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Appendix

# ***TOKYO OHKA KOGYO CO., LTD. and Subsidiaries***

Fiscal year ended December 31, 2018  
(January 1, 2018 — December 31, 2018)

***Consolidated financial statements,  
Notes to consolidated financial statements***

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## TOKYO OHKA KOGYO CO., LTD. and Consolidated Subsidiaries

### Consolidated Balance Sheets December 31, 2018 and 2017

<u>ASSETS</u>	Millions of yen		Thousands of U.S. dollars (Note 1)
	2018	2017	2018
<b>CURRENT ASSETS:</b>			
Cash and deposits (Notes 5 and 17)	¥ 37,851	¥ 27,961	\$ 341,006
Time deposits (Note 17)	18,241	16,219	164,341
Receivables:			
Trade notes and accounts (Note 17)	22,539	22,554	203,060
Securities (Notes 5, 6 and 17)	2,000	2,000	18,018
Other	493	422	4,449
Allowance for doubtful accounts	(48)	(157)	(438)
Inventories (Note 7)	17,245	15,893	155,364
Deferred tax assets (Note 14)	1,687	1,574	15,204
Prepaid expenses and other current assets	1,577	1,249	14,213
Total current assets	101,589	87,719	915,219
<b>PROPERTY, PLANT AND EQUIPMENT (Note 8):</b>			
Land	8,996	9,120	81,052
Buildings and structures	63,330	62,902	570,545
Machinery and equipment	57,203	56,406	515,344
Furniture and fixtures	20,712	20,684	186,602
Construction in progress	3,393	4,077	30,568
Total	153,636	153,192	1,384,114
Accumulated depreciation	(105,277)	(101,488)	(948,449)
Net property, plant and equipment	48,358	51,703	435,665
<b>INVESTMENTS AND OTHER ASSETS:</b>			
Investment securities (Notes 6 and 17)	12,910	16,486	116,312
Investments in and advanced to an unconsolidated subsidiary and associated companies	7	1,164	67
Investment in capital	220	—	1,981
Net defined benefit asset (Note 10)	2,065	2,352	18,611
Long-term time deposits (Note 17)	18,000	18,000	162,162
Deferred tax assets (Note 14)	438	145	3,954
Other assets	1,091	1,108	9,837
Total investments and other assets	34,734	39,258	312,927
<b>TOTAL</b>	<b>¥ 184,683</b>	<b>¥ 178,681</b>	<b>\$ 1,663,812</b>

See notes to consolidated financial statements.

<u>LIABILITIES AND EQUITY</u>	<u>Millions of yen</u>		<u>Thousands of</u>
	<u>2018</u>	<u>2017</u>	<u>U.S. dollars</u> <u>(Note 1)</u>
			<u>2018</u>
<b>CURRENT LIABILITIES:</b>			
Payables:			
Trade notes and accounts (Note 17)	¥ 11,381	¥ 10,444	\$ 102,538
Construction and other	3,834	4,966	34,541
Income taxes payable	1,130	962	10,184
Accrued expenses	3,983	3,652	35,888
Advances from customers	88	236	796
Deferred tax liabilities (Note 14)	198	329	1,791
Other current liabilities (Notes 17)	957	1,151	8,626
	<u>21,574</u>	<u>21,742</u>	<u>194,367</u>
<b>LONG-TERM LIABILITIES:</b>			
Long-term loans payable (Note 9 and 17)	10,000	—	90,090
Deferred tax liabilities (Note 14)	1,625	2,533	14,646
Net defined benefit liability (Note 10)	306	262	2,757
Other long-term liabilities (Note 11 and 17)	318	625	2,872
	<u>12,250</u>	<u>3,421</u>	<u>110,366</u>
<b>EQUITY (Notes 12 and 20):</b>			
Common stock—authorized, 197,000,000 shares in 2018 authorized, 197,000,000 shares in 2017 issued, 45,100,000 shares in 2018 issued, 45,100,000 shares in 2017	14,640	14,640	131,895
Capital surplus	15,207	15,207	137,008
Retained earnings	120,885	116,904	1,089,054
Treasury stock—at cost, 3,436,262 shares in 2018 and 3,021,037 shares in 2017	(13,816)	(11,732)	(124,470)
Accumulated other comprehensive income:			
Unrealized gain on available-for-sale securities	4,315	6,893	38,875
Foreign currency translation adjustments	3,137	4,646	28,268
Remeasurements of defined benefit plans	(239)	335	(2,159)
Total	144,130	146,896	1,298,471
Stock acquisition rights	310	247	2,797
Non-controlling interests	6,416	6,373	57,808
	<u>150,857</u>	<u>153,517</u>	<u>1,359,078</u>
<b>TOTAL</b>	<u>¥ 184,683</u>	<u>¥ 178,681</u>	<u>\$ 1,663,812</u>

## TOKYO OHKA KOGYO CO., LTD. and Consolidated Subsidiaries

### Consolidated Statements of Income Years Ended December 31, 2018 and 2017

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2018	2017	2018
NET SALES	¥105,277	¥ 92,411	\$ 948,443
COST OF SALES (Notes 7, 13 and 15)	71,896	63,805	647,714
Gross profit	33,380	28,606	300,729
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES (Notes 10, 13 and 15)	22,875	19,411	206,083
Operating income	10,505	9,194	94,645
OTHER INCOME (EXPENSES):			
Interest and dividend income	392	309	3,531
Foreign exchange gain (loss) —net	(580)	726	(5,226)
Gain (loss) on valuation of derivatives	306	(789)	2,757
Loss on impairment of long-lived assets (Note 8)	(860)	(242)	(7,750)
Other—net	50	294	457
Other (expenses) income —net	(691)	298	(6,230)
INCOME BEFORE INCOME TAXES AND NON- CONTROLLING INTERESTS	9,814	9,492	88,414
INCOME TAXES (Note 14):			
Current	2,141	2,140	19,291
Deferred	(187)	348	(1,692)
Total income taxes	1,953	2,489	17,598
NET INCOME BEFORE NON-CONTROLLING INTERESTS	7,860	7,003	70,815
NON-CONTROLLING INTERESTS IN NET INCOME	984	996	8,870
PROFIT ATTRIBUTABLE TO OWNERS OF THE PARENT	¥ 6,875	¥ 6,007	\$ 61,945

## TOKYO OHKA KOGYO CO., LTD. and Consolidated Subsidiaries

### Consolidated Statements of Income Years Ended December 31, 2018 and 2017

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	Yen		U.S. dollars
	2018	2017	2018
PER SHARE OF COMMON STOCK (Notes 13 and 20):			
Basic profit	¥ 164.92	¥ 138.31	\$ 1.48
Diluted profit	164.44	137.91	1.48
Cash dividends applicable to the year	96.00	64.00	0.86

See notes to consolidated financial statements.

**TOKYO OHKA KOGYO CO., LTD. and Consolidated Subsidiaries**

**Consolidated Statements of Comprehensive Income**  
**Years Ended December 31, 2018 and 2017**

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2018	2017	2018
NET INCOME BEFORE NON-CONTROLLING INTERESTS	¥ 7,860	¥ 7,003	\$ 70,815
OTHER COMPREHENSIVE INCOME (Note 19):			
Unrealized (loss) gain on available-for-sale securities	(2,578)	2,199	(23,229)
Foreign currency translation adjustments	(1,751)	1,457	(15,781)
Remeasurements of defined benefit plans	(575)	475	(5,184)
Share of other comprehensive income in an associate	(113)	(19)	(1,018)
Total other comprehensive income	(5,018)	4,112	(45,214)
COMPREHENSIVE INCOME (Note 19)	¥ 2,841	¥ 11,115	\$ 25,601
TOTAL COMPREHENSIVE INCOME ATTRIBUTABLE TO (Note 19):			
Owners of the parent	¥ 2,213	¥ 9,794	\$ 19,939
Non-controlling interests	628	1,321	5,661

See notes to consolidated financial statements.

