



Non-consolidated Financial Results for the Six Months Ended August 31, 2022 [IFRS]

October 7, 2022

Company name: Vario Secure Inc.

Stock exchange listing: Tokyo Stock Exchange

Code number: 4494

URL: <https://www.variosecure.net/>

Representative: Yoshihiko Inami, CEO

Contact: Hideko Isoe, Director, General Manager, Office of the President

Phone: +81-3-5577-3284

Scheduled date of filing interim securities report: October 11, 2022

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)

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

1. Non-consolidated Financial Results for the Six Months Ended August 31, 2022 (March 1, 2022 to August 31, 2022)

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

	Revenue		Operating profit		Profit before tax		Profit		Total comprehensive income	
Six months ended	Million yen	%	Million yen	%	Million yen	%	Million yen	%	Million yen	%
August 31, 2022	1,337	4.2	385	6.3	355	5.3	245	5.1	245	5.1
August 31, 2021	1,283	1.7	363	(14.2)	337	(14.5)	233	(14.6)	233	(14.6)

	Basic earnings per share	Diluted earnings per share
Six months ended	Yen	Yen
August 31, 2022	64.56	62.74
August 31, 2021	61.86	59.20

(2) Non-Consolidated Financial Position

	Total assets	Total equity	Total equity ratio
	Million yen	Million yen	%
As of August 31, 2022	7,123	4,417	62.0
As of February 28, 2022	7,122	4,323	60.7

2. Dividends

	Annual dividends				
	1st quarter-end	2nd quarter-end	3rd quarter-end	Year-end	Total
Fiscal year ended February 28, 2022	Yen —	Yen 0.00	Yen -	Yen 40.44	Yen 40.44
Fiscal year ending February 28, 2023	—	0.00			
Fiscal year ending February 28, 2023 (Forecast)			-	40.50	40.50

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

3. Non-consolidated Financial Results Forecast for the Fiscal Year Ending February 28, 2023 (March 1, 2022 to February 28, 2023)

(% indicates changes from the previous corresponding period.)

	Revenue		Operating profit		Profit before tax		Profit		Basic earnings per share
Full year	Million yen	%	Million yen	%	Million yen	%	Million yen	%	Yen
	2,650	3.2	785	4.4	756	7.9	525	4.9	128.01

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

Basic earnings per share for the fiscal year ending February 28, 2023 is calculated based on the most recent numbers of shares concerning the third-party allotment conducted on September 27, 2022.

* 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, 2022: 3,802,613 shares

As of February 28, 2022: 3,799,413 shares

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

As of August 31, 2022: 470 shares

As of February 28, 2022: 29 shares

3) Average number of shares during the period:

Six months ended August 31, 2022: 3,800,441 shares

Six months ended August 31, 2021: 3,774,875 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, 2022, expectations for the Japanese economy to return to normal were rising as the spread of COVID-19 showed signs of settling down. Meanwhile, the outlook overseas was mired by concerns over economic instability given surging resource prices worldwide due to the prolonged Russia-Ukraine situation and fluctuations in the financial markets of countries around the world.

As for the environment in the security services market surrounding the Company, the investment demand for corporate security measures has continued expanding, due to increases in cyberattacks targeting supply chains and the threat of ransomware attacks (ransom-demanding-type viruses) targeting organizations such as general companies and hospitals.

Furthermore, amidst major changes in the corporate system network environment as a result of an increase in teleworking due to the impact of COVID-19 and other factors, 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 such an environment, the Company has expanded sales promotion of Vario Managed EDR, which detects signs of cyberattacks as an endpoint security measure, and data backup services (VDaP) that protect corporate information assets from the growing threat of ransomware attacks (ransom-demanding-type viruses), in addition to conventional gateway security, in order to support the development of a secure and safe business environment through multilayered defense against an increasing array of threats. As a successor model to our in-house developed network security equipment VSR (Vario Secure Router), we released the scalable model “VSR n series” with the aim towards linking it with services of other companies.

In addition, regarding the procurement of materials, the Company may be affected by a global shortage of semiconductors. At the moment, although the Company expects the effect of such a shortage to be minimal for the fiscal year ending February 28, 2023, it is difficult to rationally calculate the effect on the Company’s performance for the fiscal year ending February 28, 2024 onward, and the Company will continue to monitor the situation.

