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Non-consolidated Financial Results for the Six Months Ended August 31, 2021 [IFRS]

October 13, 2021

Company name: Vario Secure Inc.

Stock exchange listing: Tokyo Stock Exchange

Code number: 4494

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Scheduled date of filing interim securities report: October 15, 2021

Scheduled date of commencing dividend payments: —

Availability of supplementary briefing material on interim financial results: Available

Schedule of interim financial results briefing session: Scheduled (for institutional investors and analysts, and individual investors)

(Amounts of less than one million yen are rounded down.)

1. Non-consolidated Financial Results for the Six Months Ended August 31, 2021 (March 1, 2021 to August 31, 2021)

(1) Non-consolidated Operating Results (% indicates changes from the previous corresponding period.)

	Revenue		Operating profit		Profit before tax		Profit		Total comprehensive income	
	Million yen	%	Million yen	%	Million yen	%	Million yen	%	Million yen	%
Six months ended										
August 31, 2021	1,283	1.7	363	(14.2)	337	(14.5)	233	(14.6)	233	(14.6)
August 31, 2020	1,262	0.6	423	5.5	394	7.3	273	7.5	273	7.5

	Basic earnings per share	Diluted earnings per share
Six months ended	Yen	Yen
August 31, 2021	61.86	59.20
August 31, 2020	73.41	73.41

(2) Non-Consolidated Financial Position

	Total assets	Total equity	Total equity ratio
	Million yen	Million yen	%
As of August 31, 2021	7,060	4,049	57.4
As of February 28, 2021	7,216	3,949	54.7

2. Dividends

	Annual dividends				
	1st quarter-end	2nd quarter-end	3rd quarter-end	Year-end	Total
Fiscal year ended February 28, 2021	Yen —	Yen 0.00	Yen -	Yen 39.44	Yen 39.44
Fiscal year ending February 28, 2022	—	0.00			
Fiscal year ending February 28, 2022 (Forecast)	—	0.00	-	40.44	40.44

Note: Revision to the forecast for dividends announced most recently: None

3. Non-consolidated Financial Results Forecast for the Fiscal Year Ending February 28, 2022 (March 1, 2021 to February 28, 2022)

(% indicates changes from the previous corresponding period.)

	Revenue		Operating profit		Profit before tax		Profit		Basic earnings per share
	Million yen	%	Million yen	%	Million yen	%	Million yen	%	Yen
Full year	2,649	4.1	782	2.4	732	3.4	507	3.3	134.79

Note: Revision to the financial results forecast announced most recently: None

* Notes:

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

- 1) Changes in accounting policies required by IFRS: None
- 2) Changes in accounting policies other than those in 1) above: None
- 3) Changes in accounting estimates: None

(2) Number of shares issued (common shares)

1) Total number of issued shares at the end of the period (including treasury shares):

As of August 31, 2021: 3,788,433 shares

As of February 28, 2021: 3,766,620 shares

2) Total number of treasury shares at the end of the period:

As of August 31, 2021: 29 shares

As of February 28, 2021: - shares

3) Average number of shares during the period:

Six months ended August 31, 2021: 3,774,875 shares

Six months ended August 31, 2020: 3,726,600 shares

* These interim financial results are not subject to interim review by certified public accountants or audit firms

* Explanation of the proper use of financial results forecast and other notes

Notes regarding forward-looking statements:

Financial results forecasts and other forward-looking statements contained in this document are based on information currently available to the Company and certain assumptions that management believes to be reasonable and do not represent a commitment from the Company that they will be achieved. Actual results may differ substantially for various reasons. For the assumptions underlying the financial results forecasts and other notices on the use of financial results forecasts, please refer to “(4) Explanation of Non-consolidated Financial Results Forecast and Other Forward-looking Information” of “1. Qualitative Information on Interim Financial Results for the Period under Review” in the accompanying materials.