**TOKYO OHKA KOGYO CO., LTD. and Consolidated Subsidiaries**

**Consolidated Statements of Changes in Equity  
Years Ended December 31, 2018 and 2017**

	Thousands		Millions of yen									
	Number of shares of common stock outstanding	Common stock	Capital surplus	Retained earnings	Treasury stock	Accumulated other comprehensive income (loss)			Total	Subscription rights to shares	Non- controlling interests	Total equity
						Unrealized (loss) gain on available-for-sale securities	Foreign currency translation adjustments	Remeasurements of defined benefit plans				
BALANCE, APRIL 1, 2017	43,603	¥ 14,640	¥ 15,207	¥ 113,708	¥ (4,086)	¥ 4,694	¥ 3,533	¥ (139)	¥ 147,559	¥ 221	¥ 5,150	¥ 152,931
Profit attributable to owners of the parent	—	—	—	6,007	—	—	—	—	6,007	—	—	6,007
Cash dividends paid:												
Final for prior year, ¥32.0 per share	—	—	—	(1,396)	—	—	—	—	(1,396)	—	—	(1,396)
Interim for current year, ¥32.0 per share	—	—	—	(1,397)	—	—	—	—	(1,397)	—	—	(1,397)
Purchase of treasury stock	(1,593)	—	—	—	(7,809)	—	—	—	(7,809)	—	—	(7,809)
Disposal of treasury stock	69	—	—	(18)	163	—	—	—	144	(26)	—	118
Net change in the year	—	—	—	—	—	2,199	1,112	475	3,787	52	1,222	5,062
BALANCE, DECEMBER 31, 2017	42,078	14,640	15,207	116,904	(11,732)	6,893	4,646	335	146,896	247	6,373	153,517
Profit attributable to owners of the parent	—	—	—	6,875	—	—	—	—	6,875	—	—	6,875
Cash dividends paid:												
Final for prior year, ¥32.0 per share	—	—	—	(1,346)	—	—	—	—	(1,346)	—	—	(1,346)
Interim for current year, ¥36.0 per share	—	—	—	(1,499)	—	—	—	—	(1,499)	—	—	(1,499)
Purchase of treasury stock	(442)	—	—	—	(2,194)	—	—	—	(2,194)	—	—	(2,194)
Disposal of treasury stock	27	—	—	(49)	110	—	—	—	61	(17)	—	43
Net change in the year	—	—	—	—	—	(2,578)	(1,508)	(575)	(4,662)	80	43	(4,538)
BALANCE, DECEMBER 31, 2018	41,663	¥ 14,640	¥ 15,207	¥ 120,885	¥(13,816)	¥ 4,315	¥ 3,137	¥ (239)	¥ 144,130	¥ 310	¥ 6,416	¥ 150,857

**TOKYO OHKA KOGYO CO., LTD. and Consolidated Subsidiaries**

**Consolidated Statements of Changes in Equity  
Years Ended December 31, 2018 and 2017**

Thousands of U.S. dollars (Note 1)

	Common stock	Capital surplus	Retained earnings	Treasury stock	Accumulated other comprehensive income (loss)			Total	Subscription rights to shares	Non- controlling interests	Total equity
					Unrealized (loss) gain on available-for-sale securities	Foreign currency translation adjustments	Remeasurements of defined benefit plans				
BALANCE, DECEMBER 31, 2017	\$ 131,895	\$ 137,008	\$ 1,053,192	\$(105,694)	\$ 62,105	\$ 41,859	\$ 3,025	\$ 1,323,391	\$ 2,231	\$ 57,415	\$ 1,383,038
Profit attributable to owners of the parent	—	—	61,945	—	—	—	—	61,945	—	—	61,945
Cash dividends paid:											
Final for prior year, \$0.28 per share	—	—	(12,130)	—	—	—	—	(12,130)	—	—	(12,130)
Interim for current year, \$0.32 per share	—	—	(13,510)	—	—	—	—	(13,510)	—	—	(13,510)
Purchase of treasury stock	—	—	—	(19,772)	—	—	—	(19,772)	—	—	(19,772)
Disposal of treasury stock	—	—	(441)	996	—	—	—	554	(158)	—	396
Net change in the year	—	—	—	—	(23,229)	(13,591)	(5,184)	(42,006)	725	392	(40,888)
BALANCE, DECEMBER 31, 2018	<u>\$ 131,895</u>	<u>\$ 137,008</u>	<u>\$ 1,089,054</u>	<u>\$(124,470)</u>	<u>\$ 38,875</u>	<u>\$ 28,268</u>	<u>\$ (2,159)</u>	<u>\$ 1,298,471</u>	<u>\$ 2,797</u>	<u>\$ 57,808</u>	<u>\$ 1,359,078</u>

See notes to consolidated financial statements.



# TOKYO OHKA KOGYO CO., LTD. and Consolidated Subsidiaries

## Consolidated Statements of Cash Flows Years Ended December 31, 2018 and 2017

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2018	2017	2018
<b>OPERATING ACTIVITIES:</b>			
Income before income taxes and non-controlling interests	¥ 9,814	¥ 9,492	\$ 88,414
Adjustments for:			
Income taxes paid	(2,221)	(2,286)	(20,013)
Depreciation and amortization	7,063	6,035	63,638
Provision for doubtful accounts	(244)	(130)	(2,201)
Foreign exchange loss (gain) —net	983	(1,131)	8,856
Loss on impairment of long-lived assets	860	242	7,750
(Gain) loss on valuation of derivatives	(306)	789	(2,757)
Increase in net defined benefit asset	(455)	(151)	(4,100)
Decrease in net defined benefit liability	(37)	(18)	(342)
Increase in trade notes and accounts receivable	(420)	(2,286)	(3,788)
Increase in inventories	(1,770)	(1,929)	(15,953)
Increase in trade notes and accounts payable	1,092	755	9,844
(Increase) decrease in consumption taxes refund receivable	(268)	295	(2,419)
Other—net	223	485	2,009
Net cash provided by operating activities	<u>14,311</u>	<u>10,162</u>	<u>128,936</u>
<b>INVESTING ACTIVITIES:</b>			
Deposit for time deposits—net	(2,150)	(386)	(19,372)
Purchases of property, plant and equipment	(6,491)	(5,884)	(58,485)
Purchases of intangible assets	(234)	(155)	(2,111)
Payments into long-term time deposits	(14,000)	(3,000)	(126,126)
Withdrawal of long-term time deposits	14,000	3,000	126,126
Purchases of investment securities	(210)	—	(1,893)
Proceeds from sales of investment securities	1,081	0	9,739
Other—net	(8)	432	(74)
Net cash used in investing activities	<u>(8,013)</u>	<u>(5,993)</u>	<u>(72,197)</u>
<b>FINANCING ACTIVITIES:</b>			
Proceeds of long-term loans payable	10,000	—	90,090
Repayments of long-term loans payable	—	(138)	—
Dividends paid	(2,841)	(2,785)	(25,602)
Dividends paid for non-controlling interests	(584)	(98)	(5,269)
Purchases of treasury stock	(2,212)	(7,823)	(19,934)
Other—net	(27)	173	(246)
Net cash provided by (used in) financing activities	<u>4,333</u>	<u>(10,673)</u>	<u>39,036</u>

**TOKYO OHKA KOGYO CO., LTD. and Consolidated Subsidiaries**

**Consolidated Statements of Cash Flows**  
**Years Ended December 31, 2018 and 2017**

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2018	2017	2018
FOREIGN CURRENCY TRANSLATION ADJUSTMENTS ON CASH AND CASH EQUIVALENTS	¥ (741)	¥ 557	\$ (6,677)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	9,889	(5,945)	89,098
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	29,961	35,907	269,925
CASH AND CASH EQUIVALENTS, END OF YEAR (Note 5)	<u>¥ 39,851</u>	<u>¥ 29,961</u>	<u>\$ 359,024</u>

See notes to consolidated financial statements.

## TOKYO OHKA KOGYO CO., LTD. and Consolidated Subsidiaries

### Notes to Consolidated Financial Statements Years Ended December 31, 2018 and 2017

#### 1. BASIS OF PRESENTING CONSOLIDATED FINANCIAL STATEMENTS

The accompanying consolidated financial statements have been prepared in accordance with the provisions set forth in the Japanese Financial Instruments and Exchange Act and its related accounting regulations and in conformity with accounting principles generally accepted in Japan (“Japanese GAAP”), which are different in certain respects as to application and disclosure requirements of International Financial Reporting Standards.

In preparing these consolidated financial statements, certain reclassifications and rearrangements have been made to the consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan. In addition, certain amounts reported in prior years have been reclassified to conform to the current year’s presentation.

The consolidated financial statements are stated in Japanese yen, the currency of the country in which TOKYO OHKA KOGYO CO., LTD. (the “Company”) is incorporated and operates. The translations of Japanese yen amounts into U.S. dollar amounts are included solely for the convenience of readers outside Japan and have been made at the rate of ¥111 to \$1, the approximate rate of exchange at December 31, 2018. Such translations should not be construed as representations that the Japanese yen amounts could be converted into U.S. dollars at that or any other rate.

Amounts of less than one million yen have been rounded off. As a result, the totals shown in the accompanying consolidated financial statements (both in yen and U.S. dollars) do not necessarily agree with the sum of the individual amounts.

#### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

- a. Consolidation*— The consolidated financial statements include the accounts of the Company and its eight significant subsidiaries (together, the “Group”).

Under the control or influence concept, those companies in which the Company, directly or indirectly, is able to exercise control over operations are fully consolidated, and those companies over which the Group has the ability to exercise significant influence are accounted for by the equity method.