In such an environment, the Company reported revenue exceeding that of the corresponding period of the previous fiscal year, and each level of profit under operating profit also increased year on year, due to the recurring revenue from Managed Security Services and a low cancellation rate (0.82%) (Note).

As result of the above, in the financial results on an IFRS basis for the six months ended August 31, 2022, the Company reported revenue of ¥1,337,217 thousand (a year-on-year increase of 4.2%), operating profit of ¥385,940 thousand (a year-on-year increase of 6.3%), profit before tax of ¥355,137 thousand (a year-on-year increase of 5.3%), and profit of ¥245,367 thousand (a year-on-year increase of 5.1%).

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, 2022 / (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, 2022 was as follows.

Assets

Total assets as of August 31, 2022 was ¥7,123,749 thousand, an increase of ¥1,679 thousand from the end of the previous fiscal year. This was primarily due to increases of ¥25,319 thousand in trade and other receivables, ¥62,188 thousand in inventories and ¥64,711 thousand in other current assets, as well as decreases of ¥150,609 thousand in cash and cash equivalents.

Liabilities

Total liabilities as of August 31, 2022 was ¥2,706,703 thousand, a decrease of ¥92,307 thousand from the end of the previous fiscal year. This was primarily due to an increase of ¥1,400,000 thousand in borrowings under non-current liabilities, as well as decreases of ¥1,486,677 thousand in borrowings under current liabilities.

Equity

Total equity as of August 31, 2022 was ¥4,417,045 thousand, an increase of ¥93,987 thousand from the end

of the previous fiscal year. This was primarily due to an increase of ¥245,367 thousand in retained earnings as a result of reporting profit, and a decrease in retained earnings as a result of reporting dividends of ¥153,647 thousand.

(3) Analysis of Cash Flows

Cash flows on an IFRS basis for the six months ended August 31, 2022 were as follows.

Cash and cash equivalents as of August 31, 2022 decreased by ¥150,609 thousand from the end of the previous fiscal year to ¥239,237 thousand.

Cash flows from operating activities

Net cash provided by operating activities during the six months ended August 31, 2022 was ¥201,648 thousand (¥243,480 thousand was provided in the corresponding period of the previous fiscal year). Major cash inflows included ¥355,137 thousand in profit before tax and ¥76,181 thousand in depreciation and amortization, while major cash outflows included a ¥62,188 thousand increase in inventories, ¥64,096 increase in other current assets and ¥84,944 thousand in income taxes paid.

Cash flows from investing activities

Net cash used in investing activities during the six months ended August 31, 2022 was ¥63,249 thousand (¥53,508 thousand was used in the corresponding period of the previous fiscal year). Major cash outflows included ¥56,682 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, 2022 was ¥289,002 thousand (¥369,361 thousand was used in the corresponding period of the previous fiscal year). Major cash inflows included ¥100,000 thousand net increase in short-term borrowings and ¥1,600,000 thousand proceeds from long-term borrowings, while major cash outflows included ¥1,800,000 thousand for repayments of long-term borrowings and ¥153,193 thousand for dividends paid.

(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, 2023, the forecast announced on April 13, 2022 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, 2022	As of August 31, 2022
Assets		
Current assets		
Cash and cash equivalents	389,846	239,237
Trade and other receivables	464,748	490,067
Inventories	218,104	280,293
Other current assets	176,377	241,088
Total current assets	1,249,077	1,250,687
Non-current assets		
Property, plant and equipment	206,726	165,666
Goodwill	5,054,613	5,054,613
Intangible assets	242,733	271,907
Other financial assets	63,384	63,384
Deferred tax assets	131,673	126,695
Other non-current assets	173,860	190,794
Total non-current assets	5,872,992	5,873,061
Total assets	7,122,069	7,123,749

