Japan Tobacco Inc.

Annual Report 2018

Year ended December 31, 2018

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Adjusted Operating Profit

595.5
(JPY BN)

+1.7%
Year-on-Year Change

Adjusted Operating Profit at Constant FX

+8.9%
Year-on-Year Change

637.2
(JPY BN)

Annual Dividend per Share

150
(JPY)

+7.1%
Year-on-Year Change

Fact Sheets are available at:
https://www.jt.com/investors/results/annual_report/

Environment

21.2%
Reduction in total greenhouse gas emissions between 2009 and 2017*

* The original target: reducing absolute greenhouse gas emissions by 20% between 2009 and 2020

Our Supply Chain - Agricultural Labor Practices

96%
Of our directly contracted leaf growers were observed by farming experts against our ALP standards in 2018

96%
Of our leaf merchants reported against our ALP standards in 2018

Unless the context indicates otherwise, references in this Annual Report to 'we', 'us', 'our', 'Japan Tobacco', 'JT Group' or 'JT' are to Japan Tobacco Inc. and its consolidated subsidiaries. References to 'JTI' are to JTI Holding B.V., our consolidated subsidiary, and its consolidated subsidiaries. References to 'TableMark' are to TableMark Co., Ltd. and its Group companies. References to 'Japan Tobacco Inc.' are only to Japan Tobacco Inc. and references to 'JT International Holding B.V.' are only to JTI Holding B.V. References to 'Audit & Supervisory Board' are to 'kansayaku-kai' (as defined in the Companies Act of Japan) that performs certain supervisory functions through its monitoring and audit activities within the overall scheme of corporate governance pursuant to the Companies Act of Japan. References to 'Audit & Supervisory Board Member' are to a member or members of an Audit & Supervisory Board, also referred to in Japanese as 'kansayaku' (as defined in the Companies Act of Japan).

Forward-looking statements
This presentation contains forward-looking statements. These statements appear in a number of places in this document and include statements regarding the intent, belief, or current and future expectations of our management with respect to our business, financial condition and results of operations. In some cases, you can identify forward-looking statements by terms such as "may", "will", "should", "would", "expect", "intend", "project", "plan", "aim", "seek", "target", "anticipate", "believe", "estimate", "predict", "potential" or the negative of these terms or other similar terminology. These statements are not guarantees of future performance and are subject to various risks and uncertainties. Actual results, performance or achievements, or those of the industries in which we operate, may differ materially from any future results, performance or achievements expressed or implied by these forward-looking statements. In addition, these forward-looking statements are necessarily dependent upon assumptions, estimates and data that may be incorrect or imprecise and involve known and unknown risks and uncertainties. Forward-looking statements regarding operating results are particularly subject to a variety of assumptions, some or all of which may not be realized.

Risks, uncertainties or other factors that could cause actual results to differ materially from those expressed in any forward-looking statement include, without limitation:

1. increase in awareness of health concerns related to smoking;
2. regulatory developments; including, without limitation, tax increases and restrictions on sales, marketing, packaging, labeling and use of tobacco products, privately imposed restrictions and governmental investigations;
3. litigation around the world alleging adverse health and financial effects resulting from, or relating to, tobacco products;
4. our ability to further diversify our business beyond the traditional tobacco industry;
5. our ability to successfully expand internationally and make investments outside Japan;
6. competition and changing consumer preferences;
7. our ability to manage impacts derived from business diversification or business expansion;
8. economic, regulatory and political changes, such as nationalization, terrorism, wars and civil unrest, in countries in which we operate;
9. fluctuations in foreign exchange rates and the costs of raw materials; and
10. catastrophes, including natural disasters.

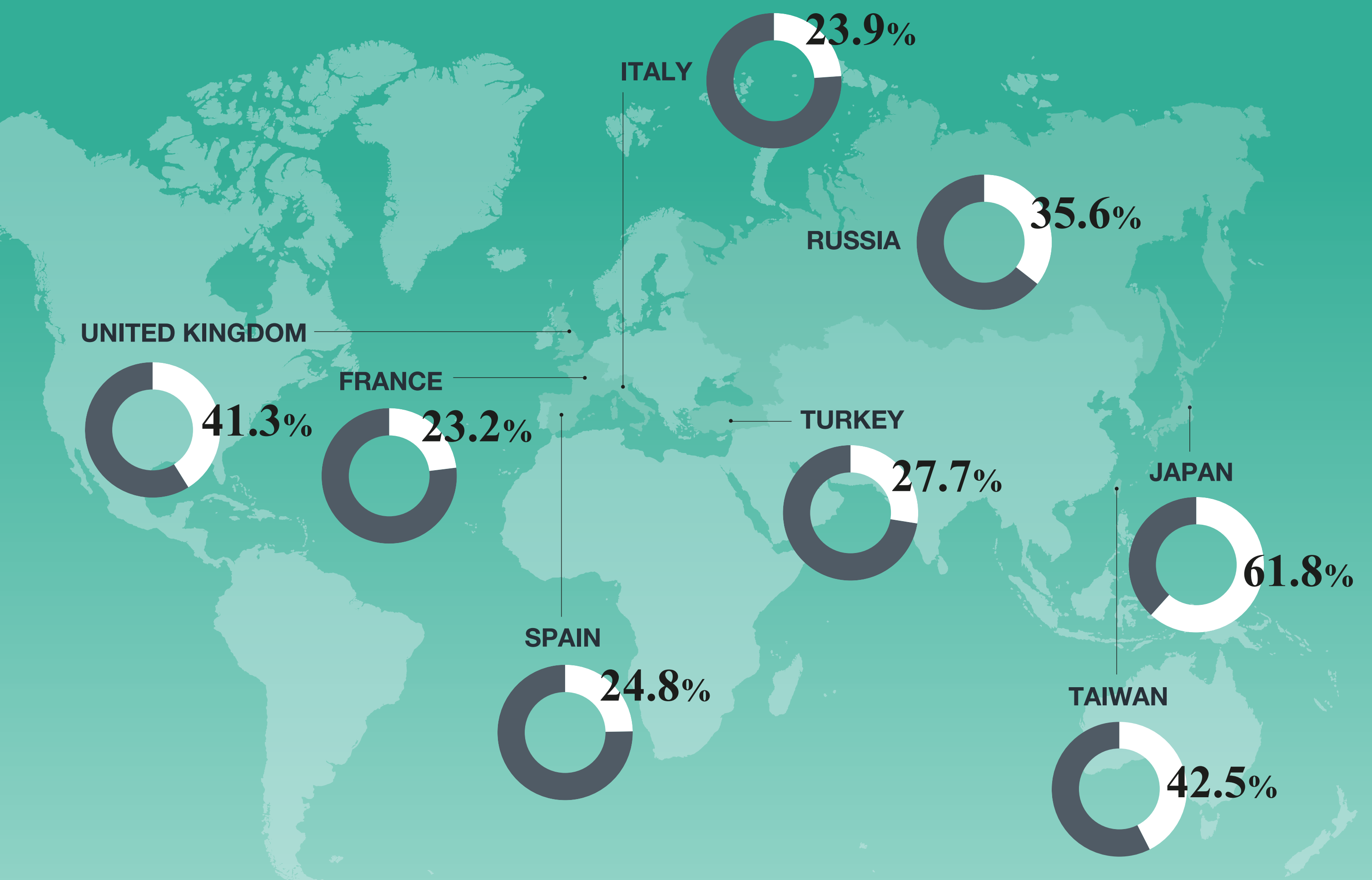
Our Businesses

Results for the fiscal year ended December 31, 2018

The JT Group is a leading global tobacco company operating in over 70 countries/regions. Our products are sold in over 130 countries/regions and our internationally recognized brands include Winston, Camel, MEVIUS and LD. Our pharmaceutical and processed food businesses complement the Group's profit growth and we are developing these businesses for sustainable growth.

Market Share

JT's position in key markets



(Source: IRI, Nielsen, Logista, TIOJ)

International Tobacco Business

The international tobacco business remains the JT Group's growth engine, accounting for over 60% of the Group's consolidated adjusted operating profit. Looking ahead, we expect the international tobacco business to continue achieving sustainable top- and bottom-line growth in the mid- to long-term period, further strengthening its competitiveness in both combustibles and Reduced-Risk Products (RRP)*.

Our international brand portfolio is very competitive and well-balanced, with strong equity brands across all relevant product categories and price segments. The portfolio includes leading brands in cigarettes and fine cut, such as Winston, Camel, MEVIUS and LD, as well as in Reduced-Risk Products, such as Ploom and Logic.

Results for 2018:

Core Revenue	Adjusted Operating Profit
11,330 (USD MM)	3,493 (USD MM)
+7.9% Year-on-Year Change	+11.3% Year-on-Year Change

- Robust volume increase driven by acquisitions and GFB expansion
- Significant core revenue growth, bolstered by improved pricing in Russia and the UK
- Strong top-line momentum drove double-digit adjusted operating profit growth

Global Flagship Brands

RRP Brands

Japanese Domestic Tobacco Business

Our Japanese domestic tobacco business generates about one third of our consolidated adjusted operating profit.

In the RMC** category, we have captured over 60% market share. We continue to enhance brand equity and strengthen our leading position. In addition, we also focus on the RRP category, which has become widely popular.

* Reduced-Risk Products (RRP): Products with the potential to reduce the risks associated with smoking.
** RMC: Ready-made cigarettes

Results for 2018:

Core Revenue	Adjusted Operating Profit
582.4 (JPY BN)	209.0 (JPY BN)
-1.4% Year-on-Year Change	-10.0% Year-on-Year Change

- National rollout of Ploom TECH
- Enhanced No. 1 position in RMC category with 61.8% market share
- Decreased revenue and profit due to a decline in RMC sales volume

Key Brands

Pharmaceutical Business

Our pharmaceutical business focuses on the research and development, manufacturing and sale of prescription pharmaceuticals. Its mission is to build an R&D-led business, aiming at first-in-class internationally competent compounds, to increase our market presence.

We concentrate on specific therapeutic areas: metabolic diseases, autoimmune/inflammatory diseases and viral infection; while Torii Pharmaceutical Co., Ltd. is in charge of manufacturing as well as sales and promotion in the domestic market.

Results for 2018:

Revenue	Adjusted Operating Profit
114.0 (JPY BN)	28.4 (JPY BN)
+8.9% Year-on-Year Change	+18.0% Year-on-Year Change

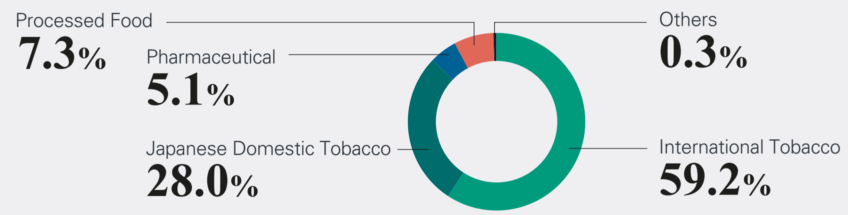
Processed Food Business

Our processed food business primarily engages in frozen and ambient processed food (mainly staple food products such as frozen noodles, frozen rice, packed cooked rice and frozen baked bread), seasonings (including yeast extracts and oyster sauce), and bakery chain outlets mainly in the Tokyo metropolitan area.

Results for 2018:

Revenue	Adjusted Operating Profit
161.4 (JPY BN)	4.1 (JPY BN)
-1.1% Year-on-Year Change	-23.6% Year-on-Year Change

Revenue Breakdown by Business Segment



Japan Tobacco Inc. and Consolidated Subsidiaries

Results for the fiscal year ended December 31, 2018

For the year:	2014 (Jan-Dec)	2015 (IFRS)	2016 (IFRS)	2017 (IFRS)	**2018 (IFRS)**
	(Continuing operations)				Billions of yen
Revenue (Note 1)	2,259.2	2,252.9	2,143.3	2,139.7	**2,216.0**
International Tobacco	1,328.0	1,317.2	1,199.2	1,237.6	**1,312.3**
Japanese Domestic Tobacco	687.4	677.3	684.2	626.8	**621.4**
Pharmaceutical	65.8	75.6	87.2	104.7	**114.0**
Beverage	–	–	–	–	**–**
Processed Food	161.2	165.8	164.1	163.1	**161.4**
Others	16.9	17.0	8.6	7.5	**6.8**
Core revenue (Note 2)					
International Tobacco	1,258.2	1,252.5	1,138.8	1,177.0	**1,250.7**
Japanese Domestic Tobacco	649.8	642.2	649.7	590.6	**582.4**
Operating profit (Note 3)	572.6	565.2	593.3	561.1	**565.0**
International Tobacco	379.5	346.9	301.8	325.6	**339.5**
Japanese Domestic Tobacco	181.5	249.2	244.1	215.8	**192.5**
Pharmaceutical	(7.3)	(2.3)	9.7	24.1	**26.3**
Beverage	–	–	–	–	**–**
Processed Food	(1.2)	3.2	5.0	5.4	**2.9**
Others	20.2	(31.8)	32.7	(9.8)	**3.8**
Adjusted operating profit (Note 3)	661.0	626.7	586.8	585.3	**595.5**
International Tobacco	447.1	394.4	336.2	351.3	**384.5**
Japanese Domestic Tobacco	238.7	254.1	260.2	232.3	**209.0**
Pharmaceutical	(7.3)	(2.3)	9.7	24.1	**28.4**
Beverage	–	–	–	–	**–**
Processed Food	1.4	2.7	5.0	5.4	**4.1**
Others	(18.9)	(22.2)	(24.4)	(27.8)	**(30.6)**
Depreciation and amortization (Note 3)	128.6	133.1	140.8	145.4	**158.7**
Profit (attributable to owners of the parent company) (Note 4)	391.4	398.5	421.7	392.4	**385.7**
Free cash flow (FCF)* (Note 5)	455.4*	386.7*	(316.2)	72.6	**105.6**

* Results from continuing operations and discontinued operations for both 2015 and Jan-Dec 2014.

Results for the fiscal year ended December 31, 2018

Consolidated (Continuing and discontinued operations combined) At year-end:	FY2014 (IFRS)	2015 (IFRS)	2016 (IFRS)	2017 (IFRS)	**2018 (IFRS)** Billions of yen
Assets	4,704.7	4,558.2	4,744.4	5,221.5	**5,461.4**
Interest-bearing debts (Note 6)	228.2	255.3	555.3	755.8	**987.6**
Liabilities	2,082.2	2,036.7	2,216.3	2,379.5	**2,761.0**
Equity	2,622.5	2,521.5	2,528.0	2,842.0	**2,700.4**
Major financial ratios					
ROE (Note 7)	14.4%	19.5%	17.2%	15.0%	**14.3%**
ROA (Note 8)	10.8%	14.8%	12.4%	10.8%	**10.0%**
Amounts per share: (in yen)					
Diluted EPS (Note 9)	199.56	270.37	235.33	218.97	**215.20**
Book value per share (attributable to owners of the parent company)	1,395.74	1,369.06	1,371.39	1,541.94	**1,468.44**
Dividend per share	100	118	130	140	**150**
Dividend payout ratio (Note 9)	50.1%	53.2%**	55.2%	63.9%	**69.7%**

** Payout ratio for 2015 is based on basic EPS from continuing operations.

Notes:

1. Excludes tobacco excise taxes and agency transactions. In addition, from 2018, in accordance with the application of IFRS 15, certain items formerly treated as selling, general and administrative expenses are accounted for as reductions of revenue.
2. Excluding revenue from distribution business of imported tobacco, among others, in the Japanese domestic tobacco business, in addition to the distribution, contract manufacturing, and other peripheral businesses in the international tobacco business.
3. Adjusted operating profit = Operating profit + amortization cost of acquired intangibles arising from business acquisitions + adjusted items (income and costs)*
   *Adjusted items (income and costs) = Impairment losses on goodwill ± restructuring income and costs ± others.
4. Under IFRS, profit is presented before deducting non-controlling interests. For comparison, we show the profit attributable to the owners of the parent company.
5. FCF = Cash flows from operating activities + cash flows from investing activities excluding the following items:
   From "cash flows from operating activities:" Interest and dividends received, interest paid and income taxes related to these items.
   From "cash flows from investing activities:" Purchase of securities/proceeds from sale and redemption of securities/payments into time deposits/proceeds from withdrawal of time deposits/others (but not business-related investment securities, which are included in the investment securities item).
6. Including lease obligation.
7. ROE = Return on equity (attributable to owners of the parent company).
8. ROA = (Profit before income taxes)/Total assets (average of beginning and ending balance of the period).
9. Based on profit (attributable to owners of the parent company).
10. The financial data disclosed herein are rounded.