Investment in an associated company COTEM Co., Ltd. was excluded from the scope of applying the equity method as the shares of the company was transferred during the nine months ended September 30, 2018. Investments in an unconsolidated subsidiary and an associated company are not accounted for by the equity method but are stated at cost as their effect on the consolidated financial statements is immaterial.

All significant intercompany balances and transactions have been eliminated in consolidation. All material unrealized profit included in assets resulting from transactions within the Group is eliminated.

- b. Cash Equivalents*— Cash and cash equivalents include cash on hand, demand deposits, and short-term investments with original maturities of three months or less that are readily convertible into cash and exposed to insignificant risk of changes in value.
- c. Allowance for Doubtful Accounts*— The allowance for doubtful accounts is stated in amounts considered to be appropriate based on the Group’s past credit loss experience and an evaluation of potential losses in the receivables outstanding.
- d. Inventories*— Merchandise, work in process, raw materials and supplies are stated at the lower of cost, determined by the first-in, first-out method, or net selling value. Finished products are stated at the lower of cost, determined by the average method, or net selling value. Inventories of manufacturing equipment are

stated at the lower of cost, determined by the specific identification method, or net selling value, which are included in raw materials, work in process and finished products.

- e. **Investment Securities**— Investment securities are classified and accounted for, depending on management's intent, as follows: (i) held-to-maturity debt securities, which are expected to be held to maturity with the positive intent and ability to hold to maturity, are reported at cost and (ii) available-for-sale securities, other than (i), are reported at fair value, with unrealized gains and losses, net of applicable taxes, reported in a separate component of equity.

Non-marketable available-for-sale securities are stated at cost determined by the moving-average method.

For other than temporary declines in fair value, investment securities are reduced to net realizable value by a charge to income.

- f. **Property, Plant and Equipment**— Property, plant and equipment are stated at cost. Depreciation of property, plant and equipment, except for lease assets, of the Company and its consolidated domestic subsidiaries is computed by the straight-line method. The range of useful lives is principally from 10 to 50 years for buildings and structures, and from 3 to 8 years for machinery and equipment, and furniture and fixtures.

- g. **Long-Lived Assets**— The Group reviews its long-lived assets for impairment whenever events or changes in circumstance indicate the carrying amount of an asset or asset group may not be recoverable. An impairment loss would be recognized if the carrying amount of an asset or asset group exceeds the sum of the undiscounted future cash flows expected to result from the continued use and eventual disposition of the asset or asset group. The impairment loss would be measured as the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of the discounted cash flows from the continued use and eventual disposition of the asset or the net selling price at disposition.

- h. **Other Assets**— Intangible assets are stated at cost less accumulated amortization, which is calculated by the straight-line method principally over 5 years.

- i. **Retirement Benefits**

*Retirement benefits to employees (including officers)*— The Company and its certain consolidated subsidiaries have funded defined benefit pension plans and lump-sum retirement payment plans.

The companies principally accounted for the retirement benefit obligations based on the projected benefit obligations and plan assets at each balance sheet date.

Prior service cost is amortized by the straight-line method over 10 years. Actuarial gains and losses are amortized by the straight-line method over 10 years from the next period in which they arise.

- j. **Asset Retirement Obligations**— The Group recognizes assets retirement obligation for buildings and sub stations in the domestic offices in accordance with the relevant laws. The amount of the asset retirement obligations is calculated with the estimated usable years of 8 to 50 years from the acquisition and the discount rate ranging from 0.4% to 2.3%.

- k. **Research and Development Costs**— Research and development costs are charged to income as incurred.

- l. **Leases** — Leased assets under the finance lease arrangements where the ownership is not transferred to lessees at the end of lease terms are capitalized to recognize lease assets and lease obligations in the balance sheet, except for leases which existed at April 1, 2008 and do not transfer ownership of the leased property to the lessee which are accounted for as operating lease transactions.

All other leases are accounted for as operating leases.

- m. **Bonuses to Directors and Corporate Auditors**— Bonuses to directors and corporate auditors are accrued at the year-end to which such bonuses are attributable.

- n. **Income Taxes**— The provision for income taxes is computed based on the pretax income included in the

consolidated statements of income. The asset and liability approach is used to recognize deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. Deferred taxes are measured by applying currently enacted tax laws to the temporary differences.

- o. Foreign Currency Transactions*— All short-term and long-term monetary receivables and payables denominated in foreign currencies are translated into Japanese yen at the current exchange rates as of the balance sheet date. The foreign exchange gains and losses from translation are recognized in the consolidated statements of income to the extent that they are not hedged by forward exchange contracts.
- p. Foreign Currency Financial Statements*— The balance sheet accounts of the consolidated foreign subsidiaries are translated into Japanese yen at the current exchange rate as of the balance sheet date except for equity, which is translated at the historical rate. Revenue and expense accounts of consolidated foreign subsidiaries are translated into Japanese yen at the average exchange rate during the period. Differences arising from such translation were recorded in “Foreign currency translation adjustments” and “Non-controlling interests” in Equity.
- q. Derivative and Hedging Activities*— The Group uses derivative financial instruments to manage its exposures to the fluctuation in foreign currency exchange. Foreign currency forward contracts are utilized by the Group to hedge foreign exchange risk. The Group does not enter into derivatives for trading or speculative purposes.

Trade receivables and payables denominated in foreign currencies for which foreign currency forward contracts are used to hedge foreign exchange risk are translated at the contracted rate if the forward contracts qualify for hedge accounting.

- r. Per Share Information*— Basic net income per share is computed by dividing net income available to common shareholders by the weighted-average number of common shares outstanding during the period.

Diluted net income per share reflects the potential dilution that could occur if securities with dilutive effects were exercised. Diluted net income per share of common stock assumes full exercise of outstanding warrants at the beginning of the year.

Cash dividends per share presented in the accompanying consolidated statements of income are dividends attributable to the respective years including dividends to be paid after the end of the year.

### 3. CHANGES IN ACCOUNTING POLICIES

Effective January 1, 2018, the Company’s overseas consolidated subsidiaries applied IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with Customers. The impact of applying these standards on the consolidated financial statements for the fiscal year ended December 31, 2018 was immaterial.

### 4. ACCOUNTING STANDARD ISSUED BUT NOT YET ADOPTED

New or revised accounting standards issued as of December 31, 2018 but not yet adopted by the Group are as follows.

- 1. The Company and its domestic subsidiaries
  - Accounting Standard for Revenue Recognition (ASBJ Statement No. 29, March 30, 2018)
  - Implementation Guidance on Accounting Standard for Revenue Recognition (ASBJ Guidance No. 30, March 30, 2018)
  - (1) Outline
    - The International Accounting Standards Board (IASB) and the U.S. Financial Accounting Standards Board (FASB) jointly developed comprehensive accounting standards for revenue recognition and issued Revenue from Contracts with Customers in May 2014 as IFRS 15 by IASB and as Topic 606 by FASB, becoming effective for annual reporting periods beginning on or after January 1, 2018, and those beginning after December 15, 2017, respectively. In light of this situation, the Accounting Standards Board of Japan

(ASBJ) developed and issued a comprehensive accounting standard for revenue recognition along with its implementation guidance.

The basic policy of ASBJ in developing an accounting standard for revenue recognition was to incorporate the fundamental principles of IFRS 15 as a starting point from the perspective of comparability between financial statements, which is one of the benefits of maintaining consistency with IFRS 15, with alternative treatments added for items requiring consideration of practices which have been generally accepted in Japan, if any, to the extent that comparability is not impaired.

(2) Scheduled date of application

The standard and its implementation guidance are scheduled to be applied from the fiscal year ending December 31, 2022.

(3) Impact of the application of the standard and its implementation guidance

The Company is currently evaluating the impact of applying “Accounting Standard for Revenue Recognition” and its implementation guidance on the consolidated financial statements.

2. Overseas subsidiaries

IFRS 16 Lease

(1) Outline

The new accounting standard requires lessees to recognize assets and liabilities on the balance sheet for nearly all leases.

(2) Scheduled date of application

The standard is scheduled to be applied from the fiscal year ending December 31, 2019.

(3) Impact of the application of the standard and its implementation guidance

The impact of applying the accounting standard on the consolidated financial statements is immaterial.

