiscal 2016 of 48.00 yen per share, an increase of 6.00 yen per share compared with the previous fiscal year. Consequently, cash dividends for the fiscal year will increase 14.00 yen per share compared with the previous fiscal year, resulting in a total of 94.00 yen per share. The consolidated payout ratio will be 37.1%.

For fiscal 2017, the Company plans to pay total cash dividends of 108.00 yen per share, an increase of 14.00 yen per share compared with the previous fiscal year. Although the operating environment is challenging, this plan is in accordance with the Company’s basic policies regarding distribution of profits, and free cash flow and other factors have also been taken into consideration. As a result, the Company is aiming for its 28th consecutive fiscal year of increases in dividends.

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2. Management Policies

1) Management Policies of the Kao Group

The Kao Group's mission is to strive for the wholehearted satisfaction and enrichment of the lives of people globally and to contribute to the sustainability of the world, with products and brands of excellent value that are created from the consumer's and customer's perspective. This commitment is embraced by all members of the Kao Group as we work together with passion to share joy with consumers and customers in our core domains of cleanliness, beauty, health and chemicals.

The Kao Group aims to be a global company that is closest to the consumers and customers in each market, earning the respect and trust of its shareholders and all other stakeholders as it achieves "profitable growth."

In its corporate governance, the Kao Group works for ongoing innovation* and further enhances its internal control system to achieve management that is swift, efficient and sound, as well as impartial and transparent, as it continuously increases its corporate value.

**Innovation is one of the values of the Kao Way, the corporate philosophy of the Kao Group.*

The corporate philosophy that forms the basis of these activities is "The Kao Way," which clearly expresses the Kao Group's unique corporate culture and the essence of its corporate spirit, and is shared and practiced by all employees.

2) Management Metric Used as a Target

EVA, which is used to measure true profit by factoring in the cost of invested capital, is the Kao Group's principal management metric. Continuous growth in EVA is linked to increased corporate value, which means long-term profits not only for shareholders, but for all Kao Group stakeholders as well. The Kao Group views EVA growth as a primary focus of operating activity that expands business scale by making the maximum use of assets, and raising asset efficiency. The Kao Group also uses this metric to determine the direction of long-term management strategies, to assess specific businesses, to make evaluations on investment in facilities, acquisitions and other items, and to develop performance targets for each fiscal year.

3) Medium-to-long-term Management Strategies of the Kao Group

1. Long-term Management Strategy

(1) <u>Long-term Targets</u>

As vision by 2030 based on the above management policies, the Kao Group aims to make Kao a company with a global presence by combining sustained "profitable growth," and "contributions to the sustainability of the world" with proposals to resolve social issues and social contribution activities conducted through its business operations. To achieve this vision, the Kao Group will promote the further reinforcement of the existing businesses that are its strength and the creation of new markets from a global perspective utilizing the R&D capabilities that will create value for the future, in addition to implementing basic measures to further raise the level of safety and reliability.

It is becoming difficult to predict the various changes that will occur throughout the world in all aspects, such as speed, size and direction. To deal with this situation, the Kao Group aims to achieve the above vision by fully embracing the slogan of "transforming ourselves to drive change."

The Kao Group's vision by 2030 is as follows.
Make the Kao Group a company with a global presence that
■ Has a distinctive corporate image
■ Is a high-profit global consumer goods company that exceeds:
  - 2.5 trillion yen in net sales (1.0 trillion yen outside Japan)
  - 17% operating margin
  - 20% ROE
■ Provides a high level of returns to stakeholders

(2) Mid-term Business Plan
The Kao Group regards its mid-term business plan for the period to 2020 as an important milestone toward achieving its vision by 2030. To enhance corporate value, it established the Kao Group Mid-term Plan 2020 "K20" targeting the four years from fiscal 2017 to fiscal 2020 and announced it publicly on December 12, 2016.