Under the 4S model, we strive to fulfill our responsibilities to our valued consumers, shareholders, employees and the wider society.

Yasutake Tango

Chairman of the Board

Y. Tango

Masamichi Terabatake

Representative Director and President, Chief Executive Officer

M. Terabatake

> We have attained sustainable profit growth and will continue through the pursuit of the 4S model.

Achieved Robust Profit Growth while Strengthening the Business Foundation for the Future

In 2018, the operating environment surrounding us continued to be challenging due to the changes in the global economy and political conditions, significant currency volatility and increased geopolitical risks. However, even in such an environment, we believe that 2018 was a year in which we achieved robust profit growth while strengthening the business foundation for sustainable profit growth in the future. In the Japanese domestic tobacco business, our presence in the RRP category was boosted by the nationwide Ploom TECH distribution. We also completed the development of new RRP such as Ploom TECH+ and Ploom S. On a conventional products front, which is the platform of profitability to support growth, we further solidified our leading position through market share gains. In the international tobacco business, we achieved strong profit growth by growing market share in our key markets and implementing a steady pricing strategy and reinforced our earnings base for further growth. In addition, we completed acquisitions in Russia and Bangladesh, and in parallel, made excellent progress integrating businesses in the Philippines, Indonesia and Ethiopia where we completed acquisitions in 2017. With regard to the pharmaceutical and processed food businesses, they fully delivered on their role to complement the Group's profit growth during 2017 and 2018, when the Japanese domestic tobacco business was facing significant headwinds. Furthermore, we are advancing a variety of initiatives to evolve our organizational capabilities in order to ensure our sustainable growth into the future. We have been putting greater focus on consumers in all that we do, as represented by our sales activities, now emphasizing face-to-face and interactive communication with consumers in the Japanese domestic tobacco business. In addition, we are accelerating collaboration between JT and JTI, aiming to make our business even more competitive and agile. As an example, we have been integrating the R&D functions of JT and JTI.

Achieve Sustainable Profit Growth for the JT Group

The key to our future success has and will continue to depend on the tobacco business. Even in an increasingly uncertain and challenging business environment, the tobacco business will play a role as the core driver of the Group's profit growth. Our Japanese domestic tobacco business will resume profit growth from this year. In parallel, it is our strong intention to increase our combined market share of RRP and conventional products by offering consumers a variety of options in each category. In the international tobacco business, we aim to continue strong profit growth through our growth agenda which includes sustainable profit growth in existing markets, geographic expansion in emerging markets and acceleration of growth in the RRP category. In 2018, our strong results confirmed that the pricing environment is still robust and that, globally, there are still opportunities to expand the profit pool of the tobacco industry.

In the pharmaceutical and processed food businesses, while both businesses are facing harsh conditions, we will rebuild a solid business base as early as possible, so that they can again complement the Group's profit growth.

Shareholders Return

Our resource allocation policy is to prioritize business investments for sustainable profit growth over the mid- to long-term as well as to strike a balance between business investments for sustainable profit growth and shareholder returns.

With regard to our shareholder return policy, we aim to enhance shareholder returns considering our mid- to long-term profit growth trend, while maintaining a strong financial base. Specifically, we work toward stable and consistent growth in dividend per share. Decisions under this policy, have been largely carried out based on the growth rate of adjusted operating profit excluding foreign exchange impacts, an indicator which represents our business performance. However, looking at all the dynamics influencing us, we decided to take into account the level of net income expected in fiscal year 2019, which will include foreign exchange impacts, to determine the dividend per share. Thus, we plan to offer an annual dividend per share of 154 yen in 2019. Looking ahead, we will continue to work toward stable and consistent growth in dividend per share and focus on adjusted operating profit excluding foreign exchange impacts as an indicator of our business performance. Lastly, we have announced that we decided to conduct a share buybacks, of up to 50 billion yen or 23 million shares, as part of our efforts to provide returns to shareholders.

Our Management Principle "4S Model"

Our management principle is the 4S model. Under the 4S model, we strive to fulfill our responsibilities to our valued consumers, shareholders, employees and the wider society, carefully considering the respective interests of these four key stakeholder groups, and exceeding their expectations wherever we can. We believe that pursuing this 4S model is the best approach to achieving sustainable profit growth over the mid- to long-term and thus increase the Group's enterprise value. It means that this conveys benefits to the four stakeholder groups.

We have enhanced our corporate governance, which is one of the key challenges for management. We base this on our belief that it is the means for conducting transparent, fair, timely and decisive decision-making for pursuing the 4S model.

In March 2019, we established the Advisory Panel on Nomination and Compensation to take over the functions of the existing Compensation Advisory Panel. The new Panel is comprised mainly of Independent Outside Directors and serves as a voluntary advisory panel to the Board of Directors. We also increased the number of Outside Directors and Outside Audit & Supervisory Board Members by one each. Through these initiatives, we are strengthening the supervisory functions and transparency of business.

We continuously aim to fulfill our responsibilities as a member of society in order to remain the preferred choice of consumers, shareholders, employees and the wider society.

Be Better, Be Faster and Be Bolder
JT is striving to be No. 1 globally by accelerating its efforts towards becoming "a company that initiates change and drives evolution."

Masamichi Terabatake

Representative Director and President,
Chief Executive Officer

In 2018, we achieved our profit target. Going forward, we will continue to prioritize business investments as we aim to ensure sustainable growth.

2018 Key Highlights

Adjusted Operating Profit
595.5
(JPY BN)
+1.7%
Year-on-Year Change

Adjusted Operating Profit at Constant FX
+8.9%
Year-on-Year Change
637.2
(JPY BN)

Annual Dividend per Share
150
(JPY)
+7.1%
Year-on-Year Change

In 2018, my first year as Group CEO, I strove to thoroughly pave a new path within the Group, and those efforts are starting to bear fruit.

Adjusted operating profit at constant FX basis grew 8.9% year-on-year, enabling us to achieve sustainable profit growth and strengthen our business foundation despite a challenging environment.

In the international tobacco business, market share gains and strong pricing in key markets, supported by the positive impact of acquisitions, drove profit performance. In the Japanese domestic tobacco business, we completed the nationwide expansion of Ploom TECH and solidified our leading position in cigarettes by increasing our market share. In the pharmaceutical business, we achieved our profit target driven by increasing royalty revenue. Going forward, due to the end of a licensing agreement in Japan related to an anti-HIV drug, we expect overseas royalties to decrease. However, we will continue working to maximize product value across the board while researching and developing next-generation strategic products. Lastly, although profit declined in the processed food business due mainly to increasing raw material costs, we will continue striving to boost profitability by stepping up sales of mainstay products and improving productivity.

During my first year as Group CEO, my priority was to strengthen our Japanese domestic tobacco business. I visited each of our domestic sites and spent a lot of time sharing my ideas directly with employees, literally telling them "I want you to think this way" or "behave in this manner". To ensure continued growth amid this tough environment, I focused on getting the JT Group and all its employees on the same page regarding what needs to be done.

Be Better, Be Faster and Be Bolder—this is the mantra we adopted after I became Group CEO. Before assuming this role, I worked at JT International S.A., a Group company based in Switzerland. The main thing I noticed when I returned to Japan was a difference in speed. I felt that decision making at JT took an excessive amount of time, especially when it came to decisions that extended beyond the organization or that encompassed multiple departments. I sensed that this lack of speed was putting us at risk, so I directed my efforts at accelerating the processes internally by promoting greater delegation of authority.

The new mantra emphasizes the fact that we will never be able to beat the competition in the future if JT does not actively change its current ways of thinking and working. We must change JT to increase the speed at which it does business. Throughout 2018, I promoted extensively this policy of "Be Better, Be Faster and Be Bolder." I believe there has been a solid response, with each of our organizations and every employee beginning to do all they can right now. For example, we quickly responded to the rapid expansion of Reduced-Risk Products (RRP) in Japan, by uncovering growth opportunities and revising our sales structure to coordinate our employees' efforts.

"We are not going to wait for change to happen. If JT continues to take action, we will see growth proliferate across Japan and the globe."

We have created an unshakable business foundation, and, in any environment, our policy will be based on the unwavering management principle of the 4S model.

The tobacco industry has traditionally had a reputation for being able to accurately assess medium- to long-term business conditions. With the emergence of the new RRP category over the last two to three years, however, we have witnessed faster changes. Naturally, investment in RRP has grown, but investors are still somewhat uneasy about whether they really can count on returns. Businesspeople, meanwhile, are feeling increasingly uncertain about the environment surrounding JT, including changes in international politics, issues associated with Brexit and other geopolitical risks, and exchange risks related to the currencies of emerging economies. In the tobacco industry, conditions grow harsher every year due to intensifying competition in the RRP category as well as tightening regulations, tax increases, and a natural decline in overall demand in the face of rising health awareness.

The JT Group—the third largest global tobacco company—adopted the 4S model to transform these risks into opportunities. Consumers are the core of the 4S model. Under this model, we will continuously provide them with better products and increase the number of options on offer. Then, we will utilize the profits gained from doing so to provide a competitive level of returns to shareholders and wider society as well as fair compensation for employees. In addition, to realize sustainable profit growth, we will not focus solely on short-term profits; rather, to ensure solid medium- to long-term returns, we will strongly prioritize business investment. By repeating these actions, we will improve profitability and deliver a stable financial foundation, which, in turn, will allow us to commit to mid to high single-digit profit growth over the mid- to long-term.

> "Deciding where to focus our limited investment capacity is one of our strengths."

One of our strengths is the fact that the 4S model is a shared philosophy that has become engrained throughout the JT Group. Obviously, it will take time for the employees of acquired companies to fully understand the 4S model. Some of our acquisitions have been utterly unprepared for business investment. When I speak to them, I explain that we can outperform the competition through such actions as overhauling production systems and unifying global brands as well as by creating products that consumers want and by appropriately investing in brand equity. I also tell them how critical it is to invest in the business with an eye on mid- to long-term returns. And, as we reap the results of these actions, they will come to understand the 4S model and that this way of thinking is the right way forward. This embodies the ideal the JT Group strives for, which is a little different from that of other tobacco companies or, for that matter, European and American companies. Employees who have had lengthy careers outside of JT will come to truly understand that sustainable growth is central to JT's business model, and I feel that this has become engrained as a steadfast policy.

M&A also provides the ultimate pool of human resources for us. We thoroughly assess each individual, giving consideration to who is best for each position, regardless of their experience or background, such as whether they came from Gallaher, JT or R.J. Reynolds. This is what we have always done. We try to be as fair as possible to each employee and place people according to their abilities regardless of their background; in this way, we have maximized the performance of the Company. By respecting the diversity of our employees' values and attributes, we have fostered an environment in which everyone can reach their full potential. Our employees represent over 100 nationalities, and we appreciate their expertise, experience, age, gender, and nationality. In the management of our diversity-rich organization, we are always trying to be fair, transparent, and respectful. This is what I believe in, a conviction that springs from our unique corporate culture.

We view risks as growth opportunities and aim to become the Global No. 1 tobacco company.

Our medium- to long-term vision in the tobacco business is to be No. 1 globally. In this case, No. 1 means steadily expanding our share of the market in each country to achieve the No. 1 sales volume in the world as well as being the first choice of consumers. Over the last twelve months since I took over the reigns, after clearly defining what we meant by No. 1, we have been adjusting our operations accordingly.

To realize our vision, we have put in place three major strategies. The first is enhancing the equity of our brands. This means solidly expanding our current market share in countries where we already have a large share, including Japan. To do so, we will steadily invest in our existing brands and products, and differentiate ourselves by developing products that consumers enjoy along with prompt and efficient services. This will, in turn, lead to steady gains in profit.

The second strategy is geographic expansion in emerging markets. As we look toward the future, we will invest some of the profits earned from existing strongholds in emerging markets. Before I assumed the role of Group CEO, I led M&A efforts, notably in 2017 with transactions in the Philippines, Indonesia and Ethiopia. In 2018, we carried out M&A in Russia and Bangladesh. These investments enhanced our revenue immediately, with the potential to generate even more revenue in the future by boosting sales volume. While we are steadily expanding our footprint in major markets, there remain markets where our presence is small. We are now turning our attention toward Asia, Africa, and South America in pursuit of greater growth for the tobacco business.

Our third major strategy is to actively invest in RRP, including in Japan. I have been involved in this new category since 2014, when I became responsible for the RRP operations at JT International S.A., overseeing investment aimed at enhancing manufacturing and R&D capabilities. In my new role, I will ensure we continue to strengthen our presence in the category and expect to invest a total of 200.0 billion yen by 2020. Moreover, in 2019, we revised the structure of the R&D organization, optimally distributing resources throughout the JT Group to enhance competitiveness. We have now begun sprinting toward the realization of our vision through the implementation of these three strategies.

> "We make decisions with an eye toward the future. However, our options are limited when no profits are made."

Japan has garnered global attention due to the rapid growth of its RRP market. The percentage of the domestic tobacco market accounted for by RRP grew from almost nothing to 3% in 2016, 12% in 2017, and 21% in 2018. This means that there had been a need for RRP in Japan all along, and, despite being the leader in the Japanese market, JT did not notice that need. As a result, consumers shifted to other companies' products. Realizing that we should have recognized this need sooner, we instructed the sales teams to rethink their approach; they should be putting consumers at the forefront and thinking about how to improve.

Although we had previously preached putting consumers at the forefront, our thinking may have been biased toward patrons of tobacconists and convenience stores. We might have been too caught up in how to control points of sale and how our products are displayed, rather than focusing on end-users.

We began 2018 by reflecting on whether we really had in place a system to listen to the needs of consumers. Our approach was to rely more on the sales teams by placing them at the core of the system. The approach allowed for more direct communication with the consumers and their feedback, enabling us to better identify consumer needs and prepare a wide array of options to satisfy these needs. Actually, we have developed a system that can design options to meet a broad range of needs; we can then develop products and test them with consumers. If the results are positive, we work to expand sales, and if they are not, we quickly move on and release something new. We develop products by broadening our imagination, thinking about what kind of needs consumers have and realizing how we can meet those needs. We do this again and again. While this all might seem obvious, we made a lot of progress in 2018 toward building a system that can foster the right kind of mindset and awareness. We are currently working to expand our lineup. Also in 2018, we rolled out the low-temperature heating product Ploom TECH nationwide, and, in January 2019, we initiated sales of Ploom TECH+, which has a richer vapor, as well as the high-temperature heating product Ploom S.

Ploom TECH uses JT's original low-temperature heating technology to greatly reduce the generation of odor* and allow consumers to enjoy a variety of flavors with a clear tobacco taste. Some consumers of tobacco products are themselves sensitive to the odor of tobacco and many people who don't smoke tobacco are also very sensitive or dislike its odor. RRP is one tool to help solve the problem posed by odor, and we expect that this strong Ploom TECH attribute will offer a huge opportunity moving forward. We are thinking about consumers in different situations, such as doing office work or going about everyday tasks. Consumer needs may vary depending on if they are in a factory, a senior facility, or a hotel or operating some kind of vehicle. For example, at senior facilities, there is the societal need to refrain from using fire to ensure safety. Delivery drivers also are prohibited from using fire and want to avoid filling up the ash tray. They also do not want to leave behind any odor, which could cause problems when another driver uses the vehicle. Smokers worry about whether

* Odor that is less than 1% of the strength of that of ready-made cigarettes

hotels have smoking rooms available. We believe that our products offer a tailored solution to these various societal and latent needs. These products can also help bring about a society where smokers and non-smokers coexist in harmony. We can create business opportunities by looking at issues from different perspectives to uncover needs and expand our RRP offerings.