## 5. CASH AND CASH EQUIVALENTS

The balances of cash and deposits reflected in the consolidated balance sheets at December 31, 2018 and 2017 were reconciled to the balances of cash and cash equivalents as presented in the consolidated statements of cash flows for the years then ended as follows:

	Millions of yen		Thousands of U.S. dollars
	2018	2017	2018
Cash and deposits	¥ 37,851	¥ 27,961	\$ 341,006
Securities	2,000	2,000	18,018
Cash and cash equivalents	<u>¥ 39,851</u>	<u>¥ 29,961</u>	<u>\$ 359,024</u>

## 6. INVESTMENT SECURITIES

Investment securities as of December 31, 2018 and 2017 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2018	2017	2018
Current:			
Negotiable certificate of deposits	¥ 2,000	¥ 2,000	\$ 18,018
Total	<u>¥ 2,000</u>	<u>¥ 2,000</u>	<u>\$ 18,018</u>
Non-current:			
Marketable equity securities	¥ 12,877	¥ 16,453	\$ 116,016
Total	<u>¥ 12,877</u>	<u>¥ 16,453</u>	<u>\$ 116,016</u>

The costs and aggregate fair values of investment securities at December 31, 2018 and 2017 were as follows:

	Millions of yen			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
<u>December 31, 2018</u>				
Securities classified as:				
Held to maturity	¥ 2,000	¥ —	¥ —	¥ 2,000
Available-for-sale	¥ 6,821	¥ 6,226	¥ (170)	¥ 12,877
	Millions of yen			
<u>December 31, 2017</u>	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities classified as:				
Held to maturity	¥ 2,000	¥ —	¥ —	¥ 2,000
Available-for-sale	¥ 6,821	¥ 9,668	¥ (37)	¥ 16,453
	Thousands of U.S. dollars			
<u>December 31, 2018</u>	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities classified as:				
Held to maturity	\$ 18,018	\$ —	\$ —	\$ 18,018
Available-for-sale	\$ 61,455	\$ 56,092	\$ (1,532)	\$ 116,016

The difference between the sum of the above fair values of the available-for-sale securities and cost of the held-to-maturity securities, and the amounts shown in the accompanying consolidated balance sheets consists of nonmarketable securities whose fair values are not readily determinable.

## 7. INVENTORIES

Inventories at December 31, 2018 and 2017 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2018	2017	2018
Merchandise and finished products	¥ 6,232	¥ 6,610	\$ 56,145
Work in process	5,516	4,343	49,697
Raw materials and supplies	<u>5,496</u>	<u>4,939</u>	<u>49,521</u>
Total	<u>¥ 17,245</u>	<u>¥ 15,893</u>	<u>\$ 155,364</u>

## 8. LONG-LIVED ASSETS

The Group reviewed its long-lived assets for impairment as of December 31, 2018 and 2017, and recognized impairment losses of ¥860 million (\$7,750 thousand) and ¥242 million, respectively for the following assets. The carrying amount of those assets was written down to the recoverable amount.

For the year ended December 31, 2018

Use	Type of assets	Location (Prefecture/Country)	Amount	
			Millions of yen	Thousands of U.S. dollars
Business assets for Equipment business	Machinery and equipment, Furniture and fixtures, Construction in progress and Intangible assets	Kanagawa and Kumamoto	¥ 415	\$ 3,744
Business assets for Equipment business	Building and structures, Machinery and equipment, Furniture and fixtures, and Construction in progress	Kumamoto	440	3,968
Idle assets	Land	Hyogo	4	37
Total			¥ 860	\$ 7,750



For the year ended December 31, 2017

Use	Type of assets	Location (Prefecture/Country)	Amount
			Millions of yen
Business assets for Equipment business	Machinery and equipment, Furniture and fixtures, Construction in progress and Intangible assets	Kanagawa, Kumamoto and Fukushima	¥ 131
Idle assets	Machinery and equipment and Furniture and fixtures	Kanagawa	75
Idle assets	Construction in progress	Fukushima	0
Idle assets	Machinery and equipment, Furniture and fixtures	U.S.A.	32
Manufacturing facilities	Machinery and equipment	U.S.A.	2
Total			¥ 242

For the purpose of evaluating and measuring impairment, assets used for business are considered to constitute a group by each business unit. Idle properties are individually evaluated.

The recoverable amount of land and buildings was measured by their net selling price estimated based on an appraisal value. The recoverable amount of the other assets was measured at their value in use based on reminder price.

## 9. LONG-TERM LOANS PAYABLE

Long-term loans payable at December 31, 2018 and 2017 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2018	2017	2018
Unsecured loan from a bank, with average interest rate of 0.49% for the years ended December 31, 2018	¥10,000	¥ —	\$90,090
Total	¥10,000	¥ —	\$90,090

The aggregate annual maturities of long-term loans payable during the next five years are summarized below:

Years ending December 31,	Millions of yen	Thousands of U.S. dollars
2019	¥ —	\$ —
2020	—	—
2021	—	—
2022	3,900	35,135
2023	—	—

## 10. RETIREMENT AND PENSION PLANS

The Company and its certain consolidated subsidiaries have funded defined benefit pension plans and lump-sum retirement payment plans.

The defined benefit corporate pension plans provide lump-sum payment or pension based on salary and service period.

The lump-sum retirement payment plans provide lump-sum payment as retirement benefit based on factors such as service period.

The details of the plans were as follows:

### 1. Defined benefit pension plans

#### (1) Retirement benefit obligations

	Millions of yen		Thousands of U.S. dollars
	2018	2017	2018
Beginning balance	¥ 16,154	¥ 16,116	\$ 145,536
Service cost	657	504	5,926
Interest cost	88	66	799
Actuarial differences incurred during the year	(225)	(129)	(2,033)
Payment of retirement benefit	(610)	(403)	(5,502)
Ending balance	<u>¥ 16,064</u>	<u>¥ 16,154</u>	<u>\$ 144,727</u>

Note: Certain consolidated subsidiaries apply a simplified method to calculate retirement benefit obligations.

#### (2) Pension assets

	Millions of yen		Thousands of U.S. dollars
	2018	2017	2018
Beginning balance	¥ 13,051	¥ 12,160	\$ 117,580
Expected return on plan assets	456	273	4,115
Actuarial differences incurred during the year	(1,047)	455	(9,437)
Contributions from employer	677	506	6,101
Payment of retirement benefit	(526)	(344)	(4,742)
Ending balance	<u>¥ 12,611</u>	<u>¥ 13,051</u>	<u>\$ 113,616</u>

#### (3) Employee retirement benefit trust

	Millions of yen		Thousands of U.S. dollars
	2018	2017	2018
Beginning balance	¥ 5,193	¥ 5,195	\$ 46,784
Expected return on plan assets	25	19	233
Actuarial differences incurred during the year	(5)	(22)	(53)
Ending balance	<u>¥ 5,213</u>	<u>¥ 5,193</u>	<u>\$ 46,964</u>

(4) Reconciliation between ending balance of retirement benefit obligations and pension assets and net defined benefit liability and net defined benefit asset recorded on the consolidated balance sheet

	Millions of yen		Thousands of
	2018	2017	U.S. dollars
Retirement benefit obligations under the funded plan	¥ 15,853	¥ 15,975	\$ 142,820
Pension assets	(12,611)	(13,051)	(113,616)
Employee retirement benefit trust	(5,213)	(5,193)	(46,964)
	(1,971)	(2,268)	(17,761)
Retirement benefit obligations under the unfunded plan	211	178	1,907
Net liabilities or assets recorded on the consolidated balance sheet	(1,759)	(2,089)	(15,853)
Net defined benefit liabilities	306	262	2,757
Net defined benefit assets	(2,065)	(2,352)	(18,611)
Net liabilities or assets recorded on the consolidated balance sheet	<u>¥ (1,759)</u>	<u>¥ (2,089)</u>	<u>\$ (15,853)</u>

(5) Net periodic benefit cost and its components

	Millions of yen		Thousands of
	2018	2017	U.S. dollars
Service cost	¥ 657	¥ 503	\$ 5,926
Interest cost	88	66	799
Expected return on plan assets	(482)	(293)	(4,349)
Amortized actuarial differences	257	312	2,318
Amortized prior service cost	(256)	(192)	(2,309)
Net periodic benefit cost of defined benefit plan	<u>¥ 264</u>	<u>¥ 396</u>	<u>\$ 2,386</u>

Note: Net periodic benefit cost of consolidated subsidiaries applying the simplified method is recorded as "Service cost."