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1. Qualitative Information on Interim Financial Results for the Period under Review

(1) Explanation of Business Results

During the six months ended August 31, 2021, there had been expectations for an economic recovery through an increase in vaccinations for preventing the spread of COVID-19. However, with the repeated and extended declaration of a state of emergency, no end of the pandemic was yet in sight. The outlook of the Japanese economy continues to remain uncertain, on the back of significant restrictions on economic activities both in Japan and overseas, due to the prolonged pandemic.

As for the environment in the security services market surrounding the Company, the investment demand for corporate security measures has continued expanding due to diversifying cyberattacks and attacks targeting the teleworking environment, which has become increasingly common as a measure to prevent the prolonged spread of COVID-19.

In particular, in conjunction with the nationwide expansion of teleworking needs, demand not only from super-large and large companies, which had previously been the drivers of such demand, but also new demand for adoption from mid-sized companies and SMEs, which were relatively reluctant toward security measures in the past, has increased. There has been a tendency for companies that have difficulty operating and managing their security to outsource operations and monitoring to security vendors, which has led to a steady expansion of the market, as a whole.

In addition, regarding the procurement of materials, the Company August be affected by a global shortage of semiconductors. Although it is difficult to rationally calculate the effect on the Company's performance at the moment, the Company will continue to monitor the situation.

In such an environment, the Company reported stable sales, exceeding those of the corresponding period of the previous fiscal year, thanks to the recurring revenue from Managed Security Services and a low cancellation rate (0.78%) (Note). Each level of profit declined year on year, due to an increase in cost of sales in conjunction with the increased revenue, construction costs of a security operation center, and investments for future growth such as recruitment aimed at strengthening of sales and management departments.

As a result of the above, in the financial results on an IFRS basis for the six months ended August 31, 2021, the Company reported revenue of ¥1,283,709 thousand (a year-on-year increase of 1.7%), operating profit of ¥363,058 thousand (a year-on-year decrease of 14.2%), profit before tax of ¥337,217 thousand (a year-on-year decrease of 14.5%), and profit of ¥233,521 thousand (a year-on-year decrease of 14.6%).

The results by segment are not stated, as the Company's segments comprise the single segment of Internet Security Services.

Note: Cancellation rate (monetary basis) = Cancellation amount for the six months ended August 31, 2021 / (Monthly revenue at the beginning of each fiscal year × 6)

(2) Explanation of Financial Position

The financial position on an IFRS basis as of August 31, 2021 was as follows.

Assets

Total assets as of August 31, 2021 was ¥7,060,004 thousand, a decrease of ¥156,160 thousand from the end of the previous fiscal year. This was primarily due to increases of ¥28,472 thousand in inventories and ¥31,481 thousand in intangible assets, as well as decreases of ¥179,389 thousand in cash and cash equivalents and ¥41,216 thousand in property, plant and equipment.

Liabilities

Total liabilities as of August 31, 2021 was ¥3,010,383 thousand, a decrease of ¥256,414 thousand from the end of the previous fiscal year. This was primarily due to an increase of ¥1,602,390 thousand in borrowings under current liabilities, as well as decreases of ¥36,872 thousand in lease liabilities and ¥1,786,677 thousand in borrowings under non-current liabilities.

Equity

Total equity as of August 31, 2021 was ¥4,049,621 thousand, an increase of ¥100,254 thousand from the end of the previous fiscal year. This was primarily due to an increase of ¥233,521 thousand in retained earnings as a result of reporting profit, and a decrease in retained earnings as a result of reporting dividends of ¥148,555 thousand.

(3) Analysis of Cash Flows

Cash flows on an IFRS basis for the six months ended August 31, 2021 were as follows.

Cash and cash equivalents as of August 31, 2021 decreased by ¥179,389 thousand from the end of the previous fiscal year to ¥414,541 thousand.