We also consider regulations to be opportunities. In 2018, in the lead up to the Tokyo Olympics and Paralympics, Japan's Diet passed The Revised Health Promotion Act, which is expected to be enforced in stages by April 2020. Restaurants and bars that understand the characteristics of Ploom TECH allow patrons to use Ploom TECH even in areas that currently prohibit cigarettes. These establishments numbered around 800 a year ago but now exceed 3,700. Once the benefits of Ploom TECH are explained to business owners as well as consumers, they realize, “Hey, this product is really great. It enables smokers and non-smokers alike to coexist.” More and more businesses are therefore allowing people to enjoy the product in their establishments, leading to the considerable growth seen in just one year. Earlier, I mentioned that we are changing our sales system so that we can communicate directly with consumers. We think another of our accomplishments this year has been an improvement in our understanding of regional characteristics and the strengthening of our sales networks rooted in regional communities.

Globally, the RRP market is still in its infancy. Although it has grown quite rapidly in Japan, no other country has matched that speed of growth. If the JT Group can first reestablish its position in Japan by capturing a larger share of the market, we can use that know-how to expand globally. The real battle has yet to begin.

> “We are under a lot of pressure, but our employees are enthusiastic and our manufacturing system is in place. The real battle has yet to begin.”

Our sustainability strategy supports the sustainable growth of our business.

In order for our Group to achieve sustainable growth, it is essential for our business to contribute to the sustainable development of our society. With this in mind, we launched our sustainability strategy in 2018. Global conditions and regulations are changing at a fast pace and the rapid growth of RRP has brought further changes to our business environment. We need to position and consider sustainability at the center of managing our business. In 2019, we appointed an Executive Officer dedicated to sustainability management and transformed the CSR Division into the Sustainability Management Division. We have tied our sustainability strategy to our business activities and to our contributions to SDGs. By pursuing the strategy globally, we will strengthen our commitment to sustainability.

In our tobacco business, we have set out four strategic focus areas: 1) products and services, 2) people, 3) supply chains, and 4) regulatory environment and illegal trade. The four strategic focus areas are supported by the JT Group's three absolute requirements for sustainability: respect for human rights, an improved social and environmental impact, and good governance and business standards. Specific targets have been set for the focus areas and by implementing PDCA cycles, we will continue to support sustainable growth. As for building a sustainable supply chain and ensuring a sustainable tobacco leaf procurement structure, rather than merely purchasing tobacco leaf from the market, we source about half of our leaf from tobacco dealers while the other half is purchased directly from contracted farmers. Securing a long-term supply of quality leaf at the best cost is critical to our future growth. By building strong relationships with our farmers, we help improve their incomes and standards of living as well as labor practices, environmental and social conditions. Furthermore, since 2011 we have been working through the ARISE (Achieving Reduction of Child Labor in Support of Education) program to eliminate child labor at tobacco farms.

Environmental protection is also essential. As a responsible company, JT operates its businesses without increasing environmental impact. Under the Environment Long-term Plan 2020, we have been taking steps to reduce the environmental impact of our Group. As a result, in 2017, we achieved our target to reduce total Greenhouse Gas (GHG) emissions three years ahead of schedule. Furthermore, we are turning our attention to the future and we have started to establish the JT Group Environment Plan 2030. Under the new plan, we will further strengthen initiatives aimed at environmental issues that could have long-term impact, not only for our Group, but also for our value chain.

By transforming itself, JT is bringing change as it steadfastly works toward sustainable growth.

No matter the environment, we believe business investment should be the priority when allocating management resources. We will also strive to steadily increase dividends while carefully balancing shareholder returns and business investments for sustainable profit growth. As for returns to shareholders, we have increased dividends in line with the pace of growth of adjusted operating profit at constant FX basis.

There has been no change in this basic policy. However, to maintain a robust financial foundation while steadily and continuously increasing dividends, we have decided to also take into consideration annual net income from fiscal year 2019 forward. As always, we will still prioritize business investment that leads to sustainable profit growth over the medium- to long-term. We will then utilize those earnings to return them at a competitive level to our shareholders while continuing to monitor trends in returns for global fast moving consumer goods (FMCG) companies.**

In 2018, I got off to a strong start in my first year as Group CEO with all of these measures. The tobacco business still has untapped potential for growth and the confidence to spark that growth. We believe that the Japanese domestic tobacco business bottomed out in 2018 and have outlined a plan to boost revenue and profit in 2019. In 2018, the international tobacco business returned to a path of profit growth driven by strategic pricing. The tobacco business overall will therefore achieve mid to high single-digit growth over the medium- to long-term. The pharmaceutical business will continue to rebuild its business foundation. The processed food business established the Food Business Planning Division in 2019. Under this new business operation system, we will work to sustainably improve profit and aim to complement Group-wide profit growth through both the pharmaceutical and processed food businesses.

With the advent of new technologies and rapid changes in the business environment, we are no longer able to rely on conventional models for success. Through unwavering adherence to the 4S model, with our diverse human resources working more boldly and with unprecedented speed, and by transforming ourselves, we aim to continue realizing sustainable growth.

** FMCG companies: Specifically, Fast Moving Consumer Goods (daily consumer goods) companies which have a stakeholder model similar to our “4S” model, and which realize strong business growth

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In FOCUS — Tackling the Illegal Trade of Our Products on p. 18
Business Plan 2019 on p. 20
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Our Sustainability Strategy

4S Model

Our management approach and our approach to sustainability are underpinned by our 4S model. Consumers, shareholders, employees and society represent the four stakeholder groups (4S) at the heart of everything we do. Based on the principles of the 4S model, we always strive to exceed the expectations of our four stakeholder groups, wherever we can.

In order for our group to achieve sustainable growth, it is essential for our business to contribute to the sustainable development of our society. We maintain ongoing dialogues with our stakeholders and work continuously on a variety of sustainability issues to fulfill our responsibilities as a member of our society.

United Nation's Sustainable Development Goals (SDGs)

Our group supports the United Nation's Sustainable Development Goals. We would like to contribute to the following SDGs through our business activities and sustainability initiatives.

The JT Group's Sustainability Strategy

In 2018, our tobacco business, the Group's core business, launched its sustainability strategy. The strategy encompasses our material issues and it is also underpinned by our 4S model. There are four focus areas with three absolute requirements for sustainability. The three absolute requirements for sustainability apply across the Group.

Tobacco Business – Sustainability Strategy

Four Focus Areas

Products and Services	We will be a total tobacco company offering consumers an even greater choice of products by focusing on quality, innovation and reduced-risk potential.
People	We will be the employer of choice by investing in people.
Supply Chain	We will reduce environmental and social risks, and enable transparent and responsible practices across our supply chain.
Regulatory Environment and Illegal Trade	We will ensure the company is included in policymaking leading to fair and balanced regulation and enhance our cooperation with governments to combat illegal trade.

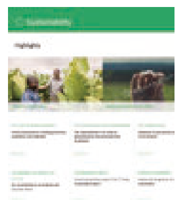
Three Absolute Requirements

RESPECT FOR HUMAN RIGHTS	AN IMPROVED SOCIAL AND ENVIRONMENTAL IMPACT	GOOD GOVERNANCE AND BUSINESS STANDARDS
We are committed to respecting human rights across our global operations and value chains, as expressed in our JT Group Human Rights Policy.	We are committed to protecting the environment and making a positive difference wherever we operate.	We are committed to promoting transparent, fair, and timely decision-making that carefully considers the respective interests of consumers, shareholders, employees, and the wider society.

Read more about the four strategic focus areas and the related targets of our tobacco business in the FY2018 JT Group Sustainability Report. The report will be available on JT's website at the end of May 2019.

Furthermore, our pharmaceutical business and processed food business are both currently formulating their respective sustainability strategies.

Learn more about JT Group's approach to sustainability on our website:
https://www.jt.com/sustainability/



Leaf Supply

Tobacco leaf sourcing is a key part of our supply chain, and a critical component of future business growth. We purchase approximately half of our tobacco leaf from directly contracted growers, and the other half from tobacco leaf merchants.

Agricultural Labor Practices

Our Agricultural Labor Practices (ALP) are based on the International Labor Organization's conventions and recommendations. The program consists of three pillars: tackling child labor, respect for the rights of workers, and ensuring workplace health and safety.

Whether we source tobacco directly or through leaf merchants, all of our suppliers have a contractual obligation to implement our ALP. The program drives a continual cycle of improvement and dialogue, a concept deeply rooted in our business. See more on ALP in our leaflet published on jti.com.

We previously made a commitment to implement ALP in all sourcing countries by 2019. We are pleased to share that in 2018, we observed 96% of our directly contracted growers and 96% of our leaf merchants reported against ALP.

	2016	2017	2018
Directly contracted growers observed against ALP	21%	90%	**96%***
Leaf merchants who reported against ALP	31%	73%	**96%**

* This percent includes Japan.

We were able to achieve almost 100% coverage in a relatively short period of time due to a successful pilot program that ran between 2013 and 2016. Our learning shaped our current approach and enabled an effective implementation with both our directly contracted growers and leaf merchants.

We have now broadened the target to include new acquisitions such as Ethiopia and Bangladesh.

Agricultural Labor Practices
We will implement our Agricultural Labor Practices (ALP) program in all sourcing countries by 2025.

ARISE

Our flagship program, ARISE – Achieving Reduction of Child Labor in Support of Education – has been committed to tackling child labor in our tobacco growing communities since 2011. In preparation for the next phase of the program, in 2018 the ARISE team carried out a Social Return on Investment assessment of the program. The aim was to better understand the value of our investments, from the perspective of our beneficiaries.

JT Group Environment Plan 2030

The JT Group strives to foster a healthy, sustainable and productive environment for future generations by balancing our activities and our relationship with the environment across our value chain and in wider society. We believe that reducing environmental impacts contributes to the sustainable growth of the JT Group, as it results in efficient resource use, improved performance and cost reduction.

In 2014, we established the Environment Long-term Plan 2020, and we have been taking steps to reduce our environmental impacts. Under this long-term plan, we have strengthened our approaches to reducing the environmental impacts across the JT Group, covering all the locations in the Japanese domestic tobacco business, the international tobacco business, the pharmaceutical business and processed food business.

Through a number of initiatives, we achieved in 2017 our key target to reduce total Greenhouse Gas (GHG) emissions from our operations by 20%, three years ahead of the schedule. Given this and that we are approaching 2020, the target year of the current plan, we have started to establish the JT Group Environment Plan 2030, looking beyond 2020.

Based on the JT Group Environment Plan 2030, which takes account of the social and business environments that have changed dramatically in recent years, we will be addressing environmental issues that may have a long-term impact on the JT Group's value chain. Specifically, we will set clear objectives and targets for Energy and Emissions, Natural Resources (water and forestry), and Waste.

For detailed information, please refer to the FY2018 JT Group Sustainability Report, which is scheduled to be published at the end of May 2019.

Our Greenhouse Gas reduction targets by 2030 confirmed as Science Based Targets (SBT)

We have set a long-term GHG emission reduction target in line with the Paris Agreement, which was approved as SBT by the Science Based Targets initiative in February 2019.

SCIENCE BASED TARGETS
DRIVING AMBITIOUS CORPORATE CLIMATE ACTION

Received high recognition from CDP (formerly the Carbon Disclosure Project)

Our approach to climate change was showcased as one of the best practices in the CDP Stories of Change published in January 2019.

CDP
DISCLOSURE INSIGHT ACTION

In FOCUS – Tackling the Illegal Trade of Our Products

Experts estimate that over 10% of all cigarettes sold globally (excluding China) are illicit, with approximately US$45 billion in global tax revenue lost each year. This illegal trade fuels human trafficking, organized crime, and terror groups; and undermines legitimate tobacco businesses. It also causes harm to consumers, as uncontrolled products circumvent regulations and quality controls.

Tackling illegal trade is a top priority for us, and our Anti-Illicit Trade team is recognized as the industry leader in combating this problem.

Key Wins in 2018

We advised 1,329 law enforcement officers on counterfeit recognition
With the goal of reducing the supply of illegal products

Over 2,775 million illegal cigarettes seized
Thanks to intelligence reports provided by our team to law enforcement

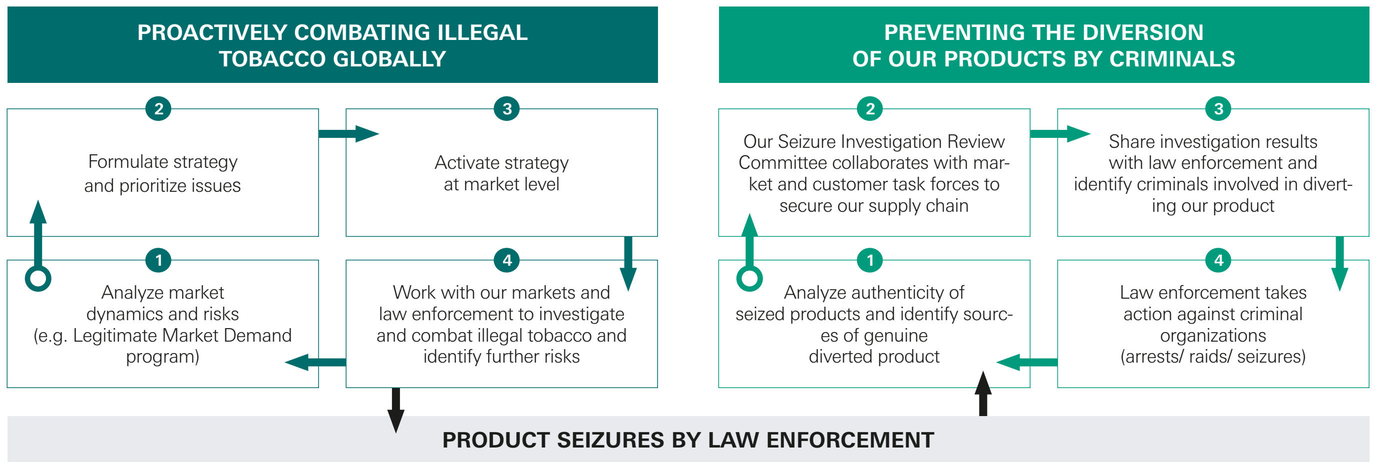
32% decrease in seizures of our genuine products
Resulting from our efforts to ensure the security of our supply chain

"JTI makes an important impact on illicit trade which is good for seizures and it's a good position regarding intelligence sharing. JTI is in the lead."

Margarete Hoffman
Head of Policy, Directorate D, OLAF

Our Approach

Our global Anti-Illicit Trade team investigates the illegal tobacco trade and protects consumers and society, as well as our business, from criminal elements. A key part of our business, the team works with our markets to secure our supply chain, and assists law enforcement in removing illegal tobacco from the marketplace. They maintain a robust dialogue with governments and law enforcement agencies on the threat of illegal tobacco through public private partnerships. Our Anti-Illicit Trade team also supports other areas of our business with research on illegal tobacco and raises awareness of the problem among our business partners, consumers and society in general. The team protects the JT Group's business and reputation, supporting our long-term, sustainable future.



Supporting Business Performance through Anti-illicit Trade Programs

Our global anti-illicit trade programs create the opportunity for public-private partnerships to combat highly organized criminality. They are also designed to support our business performance by fulfilling all legal requirements, securing our supply chain, safeguarding and creating opportunities for volume and profit growth, and protecting our company's reputation.