K20 Goals – Three Commitments
■ Commitment to fostering a distinctive corporate image
  Become a company that is always by the consumer's side
■ Commitment to profitable growth
  - Continue to set new record highs for profits
  - Aim for like-for-like* net sales CAGR of +5%, operating margin of 15%
  - Three 100 billion yen brands (*Merries* baby diapers, *Attack* laundry detergents, *Bioré* skin care products)
    **Excluding the effect of currency translation, change of sales system, etc.*

■ Commitment to returns to stakeholders
  - Shareholders: Continuous cash dividend increases (40% payout ratio target)
  - Employees: Continuous improvement in compensation, benefits and health support
  - Customers: Maximization of win-win relationships
  - Society: Advanced measures to address social issues

The Kao Group has established Integrity, passed down from Kao's founder, as one of the core Values of its corporate philosophy, the Kao Way. Under K20, this Integrity will continue to be embraced in the Group's daily business activities as it maintains thorough quality control and information control, sincere consumer communications, strict compliance and effective crisis management. Through such endeavors, the Kao Group aims to reinforce its credibility in a global society.

4) Issues for Management

With intensifying market competition, changing market structure and volatility in raw material market conditions and exchange rates, the operating environment remains uncertain. Changes in the attitudes of consumers regarding the environment, health and other matters and associated changes in their purchasing attitudes, as well as the aging society, hygiene and other social issues, are growing in significance. Moreover, amid the global expansion of business and the progress of structural changes in various fields, companies must deal with changes in the risks entailed in their businesses.

Under these conditions, the Kao Group will continuously increase corporate value by addressing and dealing appropriately with the following issues.

(1) Regarding brightening products containing the ingredient Rhododenol sold by Kanebo Cosmetics, for which a voluntary recall was announced on July 4, 2013, Kanebo Cosmetics has been responding earnestly with support for the recovery and compensation of people who have experienced vitiligo-like symptoms. In addition, the entire Kao Group is making efforts with a view of the tasks before it as working to prevent recurrence while striving to ensure greater safety and reliability.

(2) To deal with changes in the risks entailed in its businesses, the Kao Group will define the serious company-wide risks among its main risks as corporate risks and work to prevent damage to the corporate value of the Group as a whole by further enhancing its management system.

5) Basic Approach to Selection of Accounting Standards

Having decided that unifying accounting standards within the Kao Group will contribute to improving the quality of its business management, the Kao Group has voluntarily adopted International Financial Reporting Standards (IFRS) from the fiscal 2016. This will enable management based on standardized procedures and information for each Group company and business, and the Kao Group intends to reinforce its management foundation in order to increase its corporate value as a global company. The Kao Group also believes that the application of IFRS will facilitate the international comparability of its financial statements in capital markets.

Consolidated Statement of Financial Position

(Millions of yen)

	December 31, 2016	December 31, 2015	Transition date January 1, 2015
Assets			
Current assets			
Cash and cash equivalents	303,026	309,922	228,967
Trade and other receivables	208,459	210,707	212,742
Inventories	165,200	151,271	151,876
Current income tax assets	1,462	2,077	1,261
Other financial assets	13,038	5,065	4,034
Other current assets	23,812	38,005	47,299
Subtotal	714,997	717,047	646,179
Non-current assets held for sale	344	1,330	-
Total current assets	715,341	718,377	646,179
Non-current assets			
Property, plant and equipment	370,835	337,997	319,282
Goodwill	137,783	138,251	138,751
Intangible assets	14,689	15,705	23,626
Investments accounted for using the equity method	4,701	4,209	3,544
Other financial assets	25,473	29,339	26,088
Other non-current assets	18,548	17,732	7,966
Deferred tax assets	50,939	49,454	61,194
Total non-current assets	622,968	592,687	580,451
Total assets	1,338,309	1,311,064	1,226,630

Consolidated Statement of Financial Position

(Millions of yen)

	December 31, 2016	December 31, 2015	Transition date January 1, 2015
Liabilities and equity			
Liabilities			
Current liabilities			
Trade and other payables	216,893	206,760	193,460
Bonds and borrowings	30,289	339	21,422
Income tax payables	32,621	32,184	28,283
Other financial liabilities	8,164	6,929	5,765
Provisions	11,370	16,772	33,360
Other current liabilities	131,112	125,422	123,916
Total current liabilities	430,449	388,406	406,206
Non-current liabilities			
Bonds and borrowings	90,357	120,207	80,188
Retirement benefit liabilities	94,773	75,706	77,895
Other financial liabilities	11,666	11,817	12,813
Provisions	13,809	17,704	5,296
Other non-current liabilities	5,264	4,919	5,411
Deferred tax liabilities	528	318	433
Total non-current liabilities	216,397	230,671	182,036
Total liabilities	646,846	619,077	588,242
Equity			
Share capital	85,424	85,424	85,424
Capital surplus	107,648	108,659	109,561
Treasury shares	(57,124)	(8,202)	(9,719)
Other components of equity	(21,821)	(4,184)	7,601
Retained earnings	565,715	499,299	431,975
Equity attributable to owners of the parent	679,842	680,996	624,842
Non-controlling interests	11,621	10,991	13,546
Total equity	691,463	691,987	638,388
Total liabilities and equity	1,338,309	1,311,064	1,226,630