Cash flows from operating activities

Net cash provided by operating activities during the six months ended August 31, 2021 was ¥243,480 thousand (¥217,035 thousand was provided in the corresponding period of the previous fiscal year). Major cash inflows included ¥337,217 thousand in profit before tax and ¥62,316 thousand in depreciation and amortization, while major cash outflows included a ¥28,472 thousand increase in inventories and ¥107,123 thousand in income taxes paid.

Cash flows from investing activities

Net cash used in investing activities during the six months ended August 31, 2021 was ¥53,508 thousand (¥57,174 thousand was used in the corresponding period of the previous fiscal year). Major cash outflows included ¥45,241 thousand for the purchase of intangible assets.

Cash flows from financing activities

Net cash used in financing activities during the six months ended August 31, 2021 was ¥369,361 thousand (¥235,232 thousand was used in the corresponding period of the previous fiscal year). Major cash outflows included ¥200,000 thousand for repayments of long-term borrowings, ¥147,869 thousand for dividends paid, and ¥30,192 thousand for repayments of lease liabilities.

(4) Explanation of Non-consolidated Financial Results Forecast and Other Forward-looking Information

Financial results forecasts and other forward-looking statements contained in this document are based on information currently available to the Company and certain assumptions that management believes to be reasonable and actual results may differ substantially for various reasons. The impact of COVID-19 on the Company's performance is minimal. Therefore, regarding the financial results forecast for the fiscal year ending February 28, 2022, the forecast announced on April 12, 2021 will remain unchanged, and timely disclosures will be provided, if management determines that it is necessary to revise the earnings forecast, in light of business trends going forward.

2. Interim Condensed Non-consolidated Financial Statements and Primary Notes

(1) Interim Condensed Non-consolidated Statements of Financial Position

(Thousand yen)

	As of February 28, 2021	As of August 31, 2021
	<hr/>	<hr/>
Assets		
Current assets		
Cash and cash equivalents	593,930	414,541
Trade and other receivables	461,320	464,014
Inventories	119,743	148,215
Other current assets	144,196	161,396
Total current assets	<hr/> 1,319,190	<hr/> 1,188,167
Non-current assets		
Property, plant and equipment	293,232	252,015
Goodwill	5,054,613	5,054,613
Intangible assets	173,412	204,893
Other financial assets	63,384	63,384
Deferred tax assets	139,881	125,735
Other non-current assets	172,450	171,194
Total non-current assets	<hr/> 5,896,974	<hr/> 5,871,836
Total assets	<hr/> <hr/> 7,216,165	<hr/> <hr/> 7,060,004

(Thousand yen)

	As of February 28, 2021	As of August 31, 2021
Liabilities and equity		
Liabilities		
Current liabilities		
Borrowings	369,763	1,972,153
Trade and other payables	108,005	120,547
Income taxes payable	120,432	104,701
Other current liabilities	394,476	378,782
Total current liabilities	992,678	2,576,184
Non-current liabilities		
Borrowings	1,786,677	-
Lease liabilities	102,725	65,852
Provisions	18,336	18,360
Other non-current liabilities	366,380	349,986
Total non-current liabilities	2,274,119	434,199
Total liabilities	3,266,798	3,010,383
Equity		
Share capital	320,072	327,195
Capital surplus	1,629,850	1,638,064
Retained earnings	1,999,444	2,084,410
Treasury shares	-	(49)
Total equity	3,949,366	4,049,621
Total liabilities and equity	7,216,165	7,060,004

(2) Interim Condensed Non-consolidated Statements of Profit or Loss and Comprehensive Income
Interim Condensed Non-consolidated Statements of Profit or Loss
Six Months Ended August 31