	Key Strategies	Key Initiatives		2018 Performance
1	**Protect our business through anti-illicit trade operations** Focus on priority regions & markets Combat counterfeit and illicit whites*	Anti-illicit trade task forces set up in priority markets		In 2018, new task forces were set-up in our Russia, Ukraine and Belarus priority markets. In 2018, our intelligence led to the seizure of over 2,775 million cigarettes (or equivalent in tobacco).
2	**Ensure anti-illicit trade compliance** Fulfill legal obligations Legitimate Market Demand analyses and seizure investigations	Efficient and effective responses to information requests by law enforcement agencies		We responded to over 500 law enforcement information requests in 2018, and are fully compliant with all our legal obligations.
3	**Strengthen our partnership with customers, government and law enforcement** Knowledge sharing with law enforcement Implement anti-illicit trade awareness programs	Advise law enforcement on counterfeit recognition	Global media campaigns to educate consumers on the impact of illegal trade	In 2018, we advised 1,329 law enforcement officers on counterfeit recognition.

* Illicit whites: Tobacco products manufactured legitimately but without any product flow control measures afterwards and, smuggled and sold in another market.

Protecting Our Business

In 2018 our Anti-Illicit Trade team provided 1,328 intelligence reports to law enforcement agencies, leading to the seizure of more than 2,775 million illegal cigarettes. Based on our information, law enforcement raided more than 39 counterfeit tobacco factories and storage locations.

As a direct result of our work to tackle illegal trade, and based on seizure statistics, notified seizures of counterfeit products in the EU have increased by 82% over the past four years. During the same period, notified seizures of our own genuine products in the EU have decreased by 57%, thanks to our efforts in securing our supply chain in each market, with the support of the Anti-Illicit Trade team. This has been acknowledged by both the EU and the UK's HM Revenue and Customs, which recognized JTI as an industry leader in the fight against illicit trade.

Taking the Fight to the Digital World

Our project to tackle illegal online trade expanded across Western Europe in 2018. It yielded excellent results, disrupting sales through the takedown of links and social media posts that advertise JTI products illegally.

In 2018, we took down over 5,960 posts and over 65,300 items. This represents US$710,433 worth of potential product losses to the JT Group.

We continue to take down illegal advertisements and collaborate with law enforcement agencies by providing evidence that leads to prosecutions.

Drawing upon this continued success, similar projects have now launched in the Americas and Eastern Europe regions.

Ensuring Anti-illicit Trade Compliance

We comply with the European Union Cooperation Agreement signed in 2007, supplying tobacco products only in volumes that correspond with the legitimate demand of the intended market of retail sale. We have developed a global methodology to assist our markets with their annual 'Legitimate Market Demand' (LMD) calculations. Our markets perform these calculations in conjunction with their annual plan, creating a proactive supply chain control mechanism to make sure that the planned sales volumes are in line with LMD.

In 2019, some JTI markets will be implementing a mandatory Track and Trace system, including the 28** Member States of the European Union as per the European Tobacco Products Directive. We are working with key stakeholders to comply with these regulations in the most effective way, while ensuring affected markets will not be disrupted.

** As of March 31, 2019

In September 2018, the WHO FCTC Protocol to Eliminate Illicit Trade in Tobacco Products entered into force. One of the main requirements is that the Parties must implement a Track and Trace regime by 2023 (for cigarettes) and by 2028 (for all other tobacco products). In order for this regime to be effective, we support the implementation of an architecture based on "open standards" and interoperability for every actor in the supply chain, whilst taking into account existing systems such as the new EU-wide Track and Trace system.

The JT Group's Business Plan covers a three-year period, and is rolled-over annually to reflect the most recent changes in our business environment including economics, geopolitics and competition. The operating environment surrounding us is expected to revolve dramatically. By developing ourselves into a company that initiates change and drives evolution, we aim to achieve sustainable profit growth under such circumstances.

Group profit target

Annual average growth rate of adjusted operating profit at constant currency over mid- to long-term: Mid to high single-digit

Shareholder return policy

Aim to enhance shareholder returns considering the Group's mid- to long-term profit growth trend, while maintaining a strong financial base*

- Work toward stable and consistent growth in dividend per share
- Consider implementing a share buy-back program, taking into account the Group's mid-term operating environment and financial outlook
- Continue to closely monitor shareholder returns of global FMCG companies**

* As its financial policy, the Company will maintain a strong financial base that secures stability in case of changes in the business environment, such as economic crises, and flexibility enabling expeditious responses to business investment opportunities.
** FMCG companies: Specifically, Fast Moving Consumer Goods (daily consumer goods) companies which have a stakeholder model similar to our "4S" model, and which realize strong business growth

Message from the CFO on p. 25

Role & objective of each business

Tobacco Business: The core and driver of the JT Group's profit growth

Japanese Domestic Tobacco Business : Return to sustainable profit growth with both RRP as our growth driver and cigarettes as our profitable platform to support growth, increase our total market share by offering consumers various options in each category

International Tobacco Business : Further strengthen its role as the JT Group's profit growth engine, through sustainable profit growth in existing markets, geographic expansion in emerging markets and acceleration of growth in the RRP category

Pharmaceutical & Processed Food Businesses: Complement the JT Group's profit growth by rebuilding their business foundations

Pharmaceutical Business : Promote R&D for next-generation strategic products and maximize the value of each product

Processed Food Business : Business operation for sustainable top-line growth

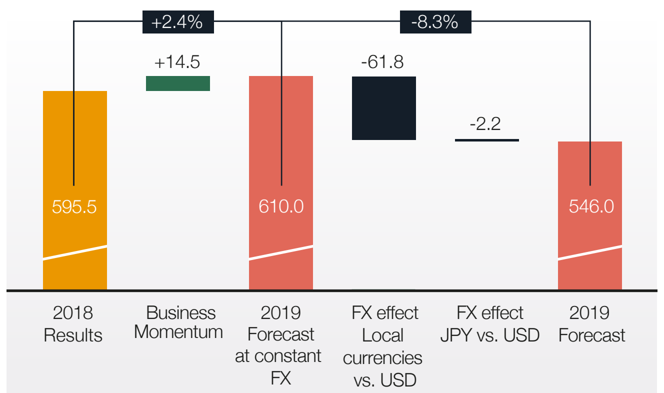
2019 Outlook

On a consolidated basis, we target adjusted operating profit at constant FX, our KPI, of 610.0 billion yen. We expect this year-on-year growth of 2.4% to be driven by the tobacco business, overcoming a significant decline in profit for the pharmaceutical business. On a reported basis, we forecast a decrease of 8.3% in adjusted operating profit due to the continuous negative FX impact.

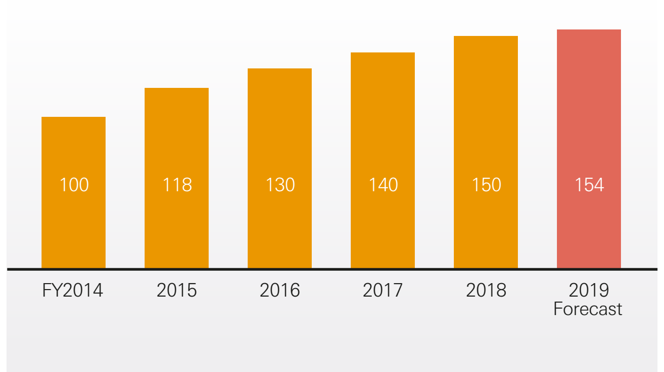
In the Japanese domestic tobacco business, the cigarette price increase in October 2018 and RRP top-line growth including Ploom TECH will more than offset the decline of JT cigarette sales volume and higher investment in sales promotions for RRP, leading to an increase in adjusted operating profit of 2.9% year-on-year. In the international tobacco business, as robust pricing gains are expected to continue in 2019 and taking into account the contribution from prior year acquisitions in Russia and Bangladesh, the adjusted operating profit in USD at constant FX is forecast to grow by 8.8%. On a reported basis, however, due to the depreciation of our key currencies, including the Iranian rial and Russian ruble, JPY based adjusted operating profit is expected to decline by 7.4%. For the pharmaceutical business, we forecast a significant decline in adjusted operating profit with the termination of the exclusive license agreements for anti-HIV drugs in Japan and also the decline of royalty revenue from outside of Japan. In the processed food business, despite soaring raw material costs, we are striving to improve profitability by enhancing productivity.

We plan to offer an annual dividend per share of 154 yen in 2019, representing a 2.7% increase year-on-year, based on the growth rate forecast of adjusted operating profit at constant FX. In addition, from fiscal year 2019, we will also consider the outlook for net income, under our shareholder return policy of "aiming to enhance shareholder returns considering the Group's mid- to long-term profit growth trend, while maintaining a strong financial base".

Adjusted Operating Profit (JPY BN)



Dividend Per Share (JPY)



Addressing diverse consumer needs by offering a broad choice

We believe that the options for adult consumers to choose the use of tobacco or nicotine products should not be restricted to any specific product category. Provided they understand the health risks associated with the use of such products, it is important that they remain free to choose the most appropriate proposition in response to their taste preferences, their living environment, their life stage or other factors. Therefore, we are committed to offering consumers a variety of choices addressing their individual needs.

Our concept is unchanged when it comes to Reduced-Risk Products (RRP) which have been gaining popularity in recent years, particularly in Europe, the USA and Japan.

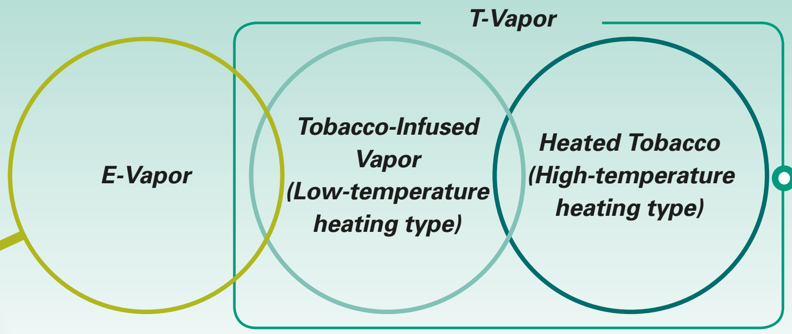
We are confident that through this approach, we will be able to deliver mid to high single-digit earnings growth over the medium- to long-term. RRP is one of the key pillars of our growth strategy in the tobacco business, and we will prioritize allocation of resources into the category.

Within RRP, we are focusing on three specific categories: E-Vapor (e-cigarettes), which does not use tobacco leaf but electronically heats liquid, and two T-Vapor technologies (Heated and Infused) which do not burn tobacco leaf, but rather offer consumers the enjoyment of an enriched tobacco vapor.

In each of these categories, we will continue to enhance our product pipeline and expand our product portfolio in line with the increasingly diverse needs of our consumers around the world.

"Logic" and "Ploom" are our flagship brands in the respective E-Vapor and T-Vapor categories.

We will maximize our presence in key markets and expand the reach of our product portfolio.



By the end of 2018, our E-Vapor products under the Logic brand were available in 11 markets, including the UK and the USA, and we recently launched a new pocket-sized, high performance device – Logic Compact – which provides high vapor and ultimate convenience to the modern, design-conscious vaper. Reactions from consumers and opinion leaders on product performance and vaping experience has been generally positive. Over the course of 2019, we will roll out Logic Compact in 13 additional geographical regions. We will thereby continue our focused geo-expansion approach, prioritizing the markets that matter the most. In E-Vapor, our strong growth will continue to accelerate, driven by new compelling products and effective execution in current and new markets.

Expanding the T-Vapor portfolio in Japan for global success in RRP

In Japan, we currently offer the broadest RRP portfolio with three T-Vapor options: Ploom TECH, Ploom TECH+ Tobacco-infused Vapor (low temperature heating) products, and Ploom S Heated Tobacco (high temperature heating). We will seek out opportunities to communicate directly with consumers in order to build awareness and recognition of how each product can satisfy their needs.

Outside Japan, we currently offer Ploom TECH in Canada, Switzerland and the USA*. In the near future, the international T-Vapor portfolio will be shaped by mining consumer insights and learnings in Japan.

* In the USA, Ploom TECH is sold by Logic Technology Development LLC, a member of the JT Group, under the name 'Logic Vapeleaf'.

Ploom TECH
- Less than 1% of the odor* and more than 99% reduction** in the levels of measured potentially harmful constituents compared to cigarette smoke
- Various flavors and clear taste of tobacco
- Easy to use and no maintenance

Ploom TECH+
- Less than 1% of the odor* and more than 99% reduction** in the levels of measured potentially harmful constituents compared to cigarette smoke
- Rich vapor with improved satisfaction
- Profound taste of tobacco

Ploom S
- Less than 5% of the odor* and more than 90% reduction** in the levels of measured potentially harmful constituents compared to cigarette smoke
- Superior taste and reduced odor
- A taste like the MEVIUS cigarettes

* Results of the research based on the three-point comparative odor intensity indication method by six people who have passed the olfactory test. Cigarette smoke and Ploom TECH, Ploom TECH+ and Ploom S tobacco vapor, which contains constituents derived from tobacco leaves, were diluted with odorless air in the bags, and the odor of each bag was statistically quantified as the "dilution factor of just no odor".

** It does not imply that the health risk associated with the use of the product is relatively small compared with that of cigarettes. It compares the amounts of nine constituents the WHO recommend to reduce as a priority, which are contained in one puff of cigarette smoke and one puff of a tobacco vapor of Ploom TECH, Ploom TECH+ and Ploom S. Standard test cigarette (3R4F) was selected as the test cigarette product.

Through M&A and organic growth, The JT Group has successfully become highly diverse and global

1985–1998

Expanding business scope and global scale

Japan Tobacco Inc. was established in 1985 upon the privatization of Japan Tobacco and Salt Public Corporation. In the next two years, the operating environment changed dramatically. Major events included the Plaza Accord of 1985 and the subsequent appreciation of the yen, the tobacco tax hike in 1986, the abolition of tariffs on imported cigarettes in 1987, and the subsequent offensive by foreign tobacco manufacturers.

To cope with the rapid deterioration of the operating environment, JT implemented measures to maintain domestic sales volume by strengthening its marketing capabilities and cost competitiveness, in addition to pursuing business diversification. This was the time when we laid the groundwork for the pharmaceutical and processed food businesses.

Since then, the total demand for tobacco in Japan has started to decline. Demand peaked in the latter half of the 1990s due to a contraction of the adult population and growing concerns with health problems associated with smoking. Amid the increasingly severe business environment, we implemented rationalization steps, selected and concentrated our diversified businesses, and expanded the international tobacco business in order to achieve sustainable growth.

- **Privatization of Japan Tobacco and Salt Public Corporation and establishment of Japan Tobacco Inc. (1985).**
- **Established the Business Development Division (1985) to aggressively develop new businesses. Subsequently, the division was reorganized to form the Pharmaceutical and Food Products Division (1990).**
- **Acquired Manchester Tobacco Company Ltd. (1992).**
- **Listed on stock exchanges in Tokyo, Osaka, Nagoya and elsewhere (1994).**
- **Acquired a majority of the outstanding shares of Torii Pharmaceutical Co., Ltd. through a tender offer (1998).**

1999–2006

Embarking on a path to growth

The international tobacco business had sales of only about 20 billion units in 1998, and its scale was limited. However, the acquisition of the non-U.S. tobacco business of RJR Nabisco Inc. in 1999 led to dramatic growth. Through this acquisition, our market expanded rapidly, with "Winston" and "Camel" joining our brand portfolio.

In the Japanese domestic tobacco business, we faced major changes, such as the termination of the Marlboro license contract, which lasted for approximately 30 years, but we worked to strengthen our business base through structural reforms.

- **Acquired non-U.S. tobacco business of RJR Nabisco Inc. (1999).**
- **Terminated license contract for the exclusive rights to produce and sell Marlboro brand products in Japan and use the Marlboro trademark in the country (2005).**

2007–2018

Driving profit growth with the international tobacco business

Since acquiring the non-U.S. tobacco business of RJR, the international tobacco business has continued to grow organically, increasing its share in each market. However, the acquisition of Gallaher (UK) in 2007 propelled the growth of the entire JT Group.