Consolidated Satement of Income

(Millions of yen)

	Notes	Fiscal year ended December 31, 2016	Fiscal year ended December 31, 2015
Net sales	1	1,457,610	1,474,550
Cost of sales		(637,502)	(658,865)
Gross profit		820,108	815,685
Selling, general and administrative expenses	2	(633,368)	(642,729)
Other operating income		13,677	14,099
Other operating expenses		(14,846)	(19,737)
Operating income	1	185,571	167,318
Financial income		1,389	1,416
Financial expenses		(5,424)	(4,213)
Share of profit in investments accounted for using the equity method		1,894	1,517
Income before income taxes		183,430	166,038
Income taxes		(55,541)	(60,086)
Net income		127,889	105,952
Attributable to:			
Owners of the parent		126,551	105,196
Non-controlling interests		1,338	756
Net income		127,889	105,952
Earnings per share			
Basic (Yen)	3	253.43	209.82
Diluted (Yen)	3	253.18	209.53

Consolidated Statement of Comprehensive Income

(Millions of yen)

	Fiscal year ended December 31, 2016	Fiscal year ended December 31, 2015
Net income	127,889	105,952
Other comprehensive income		
Items that will not be reclassified to profit or loss:		
Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income	(906)	1,795
Remeasurements of defined benefit plans	(16,111)	(770)
Share of other comprehensive income of investments accounted for using the equity method	(72)	245
Total of items that will not be reclassified to profit or loss	(17,089)	1,270
Items that may be reclassified subsequently to profit or loss:		
Exchange differences on translation of foreign operations	(16,661)	(15,064)
Net gain (loss) on derivatives designated as cash flow hedges	-	12
Share of other comprehensive income of investments accounted for using the equity method	(10)	(19)
Total of items that may be reclassified subsequently to profit or loss	(16,671)	(15,071)
Other comprehensive income, net of taxes	(33,760)	(13,801)
Comprehensive income	94,129	92,151
Attributable to:		
Owners of the parent	93,284	93,011
Non-controlling interests	845	(860)
Comprehensive income	94,129	92,151

Consolidated Statement of Changes in Equity

(Millions of yen)