	(Thousand yen)	
	For the six months ended August 31, 2020 (from March 1, 2020 to August 31, 2020)	For the six months ended August 31, 2021 (from March 1, 2021 to August 31, 2021)
Revenue	1,262,767	1,283,709
Cost of sales	463,701	490,996
Gross profit	799,066	792,712
Selling, general and administrative expenses	375,960	429,523
Other income	70	63
Other expenses	-	194
Operating profit	423,177	363,058
Finance income	221	2
Finance costs	29,111	25,843
Profit before tax	394,287	337,217
Income tax expense	120,706	103,696
Profit	273,580	233,521
Earnings per share		
Basic earnings per share (yen)	73.41	61.86
Diluted earnings per share (yen)	73.41	59.20

Interim Condensed Non-consolidated Statements of Comprehensive Income
Six Months Ended August 31

	(Thousand yen)	
	For the six months ended August 31, 2020 (from March 1, 2020 to August 31, 2020)	For the six months ended August 31, 2021 (from March 1, 2021 to August 31, 2021)
Profit	273,580	233,521
Other comprehensive income	-	-
Comprehensive income	273,580	233,521

(3) Interim Condensed Non-consolidated Statements of Changes in Equity

For the six months ended August 31, 2020 (from March 1, 2020 to August 31, 2020)

					(Thousand yen)
	Share capital	Capital surplus	Retained earnings	Treasury shares	Total
As of March 1, 2020	310,000	1,590,985	1,507,909	-	3,408,894
Profit	-	-	273,580	-	273,580
Other comprehensive income	-	-	-	-	-
Total comprehensive income	-	-	273,580	-	273,580
Share-based remuneration transactions	-	5,771	-	-	5,771
Total transactions with owners	-	5,771	-	-	5,771
As of August 31, 2020	<u>310,000</u>	<u>1,596,756</u>	<u>1,781,490</u>	<u>-</u>	<u>3,688,246</u>

For the six months ended August 31, 2021 (from March 1, 2021 to August 31, 2021)

					(Thousand yen)
	Share capital	Capital surplus	Retained earnings	Treasury shares	Total
As of March 1, 2021	320,072	1,629,850	1,999,444	-	3,949,366
Profit	-	-	233,521	-	233,521
Other comprehensive income	-	-	-	-	-
Total comprehensive income	-	-	233,521	-	233,521
Purchase of treasury shares	-	-	-	(49)	(49)
Dividends	-	-	(148,555)	-	(148,555)
Exercise of share acquisition rights	4,625	4,625	-	-	9,250
Share-based remuneration transactions	2,498	3,589	-	-	6,087
Total transactions with owners	7,123	8,214	(148,555)	(49)	(133,267)
As of August 31, 2021	<u>327,195</u>	<u>1,638,064</u>	<u>2,084,410</u>	<u>(49)</u>	<u>4,049,621</u>

(4) Interim Condensed Non-consolidated Statements of Cash Flows

	(Thousand yen)	
	For the six months ended August 31, 2020 (from March 1, 2020 to August 31, 2020)	For the six months ended August 31, 2021 (from March 1, 2021 to August 31, 2021)
Cash flows from operating activities		
Profit before tax	394,287	337,217
Depreciation and amortization	57,275	62,316
Finance income	(221)	(2)
Finance costs	29,111	25,843
Decrease (increase) in inventories	(14,244)	(28,472)
Decrease (increase) in trade and other receivables	(24,569)	(2,694)
Decrease (increase) in other current assets	(9,937)	(17,200)
Decrease (increase) in other non-current assets	1,806	1,256
Increase (decrease) in trade and other payables	(17,041)	13,468
Increase (decrease) in other current liabilities	(35,135)	(23,170)
Increase (decrease) in other non-current liabilities	15,008	(16,394)
Other	4,299	7,115
Subtotal	<u>400,639</u>	<u>359,283</u>
Interest received	2	2
Interest paid	(9,981)	(8,682)
Income taxes paid	<u>(173,624)</u>	<u>(107,123)</u>
Cash flows from operating activities	217,035	243,480
Cash flows from investing activities		
Purchase of property, plant and equipment	(7,517)	(8,267)
Purchase of intangible assets	<u>(49,657)</u>	<u>(45,241)</u>
Cash flows from investing activities	(57,174)	(53,508)
Cash flows from financing activities		
Proceeds from exercise of share acquisition rights	-	9,250
Repayments of long-term borrowings	(200,000)	(200,000)
Repayments of lease liabilities	(34,732)	(30,192)
Purchase of treasury shares	-	(49)
Dividends paid	-	(147,869)
Other	(499)	(499)
Cash flows from financing activities	<u>(235,232)</u>	<u>(369,361)</u>
Net increase (decrease) in cash and cash equivalents	(75,371)	(179,389)
Cash and cash equivalents at the beginning of the period	632,229	593,930
Net effect of currency translation on cash and cash equivalents	-	0
Cash and cash equivalents at the end of the period	<u><u>556,857</u></u>	<u><u>414,541</u></u>