International tobacco business revenues increased significantly with the addition of important markets, such as Russia and the UK. In addition, our brand portfolio grew more robust and solid thanks to the inclusion of "LD", which is currently a GFB*, and local heritage brands with a long history in each market.

In Japan, we focused on the selection and concentration of our business other than tobacco, including the acquisition of Katokichi Co., Ltd. in 2008 and the withdrawal from our beverage business in 2015. In the Japanese domestic tobacco business, we decided to change the name of "Mild Seven", which has the No. 1 share in Japan, to "MEVIUS", and reinforce the brand. We also acquired the Natural American Spirit's non-U.S. business to further strengthen our business foundation.

In recent years, in addition to geographic expansion centering on Asia, we have been actively investing in the RRP growth category. In Japan, where RRP is growing, we expanded our sales of "Ploom TECH" nationwide in 2018. Going forward, we will continue to invest in the three key areas of our tobacco business** with the aim of achieving high levels of earnings growth.

- **Acquired all outstanding shares of Gallaher Group Plc (UK) (2007).**
- **Acquired issued shares of Katokichi Co., Ltd. (2008).**
- **Changed "Mild Seven" to "MEVIUS" (2013).**
- **Acquired Natural American Spirit's non-U.S. business (2016).**
- **Acquired operations in the Philippines, Indonesia, Russia, Bangladesh and elsewhere (2016-2018).**
- **Expanded nationwide sales of "Ploom TECH" (2018).**

* GFB: Winston, Camel, MEVIUS and LD are our Global Flagship Brands.
** Sustainable profit growth in existing markets by strengthening brand equity, geographic expansion in emerging markets, and acceleration of growth in the RRP category

Achieve the JT Group's mid- to long-term profit growth through business investment and enhance shareholder returns

Naohiro Minami
Representative Director and Executive Vice President

2018 Financial Results

Adjusted operating profit at constant FX, our KPI, grew 8.9% year-on-year to 637.2 billion yen. This is most notably due to pricing in the international tobacco business, despite the profit decline in the Japanese domestic tobacco business with decreasing JT cigarette sales volume and higher investment in sales promotions for RRP. Excluding a one-time loss related to a key UK distributor going into administration, adjusted operating profit at constant FX increased by approximately 5%.

On a reported basis, revenue and adjusted operating profit growth was 3.6% and 1.7% respectively, reflecting negative FX impact.

Operating profit increased by 0.7% to 565.0 billion yen due to an increase in intangible amortization related to acquisitions. Profit decreased by 1.7% to 385.7 billion yen impacted by an increase in financial expenses.

Free cash flow increased by 33.0 billion yen to 105.6 billion yen. An increase in proceeds from real estate sales and improvement in working capital more than offset an incremental cash payment caused by the acquisitions in Russia and Bangladesh and higher capital expenditure mainly related to RRP.

2019 Financial Outlook

Revenue will remain largely unchanged, as the increase in the Japanese domestic tobacco business and international tobacco business will be offset by the negative FX impact and the decrease in the pharmaceutical business. Adjusted operating profit is forecast to decline by 8.3% year-on-year.

Operating profit and profit are expected to decrease by 4.4% and 4.1% respectively. One-time compensation gain related to the termination of the exclusive license agreement for anti-HIV drugs in the pharmaceutical business will partially offset a decline of adjusted operating profit, a decline of gain from sale of real estate and an increase in intangible amortization arising from acquisitions.

Free cash flow is estimated at 360.0 billion yen. In 2019, we do not assume new acquisitions, compared with 2018. Additionally, we will strengthen JT's ability to generate free cash flow and improve working capital.

We target growing adjusted operating profit at constant FX by 2.4% year-on-year to 610.0 billion yen.

Shareholder Return Policy

We give the highest priority to business investment which contributes to sustainable profit growth in the mid- to long-term and seek a balance between profit growth through business investment and shareholder returns under our resource allocation policy. Our policy remains unchanged, aiming to deliver a stable and consistent growth in dividend per share based on the mid- to long-term profit growth outlook while maintaining a strong financial base. We will pay an annual dividend per share of 150 yen, as announced at the beginning of the year.

On the other hand, foreign exchange has been volatile in recent years as uncertainty for world economy has increased. The negative currency impact in 2018 was over 40.0 billion yen and is expected to be over 60.0 billion yen in 2019. The current situation is expected to continue for a certain period of time, and as we aim to achieve consistent dividend per share growth, we will decide future annual dividend per share based on the mid- to long-term growth rate for adjusted operating profit at constant FX, while also taking into account the outlook for net income from 2019. We plan to offer an annual dividend of 154 yen in 2019, representing a 4 yen increase. In order to mitigate FX impact, we are hedging naturally by matching the currency for income and expense. Establishing a local manufacturing base after considering the scale of business is a case in point. For the mid- to long-term, we are working on lowering the degree of dependence on a specific currency by geographically expanding our business. We fully consider the risk of FX movement when investing into emerging markets including through M&A. For markets with mid- to long-term growth potential, we will firmly capitalize on economic growth and aim for profit growth.

As for 2019, we approved a share buy-back of up to 50.0 billion yen or 23.0 million shares over the period from February 8 to April 22 as part of our shareholder return. We have considered our FCF outlook, balance sheet and other typical elements as well as various factors including one-off cash proceeds in the pharmaceutical business and our share price movement.

We aim to deliver a stable and consistent increase in dividend based on the mid- to long-term outlook for profit growth, while growing profit through aggressive business investment.

Business Plan 2019 on p. 20

The Japan Tobacco Group's Activities

2018

March 15
Signed exclusive license agreement with ROHTO Pharmaceutical for the development and commercialization of JAK inhibitor in Japan

May 21
Announced achievement of greenhouse gas emission reduction target three years ahead of schedule, a 20% reduction in 2017 compared with 2009

June 5
Held an investor conference in London 1

July 2
Completed national roll out of the Ploom TECH starter kit and tobacco capsules in convenience stores

August 1
Completed the acquisition of Donskoy Tabak in Russia 2

August
Launched Logic Compact, the new premium E-Vapor product in the UK 3

September
JT has been selected as a member of the Dow Jones Sustainability Asia/Pacific Index for the fifth consecutive year

November 29
Completed the acquisition of tobacco business* of Akij Group in Bangladesh 4

* Acquired the shares of United Dhaka Tobacco Company Limited (UDTC), the entity taking over the tobacco business assets of Akij, as well as all tobacco related trademarks and design rights from Akij.

December 3
Launched the new white Ploom TECH starter kit and two new tobacco capsule flavors in Japan 5

Investor Relations Activities

We are pursuing the fair and broad disclosure of financial information such as operating results and non-financial information including management strategies, ESG information and the status of each business through direct communication with shareholders and institutional investors.

Our dedicated IR team based in Tokyo and Geneva hold daily dialogues with analysts and institutional investors. The following is an overview of our major IR activities in 2018.

The number of IR interviews with analysts and institutional investors in 2018 700 Approx.

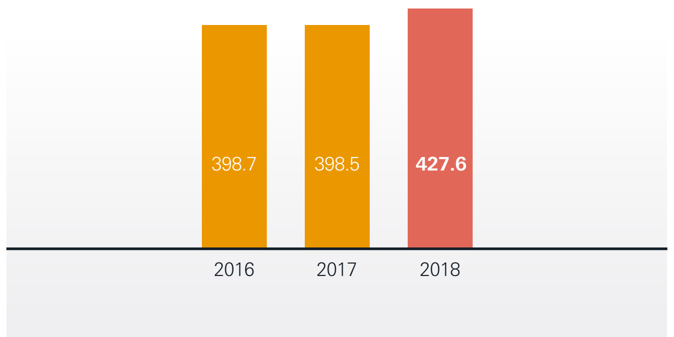
Activities	Results	Details
Report to the Board of Directors	2	We report our IR activities to the Board of Directors twice a year. In addition, we edit an internal report of IR-related activities and submit this monthly report to the management.
IR meeting for quarterly financial results	4	We hold telephone conferences for the first, second and third quarter. In addition, we organize an IR meeting for the full year results. The speakers are the president, chief financial officer and other executives.
Business conference for analysts and institutional investors	2	In June 2018, we held an investor conference in London to discuss the Group's mid- to long-term business strategy, our global tobacco growth strategy focused on M&A, and RRP business strategy. The conference attracted approximately 110 visitors and webcast viewers. In addition, as a follow-up to the London Investor Conference, we held small meetings for analysts and institutional investors in Japan.
IR interview	Approx. 700	We have IR interviews and teleconferences for analysts and institutional investors.
IR road show overseas	5	The president, executive vice president or senior vice president visits shareholders and institutional investors in major cities in North America, Europe and Asia.
IR conferences in Japan and overseas	12	We participate in conferences sponsored by securities companies and senior vice presidents or IR team members meet analysts and institutional investors both in Japan and overseas.
IR meeting for individual investors	4	An executive vice president or senior vice president visits major cities in Japan to speak at IR meetings for individual investors.

Results for the fiscal year ended December 31, 2018

In our Business Plan 2019, a target is set for adjusted operating profit growth rate at constant exchange rates. While it is a mid- to long-term target, we also monitor performance measures annually.

Tobacco Sales Volume

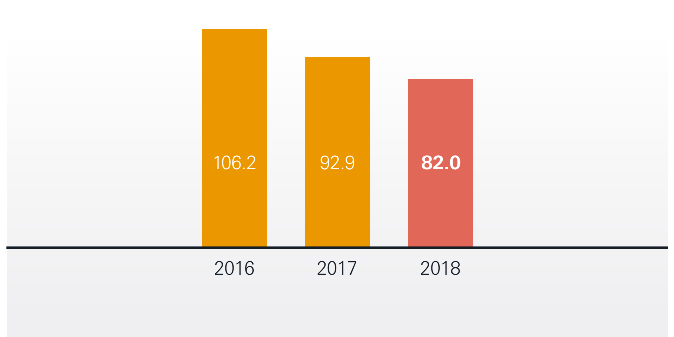
International Tobacco (BnU)



+7.3% to 427.6 BnU

For the international tobacco business, total shipment volume includes fine cut, cigars, pipe tobacco, snus and kretek, but excludes contract manufactured products, waterpipe tobacco products and Reduced-Risk Products.

Japanese Domestic Tobacco (BnU)



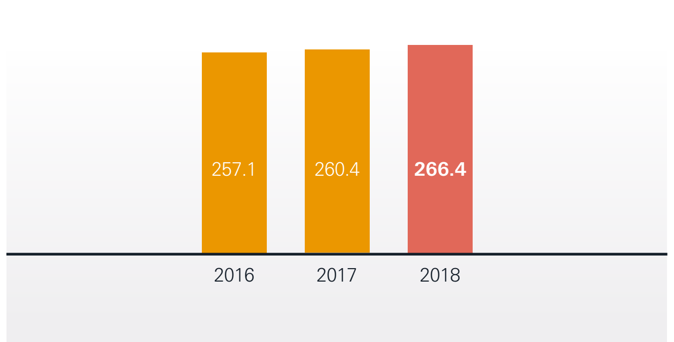
-11.7%

82.0 BnU

For the Japanese domestic tobacco business, total cigarette sales volume excludes sales volume of Japanese domestic duty free, the China business and Reduced-Risk Products.

GFB Shipment Volume

GFB Shipment Volume (BnU)

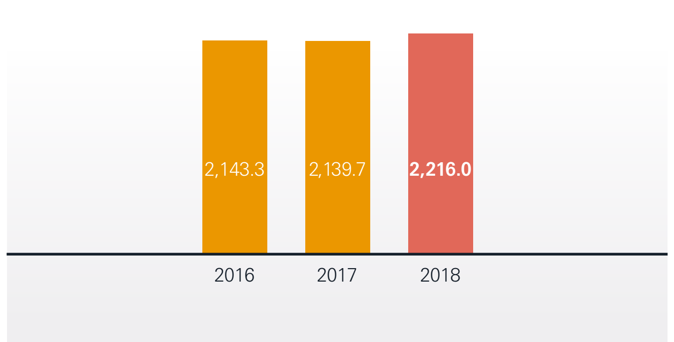


+2.3 % to 266.4 BnU

Shipment volume of GFBs, namely Winston, Camel, MEVIUS and LD in the international tobacco business.

Consolidated Revenue

Revenue (JPY BN)



+3.6% to JPY

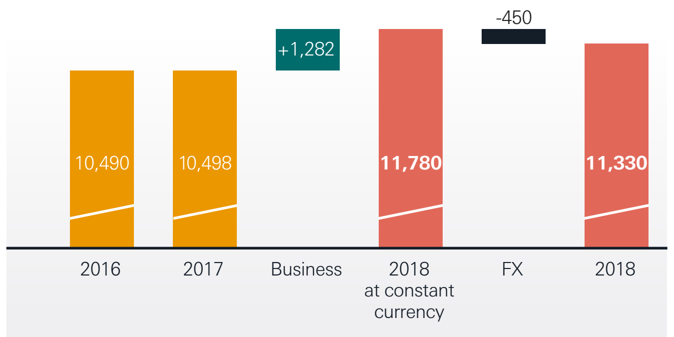
2,216.0 BN

Revenue on a consolidated basis which, for the avoidance of doubt, excludes excise and other similar taxes, as well as sales from transactions in which the JT Group acts as an agent.

In our strategic framework to achieve adjusted operating profit growth, the JT Group places a particular emphasis on "quality top-line growth", while, at the same time, focusing on building a "competitive cost base" and "robust business foundation". In line with our strategic emphasis, the measures to review our business performance are skewed towards top-line related indicators. As for shareholder return, we will deliver a sustainable and steady increase in dividend per share.

Core Revenue

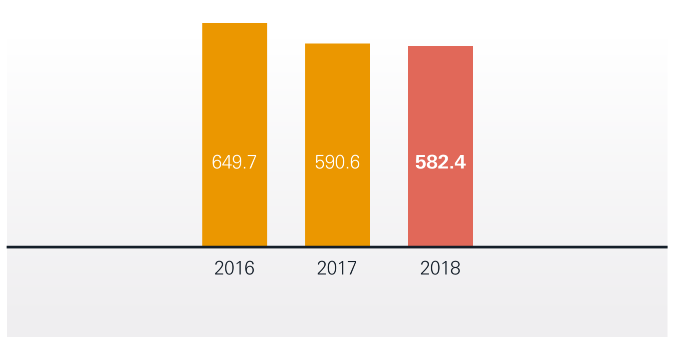
International Tobacco (USD MM)



+12.2 % at constant exchange rates to USD11,780 MM

For the international tobacco business, US dollar-based core revenue includes revenue from waterpipe tobacco products and Reduced-Risk Products, but excludes revenues from distribution, contract manufacturing and other peripheral businesses.

Japanese Domestic Tobacco (JPY BN)

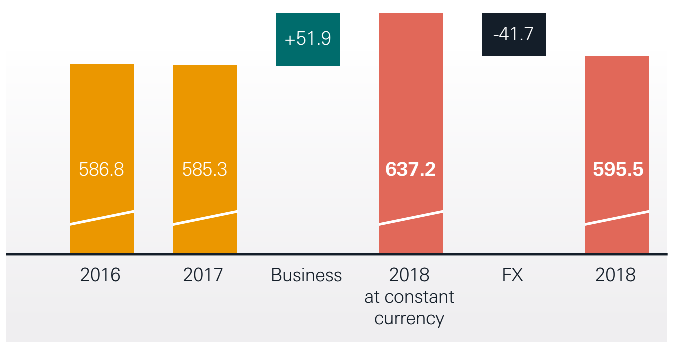


-1.4 % to JPY 582.4 BN

For the Japanese domestic tobacco business, core revenue excludes revenue from distribution of imported tobacco in Japan, among others, and includes revenue from domestic duty free, the China business and Reduced-Risk Products such as Ploom TECH devices and capsules.