	Equity attributable to owners of the parent												
				Other components of equity									
	Share capital	Capital surplus	Treasury shares	Subscription rights to shares	Exchange differences on translation of foreign operations	Net gain (loss) on derivatives designated as cash flow hedges	Net gain (loss) on revaluation of financial assets measured at fair value through other compre-hensive income	Remeasur-ements of defined benefit plans	Total	Retained earnings	Total	Non-controlling interests	Total equity
January 1, 2016	85,424	108,659	(8,202)	902	(13,513)	(3)	8,430	-	(4,184)	499,299	680,996	10,991	691,987
Net income	-	-	-	-	-	-	-	-	-	126,551	126,551	1,338	127,889
Other comprehensive income	-	-	-	-	(16,248)	7	(970)	(16,056)	(33,267)	-	(33,267)	(493)	(33,760)
Comprehensive income	-	-	-	-	(16,248)	7	(970)	(16,056)	(33,267)	126,551	93,284	845	94,129
Disposal of treasury shares	-	-	1,099	(189)	-	-	-	-	(189)	(404)	506	-	506
Purchase of treasury shares	-	-	(50,021)	-	-	-	-	-	-	-	(50,021)	-	(50,021)
Share-based payment transactions	-	-	-	227	-	-	-	-	227	-	227	-	227
Dividends	-	-	-	-	-	-	-	-	-	(44,139)	(44,139)	(955)	(45,094)
Changes in the ownership interest in a subsidiary	-	(1,011)	-	-	-	-	-	-	-	-	(1,011)	1,007	(4)
Transfer from other components of equity to retained earnings	-	-	-	(29)	-	-	(435)	16,056	15,592	(15,592)	-	-	-
Other increase (decrease)	-	-	-	-	-	-	-	-	-	-	-	(267)	(267)
Total transactions with the owners	-	(1,011)	(48,922)	9	-	-	(435)	16,056	15,630	(60,135)	(94,438)	(215)	(94,653)
December 31, 2016	85,424	107,648	(57,124)	911	(29,761)	4	7,025	-	(21,821)	565,715	679,842	11,621	691,463
January 1, 2015	85,424	109,561	(9,719)	980	-	(4)	6,625	-	7,601	431,975	624,842	13,546	638,388
Net income	-	-	-	-	-	-	-	-	-	105,196	105,196	756	105,952
Other comprehensive income	-	-	-	-	(13,513)	1	2,041	(714)	(12,185)	-	(12,185)	(1,616)	(13,801)
Comprehensive income	-	-	-	-	(13,513)	1	2,041	(714)	(12,185)	105,196	93,011	(860)	92,151
Disposal of treasury shares	-	-	1,571	(231)	-	-	-	-	(231)	(375)	965	-	965
Purchase of treasury shares	-	-	(54)	-	-	-	-	-	-	-	(54)	-	(54)
Share-based payment transactions	-	-	-	225	-	-	-	-	225	-	225	-	225
Dividends	-	-	-	-	-	-	-	-	-	(37,091)	(37,091)	(1,248)	(38,339)
Changes in the ownership interest in a subsidiary	-	(902)	-	-	-	-	-	-	-	-	(902)	(334)	(1,236)
Transfer from other components of equity to retained earnings	-	-	-	(72)	-	-	(236)	714	406	(406)	-	-	-
Other increase (decrease)	-	-	-	-	-	-	-	-	-	-	-	(113)	(113)
Total transactions with the owners	-	(902)	1,517	(78)	-	-	(236)	714	400	(37,872)	(36,857)	(1,695)	(38,552)
December 31, 2015	85,424	108,659	(8,202)	902	(13,513)	(3)	8,430	-	(4,184)	499,299	680,996	10,991	691,987

Consolidated Statement of Cash Flows

(Millions of yen)

	Fiscal year ended December 31, 2016	Fiscal year ended December 31, 2015
Cash flows from operating activities		
Income before income taxes	183,430	166,038
Depreciation and amortization	51,116	57,423
Interest and dividend income	(1,247)	(1,266)
Interest expense	1,484	1,528
Share of profit in investments accounted for using the equity method	(1,894)	(1,517)
(Gains) losses on sale and disposal of property, plant and equipment, and intangible assets	3,466	3,497
(Increase) decrease in trade and other receivables	(4,049)	(4,882)
(Increase) decrease in inventories	(17,450)	(3,964)
Increase (decrease) in trade and other payables	4,388	9,707
Increase (decrease) in retirement benefit liabilities	19,967	(997)
Other	(7,175)	2,321
Subtotal	232,036	227,888
Interest received	1,003	1,004
Dividends received	1,479	1,315
Interest paid	(1,503)	(1,462)
Income taxes paid	(48,708)	(47,073)
Net cash flows from operating activities	184,307	181,672
Cash flows from investing activities		
Payments into time deposits	(11,570)	(2,669)
Proceeds from withdrawal of time deposits	3,703	1,355
Purchase of property, plant and equipment	(74,637)	(69,023)
Purchase of intangible assets	(5,060)	(5,598)
Acquisition of subsidiaries	(3,659)	-
Other	2,584	1,811
Net cash flows from investing activities	(88,639)	(74,124)
Cash flows from financing activities		
Increase (decrease) in short-term borrowings	(44)	(1,128)
Proceeds from long-term borrowings	200	40,080
Repayments of long-term borrowings	(317)	(20,068)
Purchase of treasury shares	(50,021)	(55)
Dividends paid to owners of the parent	(44,188)	(37,137)
Dividends paid to non-controlling interests	(955)	(1,248)
Other	282	(1,217)
Net cash flows from financing activities	(95,043)	(20,773)
Net increase (decrease) in cash and cash equivalents	625	86,775
Cash and cash equivalents at the beginning of the year	309,922	228,967
Effect of exchange rate changes on cash and cash equivalents	(7,521)	(5,820)
Cash and cash equivalents at the end of the year	303,026	309,922

Notes to Consolidated Financial Statements

(Changes in accounting principles and changes in accounting estimates)

Change in useful lives of property, plant and equipment

In conducting proactive capital investment, mainly in machinery and equipment, the Kao Group recognizes that the comparability of manufacturing costs for consideration on a global level of optimization of production bases is one of the issues it must address from a management perspective.