	(Thousand yen)	
	As of February 28, 2022	As of August 31, 2022
Liabilities and equity		
Liabilities		
Current liabilities		
Borrowings	1,786,677	300,000
Trade and other payables	134,211	124,288
Income taxes payable	93,513	114,501
Other current liabilities	389,580	393,106
Total current liabilities	2,403,981	931,896
Non-current liabilities		
Borrowings	-	1,400,000
Lease liabilities	28,837	-
Provisions	18,384	18,408
Other non-current liabilities	347,807	356,398
Total non-current liabilities	395,029	1,774,807
Total liabilities	2,799,011	2,706,703
Equity		
Share capital	330,018	330,818
Capital surplus	1,641,719	1,643,223
Retained earnings	2,351,369	2,443,089
Treasury shares	(49)	(85)
Total equity	4,323,058	4,417,045
Total liabilities and equity	7,122,069	7,123,749

(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, 2021 (from March 1, 2021 to August 31, 2021)	For the six months ended August 31, 2022 (from March 1, 2022 to August 31, 2022)
Revenue	1,283,709	1,337,217
Cost of sales	490,996	539,240
Gross profit	792,712	797,977
Selling, general and administrative expenses	429,523	413,515
Other income	63	1,478
Other expenses	194	0
Operating profit	363,058	385,940
Finance income	2	1
Finance costs	25,843	30,804
Profit before tax	337,217	355,137
Income tax expense	103,696	109,770
Profit	233,521	245,367
Earnings per share		
Basic earnings per share (yen)	61.86	64.56
Diluted earnings per share (yen)	59.20	62.74

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

		(Thousand yen)
	For the six months ended August 31, 2021 (from March 1, 2021 to August 31, 2021)	For the six months ended August 31, 2022 (from March 1, 2022 to August 31, 2022)
Profit	233,521	245,367
Other comprehensive income	-	-
Comprehensive income	233,521	245,367

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

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	327,195	1,638,064	2,084,410	(49)	4,049,621

For the six months ended August 31, 2022 (from March 1, 2022 to August 31, 2022)

					(Thousand yen)
	Share capital	Capital surplus	Retained earnings	Treasury shares	Total
As of March 1, 2022	330,018	1,641,719	2,351,369	(49)	4,323,058
Profit	-	-	245,367	-	245,367
Other comprehensive income	-	-	-	-	-
Total comprehensive income	-	-	245,367	-	245,367
Purchase of treasury shares	-	-	-	(36)	(36)
Dividends	-	-	(153,647)	-	(153,647)
Exercise of share acquisition rights	800	800	-	-	1,600
Share-based remuneration transactions	-	703	-	-	703
Total transactions with owners	800	1,503	(153,647)	(36)	(151,379)
As of August 31, 2022	330,818	1,643,223	2,443,089	(85)	4,417,045

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

		(Thousand yen)
	For the six months ended August 31, 2021 (from March 1, 2021 to August 31, 2021)	For the six months ended August 31, 2022 (from March 1, 2022 to August 31, 2022)
Cash flows from operating activities		
Profit before tax	337,217	355,137
Depreciation and amortization	62,316	76,181
Finance income	(2)	(1)
Finance costs	25,843	30,804
Decrease (increase) in inventories	(28,472)	(62,188)
Decrease (increase) in trade and other receivables	(2,694)	(25,319)
Decrease (increase) in other current assets	(17,200)	(64,096)
Decrease (increase) in other non-current assets	1,256	(16,924)
Increase (decrease) in trade and other payables	13,468	(10,967)
Increase (decrease) in other current liabilities	(23,170)	10,479
Increase (decrease) in other non-current liabilities	(16,394)	8,591
Other	7,115	(6,411)
Subtotal	359,283	295,283
Interest received	2	1
Interest paid	(8,682)	(8,691)
Income taxes paid	(107,123)	(84,944)
Cash flows from operating activities	243,480	201,648
Cash flows from investing activities		
Purchase of property, plant and equipment	(8,267)	(6,566)
Purchase of intangible assets	(45,241)	(56,682)
Cash flows from investing activities	(53,508)	(63,249)
Cash flows from financing activities		
Proceeds from exercise of share acquisition rights	9,250	1,600
Net increase (decrease) in short-term borrowings	-	100,000
Proceeds from long-term borrowings	-	1,600,000
Repayments of long-term borrowings	(200,000)	(1,800,000)
Repayments of lease liabilities	(30,192)	(36,872)
Purchase of treasury shares	(49)	(36)
Dividends paid	(147,869)	(153,193)
Other	(499)	(499)
Cash flows from financing activities	(369,361)	(289,002)
Net increase (decrease) in cash and cash equivalents	(179,389)	(150,603)
Cash and cash equivalents at the beginning of the period	593,930	389,846
Net effect of currency translation on cash and cash equivalents	0	(5)
Cash and cash equivalents at the end of the period	414,541	239,237