Consolidated Adjusted Operating Profit

Adjusted Operating Profit (JPY BN)



+8.9 % at constant exchange rates to JPY 637.2 BN

+1.7% including currency impact to JPY

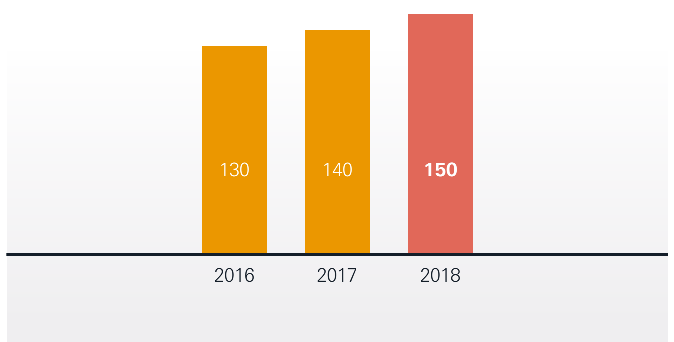
595.5 BN

Adjusted operating profit is calculated as follows: Adjusted operating profit = Operating profit + amortization cost of acquired intangibles arising from business acquisitions + adjusted items (income and costs)*

* Adjusted items (income and costs) are impairment losses on goodwill, restructuring related income and costs and others.

Dividend Per Share

Dividend Per Share (JPY)



+10 yen to

150 yen

The sum of interim and year-end dividends per share, the record dates of which fall in the relevant fiscal year.

Please be reminded that this section is intended to explain the business operations of JT to investors, but not to promote sales of tobacco products or encourage smoking by consumers.

Tobacco Business

Tobacco Industry

Market Dynamics

There are many types of tobacco products available in today's marketplace. Cigarettes remain the most popular choice for consumers, while fine cut, cigars, pipe tobacco, snuff, chewing tobacco, waterpipe tobacco and kretek continue to draw consumers' interest, with some of these product categories increasing their volumes worldwide.

In addition, Reduced-Risk Products (RRP)* have become widely popular. In particular the market size of 'E-Vapor' products has been expanding at a fast rate notably in the USA and Europe. The products use vaporized liquid solutions often containing nicotine, and vapor is inhaled to offer a different experience. As E-Vapor products do not use tobacco leaf, they are usually not regulated or taxed as tobacco products, however, regulation or taxation of E-Vapor products vary across markets.

Another type of RRP referred to as 'T-Vapor' or 'Tobacco Vapor' has been growing particularly in Japan. Unlike E-Vapor, T-Vapor products use tobacco leaf and are therefore taxed and regulated as tobacco products in principle. We expect further innovation and product offerings will drive growth in the T-Vapor category, as market players take keen interest in this new growing market.

Approximately 5.4 trillion cigarettes are consumed around the world, reaching global sales of approximately US$700 billion. China is by far the largest market, accounting for over 40% of global consumption, but it is almost exclusively operated by a state monopoly. Indonesia, Russia, the USA and Japan are the next four largest markets, according to a survey conducted in 2018.**

In general, the market dynamics of cigarettes are distinctively different between mature and emerging markets. In mature markets, industry volume tends to decline reflecting various factors such as limited economic growth, tax increases, tightening regulations, and demographic changes, among others. In addition, down-trading is prevalent in these markets. Consumers are inclined to seek more value as they feel tobacco products become less affordable in the context of limited growth of disposable income.

In emerging markets, on the other hand, total consumption tends to increase, driven by population growth and economic development, particularly many countries in Asia, the Middle East and Africa. As their disposable income increases, consumers look for quality and trade up to products in a higher price range.

Overall, global cigarette industry volume has been slightly decreasing in 2018. However, more importantly, industry value continues to grow even in the current difficult operating environment, mainly driven by price increases. This is a sign of the resilience of the industry. These trends – decline in volume and increase in value – are expected to continue in the years ahead. In addition, the RRP category value continues to grow and its market size is expected to grow from US$16 billion in 2018 to US$29 billion in 2021.**

* Reduced-Risk Products (RRP): Products with the potential to reduce the risks associated with smoking.
** Source: JT estimate (2018 data).

"Reduced-Risk Products* have been expanding at a fast rate in markets such as the USA, Europe and Japan, with global sales reaching approximately US$16 billion."

Top market players

	Share of market (%)				
	2014	2015	2016	2017	2018
Philip Morris International Inc.	24.6	25.0	24.7	24.7	24.6
British American Tobacco Plc.	18.4	18.8	19.1	23.0	24.4
Japan Tobacco Inc.	15.3	15.2	15.5	15.5	15.8
Imperial Brands Plc.	6.7	6.6	6.3	6.4	6.1

Source: JT estimate (2018 data).
Excluding China National Tobacco Corp (CNTC).

Top 10 countries by cigarette volume

	BnU				
Country	2014	2015	2016	2017	2018
China	2,549.5	2,489.5	2,350.5	2,343.9	2,368.8
Indonesia	314.3	320.4	316.1	308.2	307.1
USA	270.6	269.9	262.5	252.6	240.9
Russia	316.2	292.5	278.9	258.8	236.5
Japan	186.2	182.3	173.9	151.5	132.7
Turkey	94.7	103.2	105.5	106.2	118.5
Egypt	83.2	86.4	90.0	93.1	96.3
Bangladesh	80.6	83.4	86.1	88.9	91.6
India	95.9	88.1	84.9	81.3	82.5
Vietnam	70.4	73.9	76.3	77.0	80.9

Source: JT estimate (2018 data).

Regulations

The regulatory environment continues to be more restrictive for the tobacco industry. Restrictions on promotions and advertisements are the most common around the world. An increasing number of markets are introducing bans on smoking in public places and promoting larger health warnings on product packaging, in some cases with pictorial health warnings. There are also some markets where displaying tobacco products at retail stores is banned.

Recent regulations are focusing more on the product itself. Plain packaging, or a branding ban, has been introduced in some markets and furthermore, regulators are becoming more aggressive by restricting ingredients and emissions, following the guidelines on these attributes proposed by the Framework Convention on Tobacco Control.

In Europe, all member states have already implemented the new Tobacco Products Directive from 2017, which adopted extended health warnings, minimum packaging requirements or restrictions on the use of additives, among others. EU Member States have started implementing these restrictions. These moves to commoditize tobacco products will undermine fair competition among tobacco manufacturers trying to meet increasingly diverse consumer preferences. Worse, they could result in an undesired increase in illicit trade, as commoditized products with less uniqueness are easier to counterfeit and more difficult to detect when smuggled.

Recently new standards or frameworks for reduced risk claims have been established in a few countries such as the USA and parts of Europe. In order to gain official approval from governments, activities in developing reduced risk claims have been intensified among major global tobacco manufacturers.

Taxation

Tobacco products are subject to excise or similar taxes in addition to value-added tax in most countries as governments seek to secure their revenue or promote public health. Excise taxes were raised in various markets during the past year, including for RRP*, and in general, tax increases are passed onto prices. Therefore, repeated tax increases in a short period of time, or steep tax increases, could lead to a decline in industry volume. Often, tax increases coincide with an increase in illicit trade, which could in turn affect our business.

Competition

Excluding China, two-thirds of world industry volume is produced by four major global tobacco companies, namely Philip Morris International Inc., British American Tobacco Plc., Japan Tobacco Inc. and Imperial Brands Plc.** The competition within the industry is intense and, as consumers' needs and preferences continue to diversify, a strong portfolio with established brands is increasingly important to support market share gains. Therefore, major global companies are focusing on brand equity enhancement to strengthen their brand portfolio by introducing innovative products. Competition in the RRP category has been intensifying as recently the products have subsequently been launched in many markets.

In addition to the pursuit of organic growth, M&A is an effective way to supplement growth opportunities in this industry.

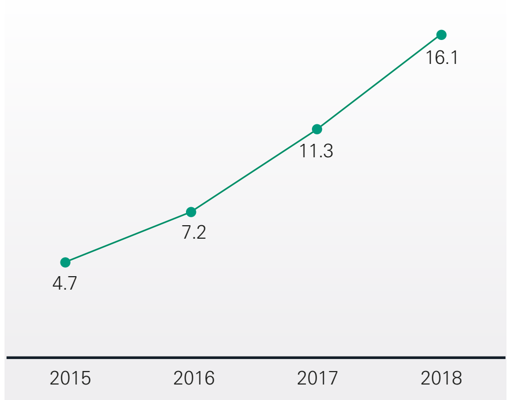
* Reduced-Risk Products (RRP): Products with the potential to reduce the risks associated with smoking.
** Source: JT estimate (2017 data).

Top brands

Brand	We Own	2013	2014	2015	2016	BnU 2017
Marlboro		395.9	391.4	392.5	384.0	365.4
Winston*	✓	140.8	132.6	135.0	141.5	146.7
Pall Mall		105.7	110.1	109.3	108.2	118.3
L&M		98.6	98.7	103.2	102.4	97.1
Camel*	✓	62.7	66.8	71.0	71.5	71.1
Rothmans		25.8	34.8	50.5	69.2	77.5
Cleopatra		53.7	56.2	59.3	65.9	68.7
MEVIUS	✓	83.7	79.1	77.3	76.2	68.6

Source: JT estimate (2017 data).
Excluding China National Tobacco Corp (CNTC).
* Winston and Camel are also owned, respectively, by Imperial Brands Plc. and Reynolds American Inc. in the USA.

RRP Category Value (USD BN)



Source: JT estimate (2018 data)

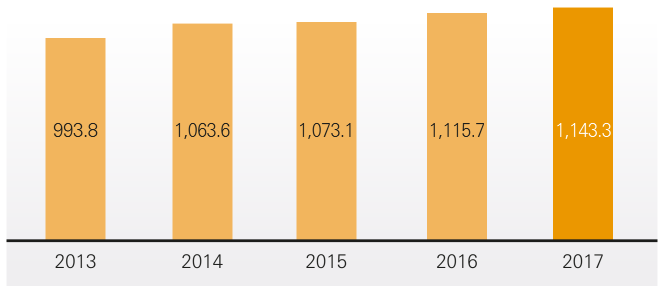
Pharmaceutical Business

Market Dynamics

The global pharmaceutical market continues to grow, reaching sales of approximately US$1,143.3 billion in 2017, an increase of 2.5% year-on-year.* Developed countries take the lead, with North America accounting for approximately 43%* of the global pharmaceutical market, the largest share. In emerging countries, demand for advanced medicine is also rapidly growing due to multiple factors including increasing health awareness, population growth, and development of public healthcare systems. Facing a rapidly aging society and fiscal deficits, however, governments often try to control drug prices and hold back medical costs.

In Japan, the main market for our pharmaceutical business, the majority of net sales comes from originator drugs. Compared with the USA and Europe, the market share in Japan for generic drugs is still small. However, the market has been expanding, in part due to government promotion of generic drugs in order to control medical care expenses. Drastic reform of the drug pricing system will create challenging circumstances due to annual drug price revision, constraints on the scope of price maintenance premium drugs, price reduction of long-listed drugs according to replacement rate, and similar factors. In April 2018, the latest round of price revisions led to an industry-wide reduction of drug prices by 7.48% on average.

Worldwide Pharmaceutical Market* (USD BN)

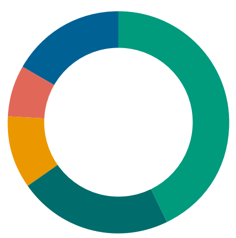


Competition

Global competition to create innovative drugs is becoming progressively more difficult because searching for new drug targets has become harder while regulatory standards for new drug approvals have become stricter.

We are building an R&D-led business to create internationally competent original compounds. Therefore, we are competing with not only Japanese domestic makers but also numerous foreign companies including global mega pharma and start-up companies.

2017 Regional Composition*



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Processed Food Business

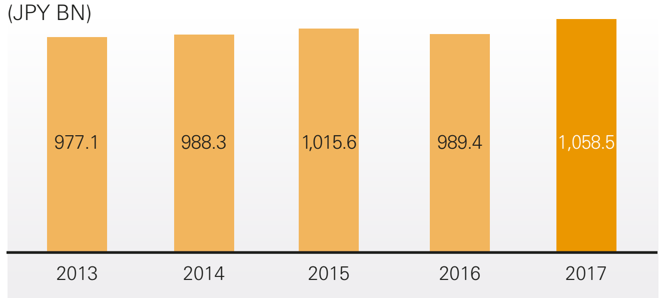
Market Dynamics

Annual consumption of frozen food in Japan increased 4.7% in 2017 to 2,855,330 tons, a record high. Domestic market size, on a consumption basis including imports, grew 7.0% year-on-year to 1,058.5 billion yen,* exceeding one trillion yen for the first time since 2015. Domestic production of frozen food in 2017 increased 3.0% from the previous year to 1,600,968 tons, a record high for the second consecutive year. Production value also grew, increasing by 4.5% to 718.0 billion yen.

We expect continuous growth for the Japanese processed food industry given the increasing number of one-person households and rising gender equality for women. Offering abundant variety, frozen foods can help meet the sophisticated needs of today's consumers as technology can now maintain fresh taste beyond defrosting.

At the same time, we believe it is necessary to monitor trends in sales channels amid the expansion of private brand products by some distribution companies and the reorganization of wholesale entities. The risk of price fluctuations in raw materials still exists due to global food shortages.

The Japanese Frozen Food Market on a Consumption Basis* (JPY BN)



* Source: Japan Frozen Food Association

Competition

TableMark is competing against major players like Maruha Nichiro, Nichirei, Ajinomoto and Nissui as well as a multitude of mid- or small-scale producers. However, the industry players are slowly specializing according to each company's product categories.

In recent years, some companies have moved to reorganize production bases with the aim of optimization, as well as dealing with aging facilities and labor shortages. The development of value-added and new-value products has also resulted in the creation and expansion of some new markets.

International Tobacco Business

Results for the fiscal year ended December 31, 2018

2018 performance was outstanding. Total shipment volume growth exceeded 7%, benefitting from acquisitions and organic share progression in both mature and emerging markets. This volume increase was complemented by significant pricing gains, which were realized by leveraging the unparalleled equity of our Global Flagship Brands.

We continued to deploy investments in a focused and disciplined manner, strengthening our competitiveness across selected markets and categories. While the expansion efforts in Reduced-Risk Products accelerated, as demonstrated by the successful launch of Logic Compact, conventional products remained the core driver of our top- and bottom-line growth.

2019 is set to be another successful year for the international tobacco business. Total volume is expected to outperform the industry, supported by the acquisitions in Russia and Bangladesh as well as by our Global Flagship Brands expanding further their consumer franchise. The pricing environment remains robust, providing opportunities for sustainable improvements. In this context, core revenue and adjusted operating profit are projected to continue growing at a sustained pace.

The international tobacco business entered 2019 with strong business fundamentals and positive momentum. This gives me great confidence in our ability to continue growing through strategic investments in our people, brands and capabilities.

Eddy Pirard

Chief Executive Officer, JT International S.A.

Key Highlights

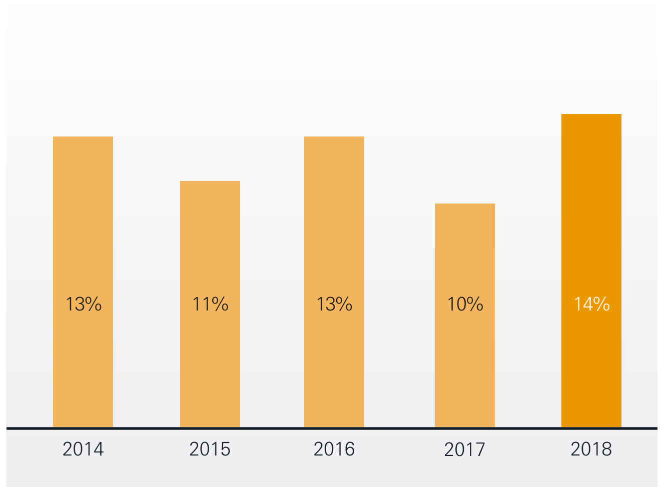
Total Shipment Volume (BnU)
427.6
+7.3%
Year-on-Year Change

GFB Shipment Volume (BnU)
266.4
+2.3%
Year-on-Year Change

Core Revenue (USD MM)
11,330
+7.9%
Year-on-Year Change

Adjusted Operating Profit (USD MM)
3,493
+11.3%
Year-on-Year Change

Adjusted Operating Profit (AOP): YoY Growth at Constant FX*



* Excluding 2017 one-time loss

Roadmap to Sustainable Growth

The international tobacco business remains focused on prioritizing investments in conventional products in markets that matter, strengthening its competitiveness in Reduced-Risk Products as well as empowering and developing its talented people.