Consequently, the Kao Group globally unified its fixed asset systems in January 2016. The Kao Group decided to take advantage of this change to make the useful lives of machinery and equipment consistent (generally 9 or 10 years depending on the type of equipment) from the fiscal year ended December 31, 2016 to better reflect the actual use of machinery and equipment in global production. The effect of this change in accounting estimates on the consolidated financial statements is immaterial.

1. Segment Information

(1) Summary of reportable segments

Major products by reportable segment are as follows:

Reportable Segments		Major Products	
Consumer Products Business	Beauty Care Business	Cosmetics	Counseling cosmetics, Self-selection cosmetics
		Skin care products	Soaps, Facial cleansers, Body cleansers
		Hair care products	Shampoos, Conditioners, Hair styling agents, Hair coloring agents
	Human Health Care Business	Food and beverage products	Beverages
		Sanitary products	Sanitary napkins, Baby diapers
		Personal health products	Bath additives, Oral care products, Men's products
	Fabric and Home Care Business	Fabric care products	Laundry detergents, Fabric treatments
		Home care products	Kitchen cleaning products, House cleaning products, Paper cleaning products, Commercial-use products
Chemical Business		Oleo chemicals	Fatty alcohols, Fatty amines, Fatty acids, Glycerin, Commercial-use edible fats and oils
		Performance chemicals	Surfactants, Plastics additives, Superplasticizers for concrete admixtures
		Specialty chemicals	Toner and toner binder for copiers and printers, Ink and colorants for inkjet printers, Fragrances and aroma chemicals

(2) Sales and results of reportable segments

(Millions of yen)

Fiscal year ended December 31, 2016	Reportable Segments							
	Consumer Products Business				Chemical Business	Total	Reconciliations[1]	Consolidated
	Beauty Care Business	Human Health Care Business	Fabric and Home Care Business	Subtotal				
Net sales								
Sales to customers	601,620	273,067	345,163	1,219,850	237,760	1,457,610	-	1,457,610
Intersegment sales and transfers[2]	-	-	-	-	36,025	36,025	(36,025)	-
Total net sales	601,620	273,067	345,163	1,219,850	273,785	1,493,635	(36,025)	1,457,610
Operating income (loss)	51,086	25,948	78,099	155,133	29,683	184,816	755	185,571
% of net sales	8.5	9.5	22.6	12.7	10.8	12.4	-	12.7
Financial income								1,389
Financial expenses								(5,424)
Share of profit in investments accounted for using the equity method								1,894
Income before income taxes								183,430
Depreciation and amortization	18,399	12,930	7,876	39,205	11,650	50,855	261	51,116
Impairment loss	43	26	40	109	-	109	-	109
Capital Expenditure[3]	20,135	41,752	16,050	77,937	11,877	89,814	86	89,900

Notes:
1. The operating income reconciliation of 755 million yen includes corporate expenses not allocated to reportable segments, as well as elimination of intersegment inventory transactions.
2. Intersegment sales and transfers are mainly calculated based on market price and manufacturing cost.
3. Capital expenditures include investments in property, plant and equipment, intangible assets and other non-current assets.