(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, issuance of new shares by a third-party allotment, and change in parent of the Company)

The Company, at its Board of Directors meeting held on September 9, 2022, resolved to conclude a capital and business alliance agreement (hereinafter, the “Capital and Business Alliance Agreement,” and the capital and business alliance pursuant to the Capital and Business Alliance Agreement is referred to as the “Capital and Business Alliance”) with HEROZ, Inc. (hereinafter, “HEROZ”), and to issue new shares by a third-party allotment to HEROZ (hereinafter, collectively the “Third-Party Allotment”). As the payment was completed on September 27, 2022, HEROZ newly became the parent of the Company.

(1) The Capital and Business Alliance

1) Purpose and rationale of the Capital and Business Alliance

Under the mission, “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 offers comprehensive network security services. We have built the stable business foundation to date with our main business which has been Internet gateway security services (perimeter security services) using network security equipment (Vario Secure Router, VSR) developed by the Company, and 84.4% of revenue was earned as recurring revenue through monthly charges (for the fiscal year ended February 28, 2022).

However, as the global situation changes drastically, the required network security measures are changing, and more proactive and immediate action is needed to respond to these changes. We have come to the conclusion that we need to strengthen the following points in order to achieve future growth by establishing a structure that enables us to quickly develop services and respond to the security needs of companies and information system divisions with excellent sensitivity, while understanding the situation in a broader scope.

- Acquisition of human resources to establish a foundation for growth
- Acceleration of service development
- Expansion of business domain of Managed Security Services (operation) (Note)

Note: “Managed Security Services” refers to 24/7/365 operation and monitoring services mainly in the network security domain.

2) Details of the capital alliance

The Company will allot 710,000 shares of its common shares to HEROZ by a third-party allotment (the percentage of voting rights held to the total voting rights after the capital increase by the Third-Party Allotment: 42.88%).

(2) Schedule of the Capital and Business Alliance

Date of resolution by the Board of Directors	September 9, 2022
Date of conclusion of the Capital and Business Alliance Agreement	September 9, 2022
Due date of payment for third-party allotment	September 27, 2022

(3) Issuance of new shares by the Third-Party Allotment

1) Overview of offering

(1) Payment period	From September 27, 2022 to September 29, 2022
(2) Number of new shares issued	710,000 shares of common shares
(3) Issuance price	¥1,178 per share
(4) Amount of funds procured	¥836,380,000 For the estimated net proceeds after deducting the estimated issue costs, please refer to “3). Amount, use, and expected timing of use of funds procured” below.
(5) Method of offering or allotment (Allottee)	Allotment of shares of the Company’s common shares to HEROZ by a third-party allotment
(6) Other	The Company and HEROZ, the allottee, concluded the Capital and Business Alliance Agreement as of September 9, 2022. Under the Capital and Business Alliance Agreement, the payment for the capital increase by the Third-Party Allotment is subject to the effectiveness of the securities registration statement under the Financial Instruments and Exchange Act and other conditions.

2) Purpose and rationale of the Third-Party Allotment

They are as described in “(1) The Capital and Business Alliance, 1) Purpose and rationale of the Capital and Business Alliance.”