In 2018, the international tobacco business recorded outstanding results, demonstrating once again the robustness of its investment strategy. Total shipment volume exceeded 400 billion sticks for the first time since 2013, driven by recent acquisitions. Organic performance was resilient, with Global Flagship Brands driving share gains in many geographies. Currency-neutral core revenue and adjusted operating profit were above guidance, increasing by double-digits.

The 2017 acquisitions in the Philippines, Indonesia and Ethiopia, combined with the more recent ones in Russia and Bangladesh, paved the way for new growth opportunities while contributing strongly to our top- and bottom-line performance in conventional products.

In Reduced-Risk Products, our presence and portfolio steadily expanded, notably in the E-Vapor category. The successful launch of Logic Compact in the UK is testament to our consumer-centric investments in product developments and commercial initiatives. Additional launches are underway, like recently in Canada, Romania and Russia.

Our talented employees are the cornerstone of the international tobacco business exceptional growth track record. For the fifth consecutive year, the organization was awarded Global Top Employer, with an unprecedented 58 offices in 53 countries certified in 2019. This successfully demonstrates our efforts to attract, retain, develop and reward talents across the value chain.

By consistently pursuing our strategic priorities, our brands will further expand their consumer franchise in both conventional products and Reduced-Risk Products. With its consumer-centric approach, the international tobacco business is strongly placed to continue growing sustainably in 2019 and beyond.

2018 Performance Review

Volume & Share

Total shipment volume increased 7.3% to 427.6 billion cigarette equivalent units. This outstanding growth was fueled by the acquisitions in the Philippines, Indonesia and Ethiopia, as well as the early benefits of Donskoy Tabak in Russia and UDTC in Bangladesh.

Organically, shipment volumes were strong and ahead of the industry trend in several geographies. Excluding acquisitions, total shipment volume declined only 1.1%, outperforming an overall industry contraction estimated at 3.3% across our top 30 markets.

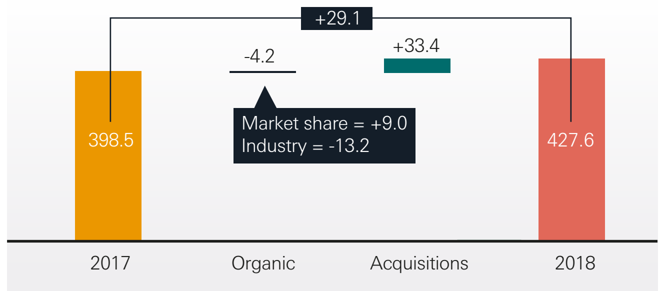
The international tobacco business grew volume in 63 markets, including Brazil, Germany, Iran, Italy, Jordan, Poland, Spain, Thailand and Turkey. This positive performance was driven by our continued market share progression, with gains in 22 of our top 30 markets.

Global Flagship Brands were paramount to our robust organic performance. GFB shipment volume grew for the fourth consecutive year, up 2.3% to 266.4 billion cigarette equivalent units, driven by share increases in both established and emerging markets. 64 markets reported GFB volume gains in 2018, of which 31 recorded double-digit growth, including Brazil, the Czech Republic, Jordan, Poland, Thailand and Turkey.

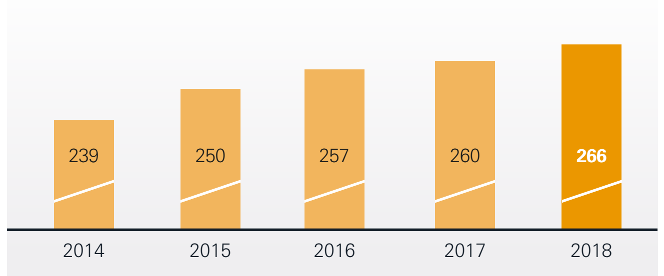
The continued progression of our Global Flagship Brands was driven by Winston, Camel and LD, which more than compensated for the decline of MEVIUS, mainly attributable to the severe industry contraction in Taiwan. Of particular note was the performance of Winston, which grew volume by 6 billion units, setting a record high of about 150 billion units. Camel and LD also performed strongly with Camel delivering its fifth consecutive year of volume growth, while LD regained momentum driven by the positive results in Jordan and Russia.

Across our top 30 markets, the international tobacco business' share of market and share of value achieved respectively 28.1% and 24.9%, growing 1.1 and 0.8 percentage points versus prior year. Over the same period, GFB share of market and share of value reached respectively 18.4% and 14.4%, an increase of 0.7 and 0.4 percentage points.

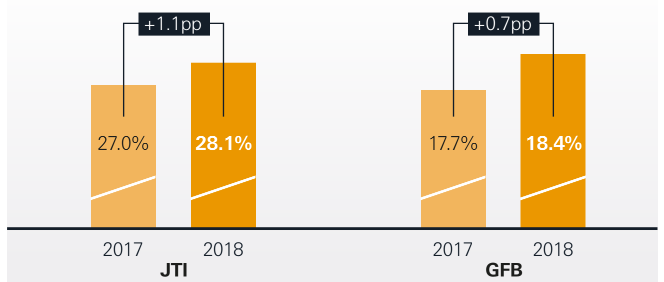
JTI Shipment Volume (BnU)



GFB Shipment Volume (BnU)



Market Share (top 30 markets)



Please be reminded that this section is intended to explain the business operations of JT to investors, but not to promote sales of tobacco products or encourage smoking by consumers.

Financials

Core revenue performance was strong, with a currency-neutral year-on-year increase of 12.2% fueled by positive price/mix and volume growth. The overall pricing environment improved in 2018, particularly in the key markets of Russia and the UK.

Our positive price/mix variance reached US$963 million, supported by significant contributions from all regional clusters except South & West Europe, due to France. Excluding France, South & West Europe generated a positive price/mix contribution, reflecting gains in several markets, including Italy and Spain.

Excluding the impact of a one-time loss in the previous year, currency-neutral adjusted operating profit increased 14.3%, driven by strong top-line performance. Importantly, this double-digit profit growth was achieved while continuing to deploy substantial business investments, notably behind Reduced-Risk Products.

In our two European clusters, combined currency-neutral adjusted operating profit grew 15.8%, despite the competition-led tax absorption in France. CIS+ and Rest-of-the-World adjusted operating profit increased 26.8% and 23.4%, respectively, driven by pricing and the contribution from acquisitions.

2018 Key Highlights

Investments That Matter

In 2018, investments in both established and emerging markets continued to strengthen the business fundamentals and competitiveness of our conventional products. Investments primarily focused on optimizing the GFB equity and portfolio, as well as strengthening distribution networks and trade partnerships.

In the key markets of Russia and the UK, top-line growth returned, driven by the increased competitiveness of our brands. In emerging markets, such as Iran and the Philippines, focused investments drove strong volume growth and market share gains.

In addition to efforts in conventional products, substantial investments continued to be deployed behind Reduced-Risk Products. Our leading positions in the European closed tanks category consolidated, driven by Logic Pro as well as the introduction of Logic Compact in the UK, where the product received very positive feedback from consumers and trade partners. Throughout the year, our E-Vapor propositions were introduced in three new markets, expanding our global RRP presence to 12 countries outside Japan by the end of 2018.

Overall, our focused investment strategy provided a more balanced and competitive business base in the international tobacco business, which will be paramount to fuel sustainable growth in 2019 and beyond.

Expanding the Business Footprint

To complement our organic growth, two acquisitions broadened our business footprint.

In August 2018, the acquisition of Donskoy Tabak (DT) in Russia was completed. The Greek manufacturer SEKAP, owned by DT, was also part of the transaction. With the addition of DT, overall volume share in Russia increased to approximately 40% and bolstered our leading position in the world's fourth largest cigarette market.

In November 2018, the acquisition of UDTC in Bangladesh was also completed. As a result, our overall volume share grew to about 20%, representing a strong number two position in the eighth largest cigarette market globally.

Consistent with our strategy, these investments accelerate our expansion in markets that matter for conventional products.

2019 Outlook

2019 is forecast to deliver continued and sustainable growth by building on the strong business fundamentals and positive momentum from the previous year.

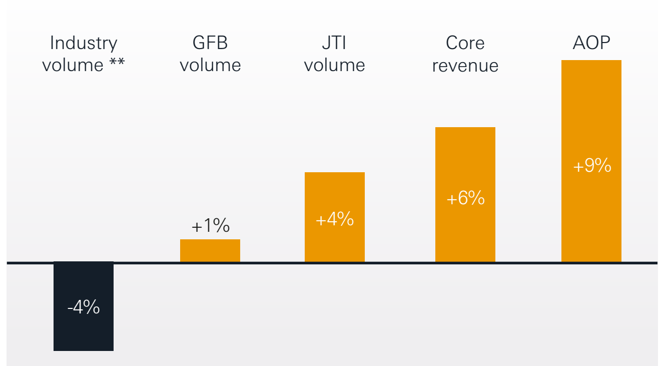
The most recent acquisitions in Russia and Bangladesh will be important growth drivers in 2019 and beyond, generating tailwinds in terms of volume, core revenue and adjusted operating profit at constant currency.

Total shipment volume is assumed to increase by about 4%, benefitting from acquisitions. On an organic basis, the continued GFB volume growth is expected to outperform the industry decline estimated at 4% across our top 30 markets.

With approximately two-thirds of the 2019 planned pricing already secured, robust core revenue and adjusted operating profit growth, at constant currency, are expected once again.

Importantly, this strong financial performance will be achieved while expanding our Reduced-Risk Products' presence with Logic Compact and while further investing in our people, brands and capabilities. In parallel, strategic assessments and initiatives across our value chain will continue to enhance our business agility.

2019 Guidance*



* 2019 variance vs. prior year. Core revenue and AOP at constant currency.
** Based on JTI's top 30 markets (RMC + Fine cut).

Global Flagship Brands

Among the world's most iconic and best-known tobacco brands, our four GFBs are at the core of our portfolio and investment strategy.

Global sales

149.9 BnU

Winston

Winston is our leading brand. Launched in 1954, Winston became the world's second biggest cigarette brand as of 2007. Winston is now present in more than 130 markets following the 2018 launches in Colombia, Guatemala and Libya.

In 2018, Winston's volume grew 3.9% to about 150 billion cigarette equivalent units, with 28 markets selling more than 1 billion cigarette equivalent units. Its strong performance was driven by a comprehensive portfolio architecture comprised of two sub-families – Core and XS.

Winston Core, of which the lead styles are Winston Blue and Red, is Winston's global bestseller. The XS family, which grew volume by more than 15% in 2018, is a more progressive range with a refined taste signature and features such as the LSS technology (Less Smoke Smell). Its growth was driven by the Compact line extensions and the success of its Flavor-on-Demand propositions in many markets, including Russia.

Winston grew share in 37 markets, achieving records in 29 of them, including Iran, the Philippines, Russia and Spain. As a result, Winston further strengthened its market share across our top 30 markets, growing 0.4 percentage points to 10.9%.

Global sales

54.2 BnU

Camel

Camel has been the world's most inspiring tobacco brand since 1913, a global icon of creativity with over 100 years of tobacco experience. With its distinctive taste signature, Camel is sold today in 110 markets following three new launches in 2018: Egypt, Nicaragua and Vietnam. In 13 of these markets, Camel's annual shipment volumes exceeded 1 billion cigarette equivalent units.

In 2018, Camel grew volume and share for the fifth consecutive year. The brand exceeded 54 billion cigarette equivalent units, increasing by 2.8% versus 2017, led by double-digit volume growth in 27 markets. This positive volume performance was driven by the strong contribution of the Czech Republic, Spain, Thailand, Tunisia and Turkey.

Last year, Camel continued to build relevance among adult smokers with new propositions, such as Camel Caster in Vietnam. This initiative enabled the brand to provide better consumer choice in one of the largest Asian markets. Camel also increased its presence in the Compact category, offering the format in 15 markets, better catering to evolving preferences of consumers.

Camel achieved record high market share in 20 geographies in 2018, with solid growth momentum not only in its European strongholds (Belgium, the Czech Republic, France, the Netherlands and Spain), but also in many emerging markets, such as the Philippines and South Africa. As a result, Camel exited 2018 with a 3.9% share in our top 30 markets, up 0.2 percentage points versus prior year.

LD

Global sales

46.6 BnU

LD

LD is one of the top best-selling tobacco brands in the world and a key value proposition globally. LD is now present in more than 50 countries following the 2018 launches in Bolivia, Egypt, Morocco, Norway and Uzbekistan.

In the highly competitive value segment, LD delivered 47 billion cigarette equivalent units in 2018, an increase of 2.2% versus 2017. Main contributors to volume increase were Jordan, Malaysia, Russia, Taiwan and the USA. Modern propositions such as Flavor-on-Demand and Compact, grew by double digits, mostly in Eastern Europe.

The brand achieved its highest ever share in 13 markets, including Canada, Russia, Singapore and Taiwan. In Taiwan, despite the industry contraction, LD reached a record share of market of 5.5% in the fourth quarter of 2018, up three percentage points versus prior year. Overall, LD reached a 3.0% market share in our top 30 markets, up 0.3 percentage points versus 2017.

Global sales

15.7 BnU

MEVIUS

Launched as Mild Seven in 1977 and rebranded in 2013, MEVIUS is the top-selling brand in Japan with over 30% market share. Internationally, MEVIUS enjoys consumer popularity in several Asian markets, as demonstrated by the record market share achieved in 2018 in Cambodia, Myanmar and Singapore.

For the full year of 2018, MEVIUS' volume decreased by 11.7%, mainly due to industry volume contraction in Taiwan and South Korea, driven by an excise tax increase and RRP category growth, respectively. Excluding such geographies, MEVIUS recorded double-digit volume growth in several markets, such as Cambodia and Myanmar.

The brand continued to grow its share of the premium segment in its top Asian markets. In Taiwan, MEVIUS remained the number one brand with a share of market of 18.4%, strengthening its leadership in premium by reaching a 62% share of segment.

Reduced-Risk Products

The Reduced-Risk Products category continued to grow over the course of 2018. The number of vaping consumers rose from 29 million in 2017 to approximately 50 million at the end of 2018, with an estimated Retail Sales Value net of taxes of around US$16 billion for the overall category.

2018 was another important business-building year with our steady expansion in the E-Vapor category. By the end of 2018, the Logic portfolio was available in 11 markets, which together represent approximately 75% of the global RRP category retail value. Our deliberate, focused approach to geo-expansion, prioritizing high-potential markets, will continue in 2019 with new market launches.

In 2018, Logic Compact, our new pocket-sized, high-performance device that provides high vapor volume and ultimate convenience for the modern, design-conscious vaper, was introduced in the UK. Logic Compact comes in a range of different colors and flavors and its presence was recently expanded to Belgium, Canada, Greece, Ireland, Italy, Romania and Russia. Further market introductions of Logic Compact will take place throughout the course of 2019.

In the T-Vapor category, we continued gathering consumer insights with Ploom TECH in Canada, Switzerland and the USA. Our T-Vapor portfolio for the international tobacco business will be shaped by mining the insights gathered in these pilot markets and leveraging the important learnings from Ploom TECH+ and Ploom S in Japan.