(6) Remeasurements of defined benefit plans (Other comprehensive income)

	Millions of yen		Thousands of
	2018	2017	U.S. dollars
Prior service cost	¥ (256)	¥ (192)	\$ (2,309)
Actuarial differences	(570)	875	(5,139)
Total	<u>¥ (826)</u>	<u>¥ 682</u>	<u>\$ (7,449)</u>

(7) Remeasurements of defined benefit plans (Accumulated other comprehensive income)

	Millions of yen		Thousands of
	2018	2017	U.S. dollars
Unrecognized prior service cost	¥ 1,281	¥ 1,538	\$ 11,549
Unrecognized actuarial differences	(1,626)	(1,055)	(14,652)
Total	<u>¥ (344)</u>	<u>¥ 482</u>	<u>\$ (3,103)</u>

(8) Plan assets and employee retirement benefit trust

(a) Components of plan assets

	<u>2018</u>	<u>2017</u>
Debt securities	50%	45%
Equity securities	26%	33%
Other	24%	22%
Total	<u>100%</u>	<u>100%</u>

(b) Components of employee retirement benefit trust

	<u>2018</u>	<u>2017</u>
Debt securities	98%	98%
Other	2%	2%
Total	<u>100%</u>	<u>100%</u>

(c) Long-term rate of return

Long-term rate of return on plan assets and employee retirement benefit trust is determined based on the current and expected allocation of plan assets and employee retirement benefit trust and current and expected long-term rate of return of various assets composing plan assets and employee retirement benefit trust.

(9) Basis for calculation of actuarial differences

	<u>2018</u>	<u>2017</u>
Discount rate	Mainly 0.53%	Mainly 0.53%
Long-term expected rate of return		
Defined benefit corporate pension plan	3.50%	3.00%
Employee retirement benefit trust	0.50%	0.50%

2. Defined contribution plans

Contributions to defined contribution pension plans by the Company and its consolidated subsidiaries

	<u>Millions of yen</u>		<u>Thousands of U.S. dollars</u>
	<u>2018</u>	<u>2017</u>	<u>2018</u>
	¥ 172	¥ 133	\$ 1,551

## 11. ASSET RETIREMENT OBLIGATIONS

The changes in asset retirement obligations during the year ended December 31, 2018 and 2017 were as follows:

	<u>Millions of yen</u>		<u>Thousands of U.S. dollars</u>
	<u>2018</u>	<u>2017</u>	<u>2018</u>
Balance at beginning of year	¥ 88	¥ 88	\$ 800
Adjustments associated with passage of time	1	0	9
Others	<u>(2)</u>	<u>—</u>	<u>(17)</u>
Balance at end of year	<u>¥ 87</u>	<u>¥ 88</u>	<u>\$ 792</u>

## 12. EQUITY

Japanese companies are subject to the Companies Act of Japan (the “Companies Act”). The significant provisions in the Companies Act that affect financial and accounting matters are summarized below:

### *a. Dividends*

Under the Companies Act, companies can pay dividends at any time during the fiscal year in addition to the year-end dividend upon resolution at the shareholders meeting. For companies that meet certain criteria such as; (1) having the Board of Directors, (2) having independent auditors, (3) having the Board of Corporate Auditors, and (4) the term of service of the directors is prescribed as one year rather than two years of normal term by its articles of incorporation, the Board of Directors may declare dividends (except for dividends in kind) if the company has prescribed so in its articles of incorporation. The Company meets all the above criteria.

The Companies Act permits companies to distribute dividends-in-kind (non-cash assets) to shareholders subject to a certain limitation and additional requirements.

Semiannual interim dividends may also be paid once a year upon resolution by the Board of Directors if the articles of incorporation of the company so stipulate. The Companies Act provides certain limitations on the amounts available for dividends or the purchase of treasury stock. The limitation is defined as the amount available for distribution to the shareholders, but the amount of net assets after dividends must be maintained at no less than ¥3 million.

### *b. Increases/Decreases and Transfer of Common Stock, Reserve and Surplus*

The Companies Act requires that an amount equal to 10% of dividends must be appropriated as a legal reserve (a component of retained earnings) or as additional paid-in capital (a component of capital surplus) depending on the equity account charged upon the payment of such dividends until the total of aggregate amount of legal reserve and additional paid-in capital equals 25% of the common stock. Under the Companies Act, the total amount of additional paid-in capital and legal reserve may be reversed without limitation. The Companies Act also provides that common stock, legal reserve, additional paid-in capital, other capital surplus and retained earnings can be transferred among the accounts under certain conditions upon resolution of the shareholders.

### *c. Treasury Stock and Treasury Stock Acquisition Rights*

The Companies Act also provides for companies to purchase treasury stock and dispose of such treasury stock by resolution of the Board of Directors. The amount of treasury stock purchased cannot exceed the amount available for distribution to the shareholders which is determined by specific formula.

Under the Companies Act, stock acquisition rights are presented as a separate component of equity.

The Companies Act also provides that companies can purchase both treasury stock acquisition rights and treasury stock. Such treasury stock acquisition rights are presented as a separate component of equity or deducted directly from stock acquisition rights.

The accompanying consolidated financial statements do not include any provision for the semiannual dividend of ¥60 (\$0.54) per share approved at the general shareholders’ meeting held on March 29, 2019, aggregating ¥2,499 million (\$22,520 thousand) in respect of the year ended December 31, 2018.

### 13. STOCK OPTIONS

(1) Share-based compensation expenses which were accounted for as cost of sales and selling, general and administrative expenses

	Millions of yen		Thousands of U.S. dollars	
	2018	2017	2018	
Cost of sales	¥ 12	¥ 8	\$ 114	
Selling, general and administrative expenses	67	43	610	

(2) Outline, number and changes of stock options

(a) Outline of stock options

Stock options outstanding as of December 31, 2018 were as follows:

Stock option	2018 Stock option	2017 Stock option	2016 Stock option
Category and number of eligible person	1 representative director of the Company 5 directors of the Company 6 executive officers of the Company	1 representative director of the Company 5 directors of the Company 5 executive officers of the Company	1 representative director of the Company 5 directors of the Company 6 executive officers of the Company
Number of options granted	Common stock: 20,200 shares	Common stock: 14,500 shares	Common stock: 29,300 shares
Date of Grant	May 16, 2018	August 4, 2017	August 4, 2016
Service period	Not specified	Not specified	Not specified
Exercise period	From May 17, 2018 to May 16, 2048	From August 5, 2017 to August 4, 2047	From August 5, 2016 to August 4, 2046
Stock option	2015 Stock option	2014 Stock option	2013 Stock option
Category and number of eligible person	1 representative director of the Company 5 directors of the Company 8 executive officers of the Company	1 representative director of the Company 5 directors of the Company 7 executive officers of the Company	2 representative directors of the Company 4 directors of the Company 7 executive officers of the Company 200 employees of the Company
Number of options granted	Common stock: 21,900 shares	Common stock: 31,500 shares	Common stock: 484,000 shares
Date of Grant	August 4, 2015	August 5, 2014	January 10, 2013
Service period	Not specified	Not specified	From January 10, 2013 to May 31, 2016
Exercise period	From August 5, 2015 to August 4, 2045	From August 6, 2014 to August 5, 2044	From June 1, 2016 to May 31, 2019

(b) Number and price of stock options

Movement in stock options during the fiscal year ended December 31, 2018 was as follows:

	Number of shares		
	2018	2017	2016
Unvested stock options:			
As of December 31, 2017	—	—	—
Granted	20,200	—	—
Forfeited	—	—	—
Vested	20,200	—	—
Unvested options as of December 31, 2018	—	—	—
Vested stock options:			
As of December 31, 2017	—	14,500	27,200
Vested	20,200	—	—
Exercised	—	—	—
Forfeited	—	—	—
Unexercised options as of December 31, 2018	20,200	14,500	27,200
	Yen		
Exercise price	¥ 1	¥ 1	¥ 1
Average share price at the time of exercise	¥ —	¥ —	¥ —
Fair value per share at grant date	¥ 4,164	¥ 3,363	¥ 2,757
	U.S. dollars		
Exercise price	\$ 0.01	\$ 0.01	\$ 0.01
Average share price at the time of exercise	\$ —	\$ —	\$ —
Fair value per share at grant date	\$ 37.51	\$ 30.29	\$ 24.83

	Number of shares		
	2015	2014	2013
Unvested stock options:			
As of December 31, 2017	—	—	—
Granted	—	—	—
Forfeited	—	—	—
Vested	—	—	—
Unvested options as of December 31, 2018	—	—	—
Vested stock options:			
As of December 31, 2017	18,200	23,800	66,000
Vested	—	—	—
Exercised	1,100	1,600	25,000
Forfeited	—	—	—
Unexercised options as of December 31, 2018	17,100	22,200	41,000
	Yen		
Exercise price	¥ 1	¥ 1	¥ 1,759
Average share price at the time of exercise	¥ 3,994	¥ 3,994	¥ 3,994
Fair value per share at grant date	¥ 3,192	¥ 2,292	¥ 417
	U.S. dollars		
Exercise price	\$ 0.01	\$ 0.01	\$ 15.57
Average share price at the time of exercise	\$ 35.98	\$ 35.98	\$ 35.98
Fair value per share at grant date	\$ 28.75	\$ 20.64	\$ 3.75

(3) Method of estimating the fair value of stock options vested

The fair value price is estimated using the Black-Scholes option pricing model with the following assumptions:

	2018
Volatility of stock price	31.961 %
Estimated remaining outstanding period	5.9 years
Estimated dividend per share	¥ 64 (\$ 0.57)
Risk-free interest rate	(0.065) %

(4) Method of estimating number of stock options vested

Only the actual number of forfeited stock options is reflected because it is difficult to reasonably estimate the number of future forfeitures.