3) Amount, use, and expected timing of use of funds procured

i. Amount of funds procured

(Thousand yen)

Total payment	Estimated issue costs	Estimated net proceeds
836,380	23,000	813,380

Notes:

1. The estimated issue costs do not include consumption tax, etc.
2. The estimated issue costs include legal fees of ¥10,000 thousand, advisory fees of ¥3,000 thousand, registration-related expenses of ¥3,000 thousand, share administration fees of ¥500 thousand, and other costs of ¥6,500 thousand.
3. Until the funds are actually used, they will be managed in a bank account.

ii. Specific use of funds procured

Specific use	Amount (Thousand yen)	Expected timing of use
(1) Personnel expenses for planning new services and establishing a structure for developing them and strengthening the sales department	258,380	March 2023 to February 2026
(2) Expenses for development of new services	100,000	March 2023 to February 2026
(3) Expenses to strengthen the operation services of the security operation center (SOC)	55,000	March 2023 to February 2026
(4) Funds for investments in companies with our peripheral technologies and services	400,000	March 2024 to February 2026
Total of above	813,380	—

(4) Change in parent of the Company

1) Circumstances giving rise to the change

In September 2021, the Company formed a capital and business alliance with HEROZ, and HEROZ

acquired 32.31% of the Company's common shares (as a percentage to the Company's total number of issued shares as of August 31, 2021) on September 13, 2021. As a result of the capital increase by the Third-Party Allotment, HEROZ, the allottee, became the new parent of the Company.

2) Overview of the shareholder change

(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	¥10,000 thousand (as of April 30, 2022)		
(6)	Date of establishment	April 30, 2009		
(7)	Total number of issued shares	15,025,582 shares		
(8)	Fiscal year closed	April 30		
(9)	Number of employees	61		
(10)	Main customers	Apple Japan, LLC, Google Inc., etc.		
(11)	Main bank	Mizuho Bank, Ltd.		
(12)	Major shareholders and percentage of shareholding (as of April 30, 2022)	Takahiro Hayashi		28.83%
		Tomohiro Takahashi		28.83%
		The Master Trust Bank of Japan, Ltd. (Trust Account)		4.16%
		BIGLOBE Inc.		2.66%
		Bandai Namco Entertainment Inc.		1.17%
		Netmarble Japan Inc.		1.17%
		KOEI TECHMO GAMES CO., LTD.		1.11%
		TAKENAKA CORPORATION		1.08%
		KIA FUND F149		0.99%
Rakuten Securities, Inc.		0.76%		
(13)	Relationship between the listed company and the company (as of August 31, 2022)	Capital relationship	HEROZ holds 32.21% of the Company’s voting rights.	
		Personal relationship	One director of the Company concurrently serves as a director of HEROZ.	
		Business relationship	There are transactions in which HEROZ provides AI services to the Company.	
		Status as a related party	HEROZ is a related party as defined in Article 8, Paragraph 17 of the Regulation on Terminology, Forms, and Preparation Methods of Financial Statements.	
(14) Operating results and financial condition of the company for the past three years				
	Fiscal year	Fiscal year ended April 30, 2020	Fiscal year ended April 30, 2021	Fiscal year ended April 30, 2022
	Net assets	¥6,182 million	¥6,403 million	¥6,440 million
	Total assets	¥6,408 million	¥6,546 million	¥6,635 million
	Net assets per share	¥414.46	¥426.13	¥428.65
	Net sales	¥1,544 million	¥1,556 million	¥1,482 million
	Operating profit	¥459 million	¥294 million	¥34 million
	Ordinary profit	¥404 million	¥285 million	¥87 million
	Profit	¥255 million	¥207 million	¥49 million
	Earnings per share	¥17.84	¥13.85	¥3.29
	Dividend per share	¥—	¥—	¥—

3) Number of voting rights (number of shares held) held by the shareholder before and after the change and percentage to the total number of voting rights held by all shareholders

HEROZ, Inc.

	Attribute	Number of voting rights (percentage to the total number of voting rights held by all shareholders)			Major shareholder ranking
		Direct	Indirect	Total	
Before the change	Other subsidiary/associate and major and largest shareholder	12,240 units (32.21%)	– unit (–%)	12,240 units (32.21%)	1
After the change	Parent company and major and largest shareholder	19,340 units (42.88%)	– unit (–%)	19,340 units (42.88%)	1

Notes:

1. The above table is based on the shareholder register as of August 31, 2022.
2. The major shareholder ranking after the change has been determined based on the situation as of August 31, 2022.
3. The percentage to the total number of voting rights held by all shareholders is calculated based on the total number of issued shares less treasury shares and shares less than one unit and rounded to two decimal places.

4) Date of change

Issuance date of the shares (September 27, 2022)