Fiscal year ended December 31, 2015	Reportable Segments							
	Consumer Products Business				Chemical Business	Total	Reconciliations[1]	Consolidated
	Beauty Care Business	Human Health Care Business	Fabric and Home Care Business	Subtotal				
Net sales								
Sales to customers	608,617	281,672	335,308	1,225,597	248,953	1,474,550	-	1,474,550
Intersegment sales and transfers[2]	-	-	-	-	39,517	39,517	(39,517)	-
Total net sales	608,617	281,672	335,308	1,225,597	288,470	1,514,067	(39,517)	1,474,550
Operating income (loss)	37,929	33,368	66,124	137,421	28,593	166,014	1,304	167,318
% of net sales	6.2	11.8	19.7	11.2	9.9	11.0	-	11.3
Financial income								1,416
Financial expenses								(4,213)
Share of profit in investments accounted for using the equity method								1,517
Income before income taxes								166,038
Depreciation and amortization	26,028	10,236	8,072	44,336	12,804	57,140	283	57,423
Impairment loss	2,476	510	657	3,643	388	4,031	-	4,031
Capital Expenditure[3]	20,458	30,962	15,150	66,570	16,244	82,814	34	82,848

Notes:
1. The operating income reconciliation of 1,304 million yen includes corporate expenses not allocated to reportable segments, as well as elimination of intersegment inventory transactions.
2. Intersegment sales and transfers are mainly calculated based on market price and manufacturing cost.
3. Capital expenditures include investments in property, plant and equipment, intangible assets and other non-current assets.

(3) Geographical Information

The breakdown of sales to customers and non-current assets (excluding financial assets, deferred tax assets and retirement benefit assets) by geographic area is as follows:

(Millions of yen)

Sales to customers	Fiscal year ended December 31, 2016	Fiscal year ended December 31, 2015
Japan	964,904	956,033
Asia	251,284	249,335
(China)	103,346	96,565
Americas	120,782	134,080
(United States)	93,148	102,865
Europe	120,640	135,102
Total	1,457,610	1,474,550

Note: Sales are classified based on the location of customers.

Non-current assets (excluding financial assets, deferred tax assets and retirement benefit assets)	Fiscal year ended December 31, 2016	Fiscal year ended December 31, 2015	Transition date January 1, 2015
Japan	415,993	375,831	357,162
Asia	81,927	86,362	81,980
Americas	22,854	21,535	20,738
Europe	24,731	29,126	32,238
Total	545,505	512,854	492,118

2. Selling, General and Administrative Expenses

The breakdown of selling, general and administrative expenses is as follows:

(Millions of yen)

	Fiscal year ended December 31, 2016	Fiscal year ended December 31, 2015
Freight/warehouse	58,168	60,737
Advertising	97,437	94,745
Sales promotion	83,161	79,910
Employee benefits	191,122	191,392
Depreciation	11,236	11,695
Amortization	6,173	13,957
Research and development	54,567	52,699
Other	131,504	137,594
Total	633,368	642,729

3. Earnings per Share

(1) The basis for calculating basic earnings per share

(Millions of yen)

	Fiscal year ended December 31, 2016	Fiscal year ended December 31, 2015
Net income, attributable to owners of the parent	126,551	105,196
Amounts not attributable to ordinary shareholders of the parent	-	-
Net income used to calculate basic earnings per share	126,551	105,196
		(Thousands of shares)
Weighted average number of ordinary shares	499,355	501,352
		(Yen)
Basic earnings per share	253.43	209.82

(2) The basis for calculating diluted earnings per share

(Millions of yen)

	Fiscal year ended December 31, 2016	Fiscal year ended December 31, 2015
Net income used to calculate basic earnings per share	126,551	105,196
Adjustments to net income	-	-
Net income used to calculate diluted earnings per share	126,551	105,196
		(Thousands of shares)
Weighted average number of ordinary shares	499,355	501,352
Increase in ordinary shares		
Subscription rights to shares	483	701
Weighted average number of ordinary shares after dilution	499,838	502,053
		(Yen)
Diluted earnings per share	253.18	209.53
Summary of potential ordinary shares not included in the calculation of diluted earnings per share because they have no dilutive effect	-	-

4. Significant Subsequent Events

At its meeting held on February 2, 2017, the Board of Directors resolved to retire treasury shares in accordance with Article 178 of the Companies Act. The number of shares to be retired corresponds to the number of shares of Kao Corporation's shares purchased from the market during the fiscal year ended December 31, 2016.

Shares to be retired: Ordinary shares of the Company

Number of shares to be retired: 9,000,000 shares

Value of shares to be retired (plan): 48,429 million yen

Scheduled retirement date: March 1, 2017

Notes regarding Assumption of Going Concern

None applicable.