## 14. INCOME TAXES

The Company and its domestic subsidiaries are subject to Japanese national and local income taxes which, in the aggregate, resulted in a normal effective statutory tax rate of approximately 30.6% and 30.6% for the year ended December 31, 2018 and 2017, respectively. Foreign subsidiaries are subject to income taxes of the countries in which they operate.

The tax effects of significant temporary differences and tax loss carryforwards, which resulted in deferred tax assets and liabilities at December 31, 2018 and 2017 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2018	2017	2018
Current:			
Deferred tax assets:			
Accrued bonuses for employees	¥ 513	¥ 523	\$ 4,628
Unrealized gains on finished goods	652	644	5,881
Loss on valuation of inventories	271	235	2,441
Other	308	217	2,776
Less valuation allowance	(1)	(5)	(14)
Total	<u>1,744</u>	<u>1,616</u>	<u>15,712</u>
Deferred tax liabilities:			
Other	(255)	(370)	(2,301)
Total	<u>(255)</u>	<u>(370)</u>	<u>(2,301)</u>
Net deferred tax assets (liabilities)	<u>¥ 1,489</u>	<u>¥ 1,246</u>	<u>\$ 13,411</u>
Non-current:			
Deferred tax assets:			
Net defined benefit liability and asset	1,024	923	9,233
Tax loss carryforwards	179	132	1,615
Loss on devaluation of investment securities	343	343	3,098
Allowance for doubtful accounts	31	60	279
Loss on impairment of long-lived assets	851	694	7,667
Other	704	638	6,343
Less valuation allowance	(890)	(771)	(8,025)
Total	<u>2,243</u>	<u>2,021</u>	<u>20,210</u>
Deferred tax liabilities:			
Reserve for advanced depreciation	(220)	(233)	(1,983)
Unrealized gain on available-for-sale securities	(1,750)	(2,738)	(15,770)
Undistributed earnings of foreign subsidiaries	(1,102)	(1,222)	(9,929)
Accelerated depreciation	(346)	(172)	(3,120)
Other	(11)	(41)	(99)
Total	<u>(3,430)</u>	<u>(4,408)</u>	<u>(30,902)</u>
Net deferred tax assets (liabilities)	<u>¥ (1,187)</u>	<u>¥ (2,387)</u>	<u>\$ (10,691)</u>

Note: Net deferred tax assets (liabilities) are included in the following accounts:

	Millions of yen		Thousands of U.S. dollars
	2018	2017	2018
Current assets: Deferred tax assets	¥ 1,687	¥ 1,574	\$ 15,204
Non-current assets: Deferred tax assets	438	145	3,954
Current liabilities: Deferred tax liabilities	(198)	(329)	(1,791)
Non-current liabilities: Deferred tax liabilities	¥ (1,625)	¥ (2,533)	\$ (14,646)

Reconciliation between the normal effective statutory tax rates and the actual effective tax rates reflected in the accompanying consolidated statements of income for the year ended December 31, 2018 and 2017 were as follows:

	<u>2018</u>	<u>2017</u>
Normal effective statutory tax rate	30.6%	30.6%
Adjustments:		
Non-taxable dividend income	(5.5)	(3.5)
Different income tax rates applicable to income in certain foreign countries	(8.3)	2.5
Dividends from consolidated foreign subsidiaries eliminated for consolidation purposes	5.5	3.5
Tax credit for research and development costs	(4.2)	(6.1)
Other—net	<u>1.8</u>	<u>(3.3)</u>
Actual effective tax rate	<u>19.9%</u>	<u>23.7%</u>

#### 15. RESEARCH AND DEVELOPMENT COSTS

Research and development costs charged to income were as follows:

	<u>Millions of yen</u>		<u>Thousands of U.S. dollars</u>
	<u>2018</u>	<u>2017</u>	<u>2018</u>
Selling, general and administrative expenses	¥ 8,334	¥ 6,808	\$ 75,083
Cost of sales	<u>192</u>	<u>112</u>	<u>1,730</u>
Total	<u>¥ 8,526</u>	<u>¥ 6,921</u>	<u>\$ 76,814</u>

#### 16. LEASES

The Group leases certain buildings and structures, machinery, computer hardware, software and other assets. The minimum rental commitments under non-cancelable operating leases at December 31, 2018 and 2017 were as follows:

	<u>Millions of yen</u>		<u>Thousands of U.S. dollars</u>
	<u>2018</u>	<u>2017</u>	<u>2018</u>
Due within one year	¥ 83	¥ 96	\$ 755
Due after one year	<u>528</u>	<u>578</u>	<u>4,761</u>
Total	<u>¥ 612</u>	<u>¥ 674</u>	<u>\$ 5,516</u>

## 17. FINANCIAL INSTRUMENTS

### (1) *Group Policy for Financial Instruments*

The Group raises the funds necessary for its business operation and capital expenditure by taking into consideration the capital structure suitable for the economic environment and the actual state of the entity. Derivatives are used to avoid risks described below, and not for speculative purposes.

### (2) *Nature and Extent of Risks Arising from Financial Instruments*

Trade receivables such as trade notes and accounts are exposed to customer credit risk. Also, trade receivables denominated in foreign currencies arising from exporting products are exposed to the risk of exchange rate fluctuations.

Securities are negotiable certificate of deposit which is expected to be settled with short term and investment securities, mainly equity instruments of customers and suppliers of the Group are exposed to the risk of market price fluctuations.

Payment terms of payables, such as trade notes and accounts, are less than one year. A part of those trade payables is denominated in foreign currencies and exposed to the risk of exchange rate fluctuations.

Long-term loans payable has fixed interest rates to hedge the risk of interest rate fluctuations.

Derivatives mainly include foreign currency forward contracts and currency option contracts, which are used to manage exposure to market risks from changes in foreign exchange rates of receivables and payables. Please see Note 18 for more detail about derivatives.

### (3) *Risk Management for Financial Instruments*

#### *Credit risk management*

The Group manages its credit risk from receivables in accordance with internal guidelines, which include monitoring of payment terms and balances of major customers by the credit administration department to identify the default risk of customers in the early stages. With respect to held-to-maturity securities, the Group manages its exposure to credit risk by limiting its holdings to high credit rating bonds. With respect to derivatives, the Group manages its exposure to credit risk by limiting its counterparties to major and creditworthy international financial institutions.

The maximum credit risk exposure of financial assets is limited to their carrying amounts as of December 31, 2018.

#### *Market risk management (foreign exchange and interest rate risk)*

Foreign currency trade receivables and payables are exposed to market risk resulting from fluctuations in foreign currency exchange rates. Such foreign exchange risk, which is managed monthly by currency, is hedged mainly by foreign currency forward contracts and currency option contracts. In addition, foreign currency forward contracts may be used at the maximum of expected amounts of foreign currency trade receivables and payables.

In addition, long-term loans payable has fixed interest rates to hedge the risk of interest rate fluctuations. Derivative transactions are executed and managed in accordance with "Financial Risk Management Rules."

Investment securities are managed by monitoring market values and financial position of issuers on a regular basis.

### (4) *Fair Values of Financial Instruments*

Fair values of financial instruments are based on quoted price in active markets. When quoted price is not available, other values calculated using reasonable valuation techniques are used. Please see Note 18 for the detail of fair value for derivatives.