(5) Notes to Interim Condensed Non-consolidated Financial Statements

Notes on going concern assumption

Not applicable

Changes in accounting policies

Not applicable

Changes in accounting estimates

Not applicable

Segment information

This information is omitted, as the Company's segments comprise the single segment of Internet Security Services.

Events after the reporting period

(Conclusion of a capital and business alliance agreement)

The Company, at its Board of Directors meeting held on September 10, 2021, resolved to carry out a capital and business alliance (hereinafter, the "Capital and Business Alliance") with HEROZ, Inc. (hereinafter, "HEROZ"), and concluded a capital and business alliance agreement as of the same date.

(1) Purpose and rationale

Under the management philosophy, "To ensure that all enterprises using the Internet can easily and securely carry out their business, we will offer the very best services to Japan and to the world," the Company, as a provider of Internet security services, offers comprehensive network security services to protect companies' networks from a variety of threats, including cyber-attacks, unauthorized access to internal networks, computer virus infections, and data theft, and to ensure the safe use of the Internet.

HEROZ, building on its concept of "a heart filled with amazement," offers services that utilize AI to make people's lives more convenient and enjoyable, by providing applications such as intellectual games on smartphones and tablet devices for individuals, as well as AI services such as machine learning in various fields for corporate customers.

The Company has decided to carry out the Capital and Business Alliance, in an effort to establish a framework for the continuous creation of new services that can only be achieved by a dedicated group of engineers, through the combination of the "AI human resources of HEROZ" and the "rare domain knowledge held by the Company's security human resources."

(2) Details of the business alliance

The Company and HEROZ aim to create and expand sales of new products and services, while generating and maximizing synergies to increase the corporate value of both companies, by mutually providing and collaborating on management resources, including the industry domain knowledge and data held by the Company and the AI technology held by HEROZ.

(3) Details of the capital alliance

On September 13, 2021, HEROZ acquired 1,224,000 shares of the Company's common shares (32.31%, rounded off to two decimal places, of the total number of issued shares as of August 31, 2021) held by iSigma Business Advancement Fund No. 2 (hereinafter, "iSigma Fund No. 2") and i-Sigma BAF Officers' and Employees' Fund 5i Partnership, for a total of ¥1,958,400 thousand (¥1,600 per share).

As a result, HEROZ replaced iSigma Fund No. 2, and became an entity with significant influence over the Company, in accordance with IFRS.

(4) Overview of the counterparty of the capital alliance

1)	Company name	HEROZ, Inc.
2)	Location	2F PMO Tamachi, 5-31-17, Shiba, Minato-Ku, Tokyo
3)	Name and title of representative	Takahiro Hayashi, Co-CEO
4)	Business description	Planning, development, and operation of services utilizing AI technology
5)	Capital	¥2,276,959 thousand (as of April 30, 2021)

(5) Impact on financial results

The impact of the Capital and Business Alliance on the Company's financial results for the fiscal year ending February 28, 2022 is currently under review. However, the Company has determined that the alliance will contribute to an improvement of financial results in the medium to long term.