#### (a) *Fair value of financial instruments*

<u>December 31, 2018</u>	<u>Millions of yen</u>		
	<u>Carrying</u>	<u>Fair value</u>	<u>Unrealized</u>

	<u>amount</u>		<u>gain/loss</u>
Cash and deposits	¥ 37,851	¥ 37,851	¥ —
Time deposits	18,241	18,241	—
Receivables—Trade notes and accounts	22,539	22,539	—
Securities and Investment securities:			
Held to maturity	2,000	2,000	—
Available-for-sale securities	12,877	12,877	—
Long-term time deposits	<u>18,000</u>	<u>17,999</u>	<u>(0)</u>
 Total	 <u>¥ 111,511</u>	 <u>¥ 111,510</u>	 <u>¥ (0)</u>
 Payables—Trade notes and accounts	 ¥ 11,381	 ¥ 11,381	 ¥ —
Long-term loans payable	<u>10,000</u>	<u>10,088</u>	<u>88</u>
 Total	 <u>¥ 21,381</u>	 <u>¥ 21,469</u>	 <u>¥ 88</u>
Derivative transactions	<u>¥ (439)</u>	<u>¥ (439)</u>	<u>¥ —</u>

<u>December 31, 2017</u>	Millions of yen		
	<u>Carrying amount</u>	<u>Fair value</u>	<u>Unrealized gain/loss</u>
Cash and deposits	¥ 27,961	¥ 27,961	¥ —
Time deposits	16,219	16,219	—
Receivables—Trade notes and accounts	22,554	22,554	—
Securities and Investment securities:			
Held to maturity	2,000	2,000	—
Available-for-sale securities	16,453	16,453	—
Long-term time deposits	<u>18,000</u>	<u>17,999</u>	<u>(0)</u>
Total	<u>¥ 103,189</u>	<u>¥ 103,189</u>	<u>¥ (0)</u>
Payables—Trade notes and accounts	<u>¥ 10,444</u>	<u>¥ 10,444</u>	<u>¥ —</u>
Total	<u>¥ 10,444</u>	<u>¥ 10,444</u>	<u>¥ —</u>
Derivative transactions	<u>¥ (979)</u>	<u>¥ (979)</u>	<u>¥ —</u>

<u>December 31, 2018</u>	Thousands of U.S. dollars		
	<u>Carrying amount</u>	<u>Fair value</u>	<u>Unrealized gain/loss</u>
Cash and deposits	\$ 341,006	\$ 341,006	\$ —
Time deposits	164,341	164,341	—
Receivables—Trade notes and accounts	203,060	203,060	—
Securities and Investment securities:			
Held to maturity	18,018	18,018	—
Available-for-sale securities	116,016	116,016	—
Long-term time deposits	<u>162,162</u>	<u>162,158</u>	<u>(3)</u>
Total	<u>\$ 1,004,604</u>	<u>\$ 1,004,600</u>	<u>\$ (3)</u>
Payables—Trade notes and accounts	\$ 102,538	\$ 102,538	\$ —
Long-term loans payable	<u>90,090</u>	<u>90,883</u>	<u>793</u>
Total	<u>\$ 192,628</u>	<u>\$ 193,422</u>	<u>\$ 793</u>
Derivative transactions	<u>\$ (3,961)</u>	<u>\$ (3,961)</u>	<u>\$ —</u>

#### Cash and deposits, and Time Deposits

The carrying values of cash and deposits, and time deposits approximate fair value because of their short maturities.

#### Receivables—Trade Notes and Accounts

The carrying values of receivables—trade notes and accounts approximate fair value because of their short maturities.

#### Securities and Investment Securities

The carrying value of securities, approximate fair value because of their short maturities. the fair values of investment securities are measured at the quoted market price of the stock exchange for the equity instruments, and at the quoted price obtained from the financial institution for certain debt instruments. The information of the fair value for the marketable and investment securities by classification is included in Note 6.

#### Long-Term Time Deposits

Long-term time deposits are measured at fair value using the discounted cash flow on deposits held at banks. The discounted rate used is the deposit interest rate assuming the same period.

#### Payables—Trade Notes and Accounts

The carrying values of payables—trade notes and accounts approximate fair value because of their short maturities.

#### Long-Term Loans Payable

The carrying values of short-term loans payable approximate fair value because of their short maturities. The fair value of long-term loans payable is calculated by discounting the sum of its principal and interest at an interest rate at which a similar new loans payable is assumed to be made.

#### Derivatives

The information of the fair value for derivatives is included in Note 18.

(b) *Financial instruments whose fair value cannot be reliably determined*

	Carrying amount		
	Millions of yen		Thousands of U.S. dollars
	2018	2017	2018
Investments in equity instruments that do not have a quoted market price in an active market	¥40	¥1,198	\$363
Investments in capital that do not have a quoted market price in an active market	220	—	1,981

(5) *Maturity Analysis for Financial Assets and Securities with Contractual Maturities*

	Millions of yen		
	Due in 1 year or less	Due after 1 year through 5 years	Due after 5 years through 10 years
<u>December 31, 2018</u>			
Cash and deposits	¥ 37,851	¥ —	¥ —
Time deposits	18,241	—	—
Receivables—Trade notes and accounts	22,539	—	—
Securities and Investment securities:			
Held to maturity			
Negotiable certificate of deposit	2,000	—	—
Long-term time deposits	—	18,000	—
Total	<u>¥ 80,633</u>	<u>¥ 18,000</u>	<u>¥ —</u>

	Millions of yen		
	Due in 1 year or less	Due after 1 year through 5 years	Due after 5 years through 10 years
<u>December 31, 2017</u>			
Cash and deposits	¥ 27,961	¥ —	¥ —
Time deposits	16,219	—	—
Receivables—Trade notes and accounts	22,554	—	—
Securities and Investment securities:			
Held to maturity			
Negotiable certificate of deposit	2,000	—	—
Long-term time deposits	—	18,000	—
Total	<u>¥ 68,736</u>	<u>¥ 18,000</u>	<u>¥ —</u>

	Thousands of U.S. dollars		
	Due in 1 year or less	Due after 1 year through 5 years	Due after 5 years through 10 years
<u>December 31, 2018</u>			
Cash and deposits	\$ 341,006	\$ —	\$ —
Time deposits	164,341	—	—
Receivables—Trade notes and accounts	203,060	—	—
Securities and Investment securities:			
Held to maturity			
Negotiable certificate of deposit	18,018	—	—
Long-term time deposits	—	162,162	—
Total	<u>\$ 726,425</u>	<u>\$ 162,162</u>	<u>\$ —</u>

## 18. DERIVATIVES

The Group enters into foreign currency forward contracts to hedge foreign exchange risk associated with certain assets and liabilities denominated in foreign currencies.

All derivative transactions are entered into to hedge foreign currency exposures incorporated within its business. Accordingly, market risk in these derivatives is basically offset by opposite movements in the value of hedged assets or liabilities.

Because the counterparties to these derivatives are limited to major international financial institutions, the Group does not anticipate any losses arising from credit risk.

Derivative transactions entered into by the Group have been made in accordance with internal policies which regulate the authorization and credit limit amounts.

### *Derivative Transactions to Which Hedge Accounting is not Applied*

	Millions of yen							
	2018				2017			
	Contract amount	Contract amount due after one year	Fair value	Unrealized gain (loss)	Contract amount	Contract amount due after one year	Fair value	Unrealized gain (loss)
Foreign currency forward contracts:								
Sell:								
KRW	¥ 7,216	¥ 2,714	¥ (439)	¥ (439)	¥ 7,710	¥ 3,000	¥ (979)	¥ (979)
Currency option contracts:								
Written call option:								
US\$	—	—	—	—	33	—	0	0
Purchased put option:								
US\$	—	—	—	—	33	—	0	0
Total	<u>¥ 7,216</u>	<u>¥ 2,714</u>	<u>¥ (439)</u>	<u>¥ (439)</u>	<u>¥ 7,778</u>	<u>¥ 3,000</u>	<u>¥ (979)</u>	<u>¥ (979)</u>

	Thousands of U.S. dollars			
	2018			
	Contract amount	Contract amount due after one year	Fair value	Unrealized gain (loss)
Foreign currency forward contracts:				
Sell:				
KRW	\$ 65,012	\$24,452	\$ (3,961)	\$ (3,961)
Currency option contracts:				
Written call option:				
US\$	—	—	—	—
Purchased put option:				
US\$	—	—	—	—
Total	<u>\$ 65,012</u>	<u>\$24,452</u>	<u>\$ (3,961)</u>	<u>\$ (3,961)</u>

\* The fair value is based on prices provided by financial institutions.



*Derivative Transactions to Which Hedge Accounting is Applied*

<u>December 31, 2018</u>	<u>Hedged Item</u>	<u>Millions of yen</u>		
		<u>Contract amount</u>	<u>Contract amount due after one year</u>	<u>Fair value</u>
Foreign currency forward contracts:				
Selling U.S.\$	Receivables—Trade accounts	¥ 2,238	¥ —	*
Selling EUR	Receivables—Trade accounts	189	—	*
Selling NT\$	Receivables—Trade accounts	938	—	*

<u>December 31, 2017</u>	<u>Hedged Item</u>	<u>Millions of yen</u>		
		<u>Contract amount</u>	<u>Contract amount due after one year</u>	<u>Fair value</u>
Foreign currency forward contracts:				
Selling U.S.\$	Receivables—Trade accounts	¥ 3,778	¥ —	*
Selling EUR	Receivables—Trade accounts	258	—	*
Selling NT\$	Receivables—Trade accounts	1,189	—	*

<u>December 31, 2018</u>	<u>Hedged Item</u>	<u>Thousands of U.S. dollars</u>		
		<u>Contract amount</u>	<u>Contract amount due after one year</u>	<u>Fair value</u>
Foreign currency forward contracts:				
Selling U.S.\$	Receivables—Trade accounts	\$ 20,169	\$ —	*
Selling EUR	Receivables—Trade accounts	1,710	—	*
Selling NT\$	Receivables—Trade accounts	8,457	—	*

\* The fair value of such foreign currency forward contracts is included in that of the hedged items (i.e., receivables—trade accounts).

## 19. COMPREHENSIVE INCOME

Reclassification adjustments and tax effects regarding other comprehensive income for the year ended December 31, 2018 and 2017 were as follows:

	Millions of yen		Thousands of
	2018	2017	U.S. dollars
			2018
Unrealized gain on available-for-sale securities:			
Recognized during the year	¥ (3,566)	¥ 3,097	\$ (32,127)
Reclassification adjustments	—	(0)	—
Before tax effects adjustment	(3,566)	3,097	(32,127)
Tax effects	987	(898)	8,897
Unrealized gain on available-for-sale securities	(2,578)	2,199	(23,229)
Foreign currency translation adjustments:			
Recognized during the year	(1,751)	1,457	(15,781)
Reclassification adjustments	—	—	—
Foreign currency translation adjustments	(1,751)	1,457	(15,781)
Remeasurements of defined benefit plans:			
Recognized during the year	(826)	562	(7,449)
Reclassification adjustments	—	119	—
Before tax effects adjustment	(826)	682	(7,449)
Tax effects	251	(207)	2,264
Remeasurements of defined benefit plans	(575)	475	(5,184)
Share of other comprehensive income in companies accounted for by the equity method:			
Recognized during the year	(113)	(19)	(1,018)
Total other comprehensive income	¥ (5,018)	¥ 4,112	\$ (45,214)

## 20. NET INCOME PER SHARE

Basic net income per share (“EPS”) for the years ended December 31, 2018 and 2017 was as follows:

	Yen		U.S. dollars
	2018	2017	2018
Basic EPS	¥ 164.92	¥ 138.31	\$ 1.48
Diluted EPS	164.44	137.91	1.48

Basis for the calculation of basic and diluted net income per share is as follows:

	Millions of yen		Thousands of U.S. dollars
	2018	2017	2018
Profit attributable to owners of the parent	¥ 6,875	¥ 6,007	\$ 61,945

	Thousands of shares	
	2018	2017
Earnings per share:		
Weighted-average number of shares*	41,692	43,432

Diluted earnings per share:

Increase in number of common stock	120	125
(Of those, new share subscription rights)	(120)	(125)

\* Weighted-average shares for the year ended December 31, 2018 and 2017 excluded the Company’s shares held by the Employee Stock Ownership Plan Trust. In addition, the Employee Stock Ownership Plan Trust expired on March 20, 2017.

## 21. SEGMENT INFORMATION

**For the Years Ended December 31, 2018 and 2017**

(1) Description of reportable segments

The Group’s reportable segments are those for which separate financial information is available and regular evaluation by the Company’s management is being performed in order to decide resources allocation within the Group and to evaluate performance. Therefore, the Group consists of the Material Business and Equipment Business. The Material Business consists of photoresists and related materials and specialty chemicals. The Equipment Business consists of semiconductor manufacturing equipment and LCD manufacturing equipment.

(2) Methods of measurement for the amounts of sales, profit (loss), assets and other items for each reportable segment

The accounting policies of each reportable segment are consistent with those disclosed in Note 2, “Summary of Significant Accounting Policies.”

(3) Information about sales, profit (loss), assets and other items was as follows:

	Millions of yen				
	2018				
	Reportable segment			Reconciliations	Consolidated
Material business	Equipment business	Total			
Sales:					
Sales to customers	¥102,621	¥ 2,655	¥105,277	¥ —	¥ 105,277
Intersegment sales or transfers	<u>5</u>	<u>41</u>	<u>46</u>	<u>(46)</u>	<u>—</u>
Total sales	<u>¥102,626</u>	<u>¥ 2,697</u>	<u>¥105,324</u>	<u>¥ (46)</u>	<u>¥ 105,277</u>
Segment income (loss)	¥ 15,075	¥ (883)	¥ 14,191	¥ (3,686)	¥ 10,505
Segment assets	104,903	4,245	109,148	75,534	184,683
Other:					
Depreciation	6,769	63	6,832	231	7,063
Increase in property, plant and equipment and intangible assets	5,001	482	5,483	393	5,877

Note: Reconciliations to

- Segment income (loss) amounting to ¥(3,686) million (\$33,209 thousand) includes common costs of ¥(3,686) million (\$33,209 thousand), which are not allocated to reportable segments.
- Segment assets amounting to ¥75,534 million (\$680,488 thousand) include working capital (the Company's cash, deposits, and long-term time deposits) and investment securities of ¥68,018 million (\$612,782 thousand), which are not allocated to reportable segments.
- Increase in property, plant and equipment and intangible assets of ¥393 million (\$3,548 thousand) is related to common assets.

	Millions of yen				
	2017				
	Reportable segment			Reconciliations	Consolidated
Material business	Equipment business	Total			
Sales:					
Sales to customers	¥ 90,531	¥ 1,880	¥ 92,411	¥ —	¥ 92,411
Intersegment sales or transfers	<u>1</u>	<u>41</u>	<u>43</u>	<u>(43)</u>	<u>—</u>
Total sales	<u>¥ 90,532</u>	<u>¥ 1,921</u>	<u>¥ 92,454</u>	<u>¥ (43)</u>	<u>¥ 92,411</u>
Segment income (loss)	¥ 12,816	¥ (664)	¥ 12,151	¥ (2,957)	¥ 9,194
Segment assets	106,220	3,026	109,247	69,433	178,681
Other:					
Depreciation	5,833	24	5,858	177	6,035
Increase in property, plant and equipment and intangible assets	6,579	138	6,718	135	6,853

Note: Reconciliations to

—Segment income (loss) amounting to ¥(2,957) million includes common costs of ¥(2,957) million, which are not allocated to reportable segments.

—Segment assets amounting to ¥69,433 million include working capital (the Company's cash, deposits, and long-term time deposits) and investment securities of ¥62,415 million, which are not allocated to reportable segments.

— Increase in property, plant and equipment and intangible assets of ¥135 million is related to common assets.

	Thousands of U.S. dollars				
	2018				
	Reportable segment			Reconciliations	Consolidated
Material business	Equipment business	Total			
Sales:					
Sales to customers	\$ 924,520	\$ 23,923	\$ 948,443	\$ —	\$ 948,443
Intersegment sales or transfers	<u>46</u>	<u>374</u>	<u>421</u>	<u>(421)</u>	<u>—</u>
Total sales	<u>\$ 924,566</u>	<u>\$ 24,298</u>	<u>\$ 948,864</u>	<u>\$ (421)</u>	<u>\$ 948,443</u>
Segment income (loss)	\$ 135,816	\$ (7,961)	\$ 127,854	\$ (33,209)	\$ 94,645
Segment assets	945,074	38,248	983,323	680,488	1,663,812
Other:					
Depreciation	60,982	569	61,552	2,085	63,638
Increase in property, plant and equipment and intangible assets	45,054	4,344	49,399	3,548	52,947

## Related Information

### For the Fiscal Period Ended December 31, 2018 and the Fiscal Year Ended 2017

#### (1) Information about geographical areas

##### (a) Sales

	Millions of yen		Thousands of U.S. dollars
	2018	2017	2018
Japan	¥ 24,750	¥ 19,319	\$ 222,979
Taiwan	41,399	40,469	372,967
Korea	12,286	11,229	110,692
U.S.A.	10,978	9,591	98,901
Other areas	15,862	11,801	142,902
Total	<u>¥ 105,277</u>	<u>¥ 92,411</u>	<u>\$ 948,443</u>

Note: Sales are classified in countries or regions based on location of customers.

##### (b) Property, Plant and Equipment

	Millions of yen		Thousands of U.S. dollars
	2018	2017	2018
Japan	¥ 28,780	¥ 29,006	\$ 259,287
Taiwan	7,384	7,933	66,524
Korea	8,363	11,525	75,344
U.S.A.	3,470	2,949	31,261
Other areas	360	288	3,245
Total	<u>¥ 48,358</u>	<u>¥ 51,703</u>	<u>\$ 435,665</u>

#### (2) Information about major customers

Name of customers	Relevant segment	Sales amount		Thousands of
		Millions of yen		U.S. dollars
		2018	2017	2018
Taiwan Semiconductor Manufacturing Company, Ltd.	Material Business	¥ 24,603	¥ 23,263	\$ 221,651

## CAUTIONARY STATEMENT

The Company's financial statements in English have not been audited by independent auditors. However, the original Japanese financial statements on which they are based have been audited by independent auditors.