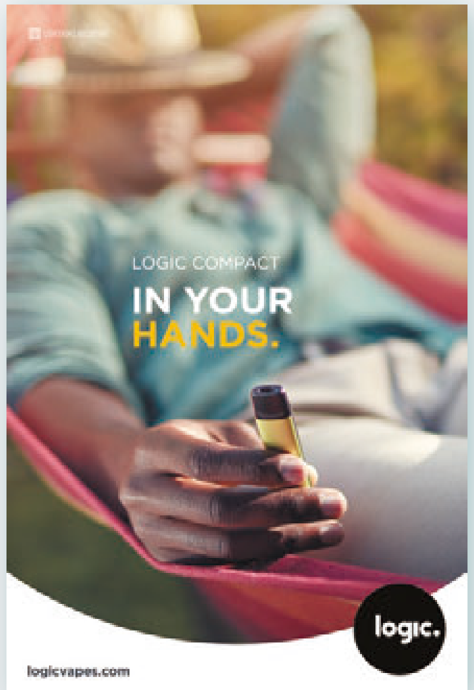
Significant efforts are being deployed and new capabilities are being built to deeply understand what will drive consumer preference in Reduced-Risk Products. Beyond just looking at a satisfying tobacco experience that has the potential to reduce risk, consumers are also driven by other important factors, such as external needs or the convenience of vaping in more situations, while others are conscious of social considerations, such as products with no smoke smell. In certain markets, affordability and taste satisfaction primarily influence purchasing behavior. Since consumers are the ultimate catalysts for innovation, their needs will continue to be at the heart of our product development and commercialization efforts.

To handle product expansion in E-Vapor and T-Vapor, our robust supply chain centered in both China and Japan, was supplemented by the opening in 2018 of in-house production facilities to manufacture liquids from our European Flavor House in Gostkow, Poland.

2019 and upcoming years will continue to see relentless efforts to develop new products with the potential to exceed consumer expectations while reducing the risks associated with smoking. These developments will raise our future competitiveness and expand our portfolio, which combined with secured capacity to meet demand, will drive share growth in the Reduced-Risk Products category.

Our fruitful research and development initiatives and ongoing scouting efforts were recently strengthened by a new partnership with Plug-and-Play, a California-based leader in incubator technology platforms which is expected to bring innovators and data experts together, with the aim to explore and develop consumer-relevant features for the next generation of products and services. This new initiative will further broaden our network to new sets of entrepreneurs who can bring disruptive ideas that will ultimately boost the future growth of Logic and Ploom.

Global RRP Strategy on p. 22



Japanese Domestic Tobacco Business

Results for the fiscal year ended December 31, 2018

Cigarette industry volume declined 12.4% and JT cigarette sales volume declined 11.7% year-on-year, due to the underlying trend (natural decline), expansion of Reduced-Risk Products (RRP)* and the impact of a price increase in October 2018.

Though JT cigarette market share contracted briefly due to the price increase, our cigarette market share in December 2018 almost recovered to the same level as before the price increase. For the full year, we achieved 61.8% cigarette market share, an increase of 0.5 percentage points year-on-year led by the solid performance of the core brands.

The overall RRP market size for 2018 was about 21% of the total tobacco industry volume (based on shipment volume). We rolled out Ploom TECH nationwide in July 2018 and throughout 2018, we sold 2.8 billion cigarette equivalent units. Our marketing and sales activities have been focusing more on direct communication with consumers to share the benefits of low temperature heating product, and this approach has been working well. We will continue this so that more consumers recognize the benefits.

We aim to return to profit growth, by managing RRP and cigarettes in a more comprehensive manner. In parallel, it is our strong intention to increase our combined market share of RRP and cigarettes by offering consumers a variety of options in each category.

Chito Sasaki

President, Japanese Domestic Tobacco Business, Tobacco Business

Performance Overview

Volume and Financial

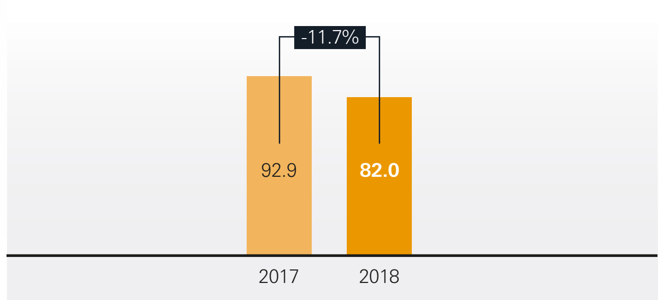
- Revenue and profit decreased due to cigarette industry volume decline
  - In 2018, JT cigarette sales volume decreased 11.7% to 82.0 BnU mainly due to cigarette industry volume decline.
  - JT RRP sales volume reached 2.8 billion cigarette equivalent units.
  - Core revenue decreased 1.4% to 582.4 billion yen mainly because of JT cigarette sales volume decline.
  - Adjusted operating profit decreased 10.0% to 209.0 billion yen affected by revenue decline and increase in marketing expense.

* RRP: Reduced-Risk Products with the potential to reduce the risks associated with smoking.

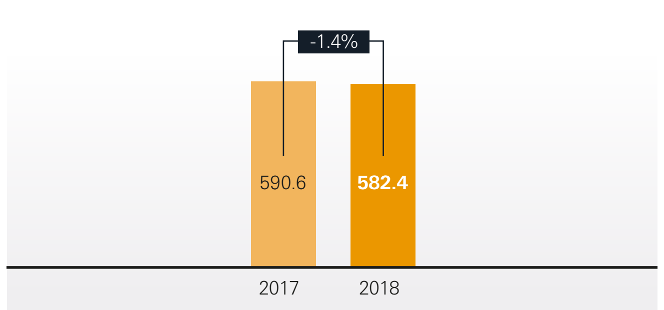
Key Highlights

JT Cigarette Sales Volume	Core Revenue	Adjusted Operating Profit
82.0	582.4	209.0
(BnU)	(JPY BN)	(JPY BN)
-11.7%	-1.4%	-10.0%
Year-on-Year Change	Year-on-Year Change	Year-on-Year Change

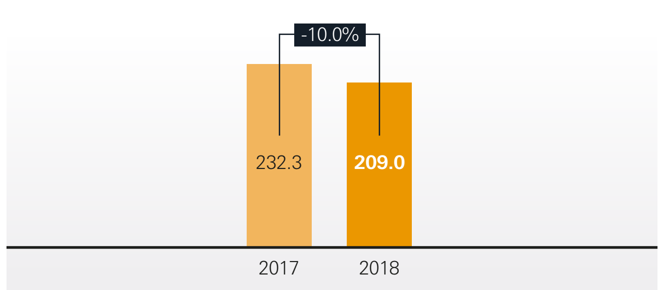
JT Cigarette Sales Volume (BnU)



Core Revenue (JPY BN)



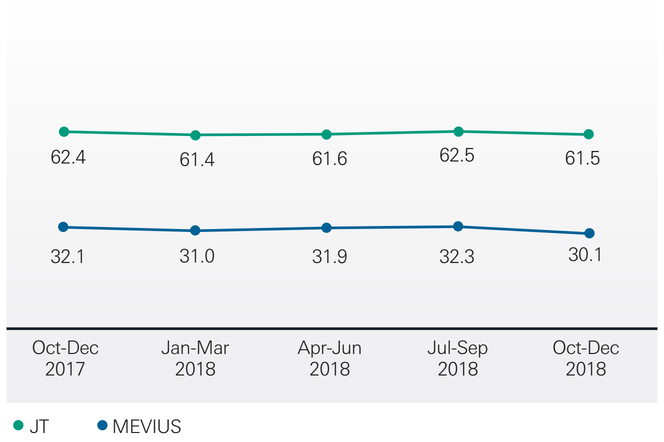
Adjusted Operating Profit (JPY BN)



Share Performance

- In 2018, as a result of continuous investment in sales promotion and brand equity enhancement with a focus on MEVIUS, our cigarette market share improved, with both JT and MEVIUS outperforming their results for 2017 on a full-year basis.
  - 2018 cigarette market share: 61.8% (2017: 61.3%, +0.5 percentage points)
- JT market share in RRP category increased due to Ploom TECH's nationwide rollout in July 2018.
  - JT market share in RRP category in the fourth quarter of 2018 was about 10% (in convenience stores).

Cigarette Market Share Evolution of JT and MEVIUS (%)



Roadmap to Sustainable Growth

The Japanese domestic tobacco business aims to return to sustainable profit growth, by managing RRP and cigarettes in a more comprehensive manner. In parallel, it is our strong intention to increase our combined market share of RRP and cigarettes by offering consumers various options in each category.

As RRP is the pillar of our growth, although competition has further intensified, we prioritize the allocation of resources into this category. Our nationwide roll-out for Ploom TECH+ is planned in July 2019 and in September 2019 for Ploom S, which will increase our product offerings. In order to be chosen by consumers, it is imperative to build awareness and recognition for each product. We will strengthen marketing initiatives to enhance our competitiveness and win the leading position.

For cigarettes, industry volume shows resiliency and remains solid. This category continues to be the platform of profitability to support growth. We will enhance the equity of our core brands.

Outlook

In 2019, we forecast that our revenue and adjusted operating profit will increase by 6.5% and 2.9%, respectively. This is based on cigarette pricing and increased RRP sales volume with two new products that will more than offset a decline in JT cigarette sales volume.

Please be reminded that this section is intended to explain the business operations of JT to investors, but not to promote sales of tobacco products or encourage smoking by consumers.

Our Core Brands

Natural American Spirit

- The Natural American Spirit brand was born in the USA in 1982, and introduced to Japan in 1996.
- JT Group completed the acquisition of the Natural American Spirit non-U.S. business in January 2016 and has since been expanding its markets including Japan, Germany, Italy, Switzerland, the UK and Spain.
- The Natural American Spirit brand vision is unchanged even after its phenomenal growth globally with the idea to provide the most premium, additive-free, all natural tobacco product.
- The Natural American Spirit family comprises a line-up of 10 cigarette products as well as 3 Roll-your-own products.

MEVIUS

- Evolved in 2013 from Mild Seven, MEVIUS has commanded the No. 1 share in the Japanese domestic cigarette market for more than 40 years.
- Available in regular for smooth taste and menthol, MEVIUS allows consumers to enjoy premium high-quality products with 100% natural menthol.
- The MEVIUS family comprises a line-up of 40 cigarette products as well as 6 capsule products for Ploom TECH, 4 capsule products for Ploom TECH+ and 3 stick products for Ploom S, JT's tobacco vapor products.

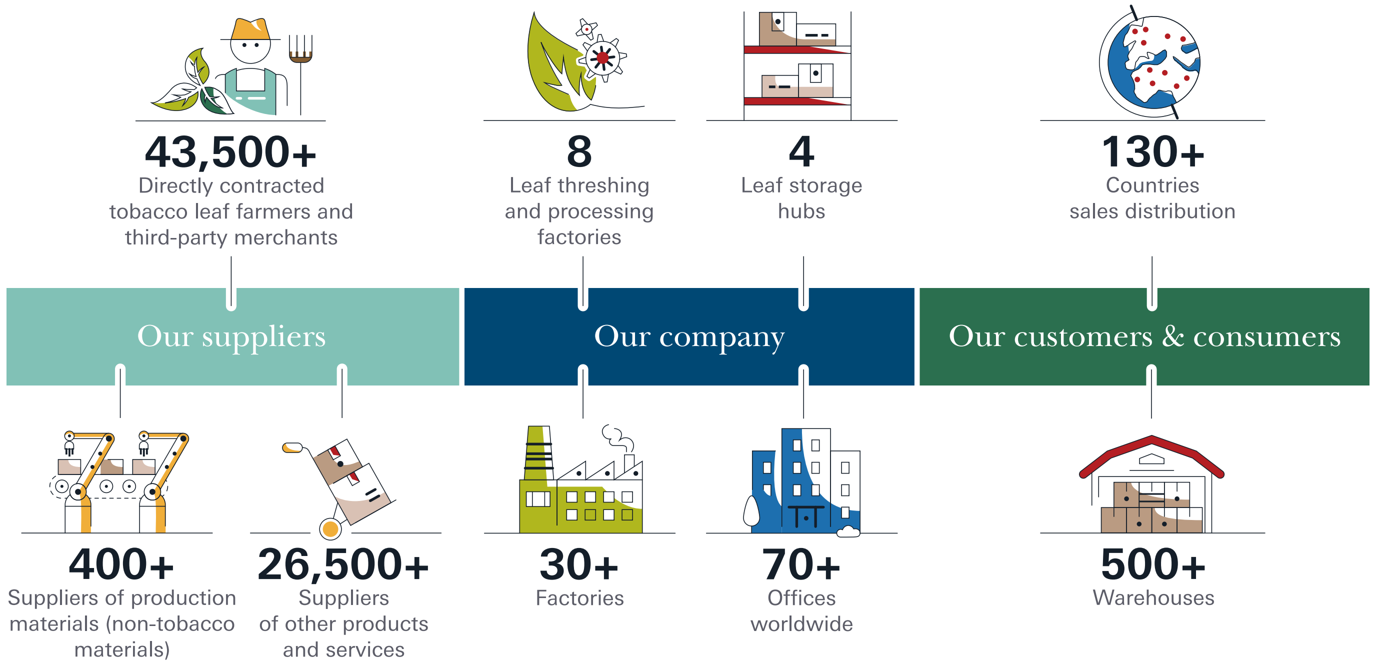
Seven Stars

- Launched in 1969, Seven Stars featured Japan's first domestically produced charcoal filter in pursuit of better taste.
- Since its launch, Seven Stars has consistently offered unique value in terms of taste, aroma and product design.
- Seven Stars Original soft package with 14 mg tar has remained the most sold product in the Japanese domestic cigarette market for 11 years through 2018.
- The Seven Stars family comprises a line-up of 8 products.

Winston

- First introduced in 1954 in the USA.
- In 2015, CABIN and CASTER were migrated into Winston in Japan. Winston has three types of taste, "Bitter," "Straight" and "Sweet," in both the Regular and Menthol segments.
- The Winston family comprises a line-up of 26 products.

Tobacco Business Value Chain



R&D

Create value for the business through innovation and quality

- We focus on fundamental research and product technology development, taking advantage of our global research platform, in close collaboration with other functions. In particular, our R&D activities focus on these areas.
  - Develop products and analytical capabilities in line with market needs and our anticipation of regulatory trends
  - Maintain existing products to comply with regulatory changes
  - Develop new technologies and improve production processes to maintain competitiveness and increase efficiency
  - Drive product innovation to enhance equity from various aspects, including tobacco leaves, blends, filters, printing techniques and packaging
  - Develop RRP

Procurement

Ensure stable supply of quality tobacco leaf

- Tobacco leaf is the most important material for our products, and we dedicate our efforts to strengthen our capability to ensure a stable supply of quality leaf in the long-term.
  - Increase the proportion of leaves from our vertical integration bases in Africa, Brazil and the USA
  - Enhance sustainability of tobacco farming by helping farmers to improve productivity as well as taking initiatives to support their communities
  - Maintain good relationships with external suppliers to ensure sufficient supply at competitive prices
- With regard to non-tobacco materials, we aim to mitigate cost increases due to design enhancements and investment in innovative products by, among others, effectively managing procurement lot-size.

Manufacturing

Support top-line growth by delivering quality products

- Our emphasis on product quality is increasing to meet consumer expectations for innovative offerings. In addition, we consistently pursue an optimal manufacturing footprint which ensures efficient and timely product deliveries to markets.
  - Ensure high quality of products and enhance flexibility in the manufacturing process, overcoming complexity in manufacturing due to an increase in number of products
  - Strengthen our ability for business continuity in times of emergency
  - At the same time, seek efficiency by containing cost increases through continuous improvement and reviewing our manufacturing footprint for further optimization

Marketing

Enhance equity of flagship brands

- Our strategic focus is placed on our flagship brands and we strive to enhance their equity through effective communications with consumers.
  - Allocate appropriate resources to support GFB's equity building
  - Implement responsible marketing programs in compliance with applicable laws and regulations as well as our internal global marketing principles

Sales & Distribution

Expand product availability by leveraging our trade marketing excellence

- There are various sales channels for tobacco products such as supermarkets, convenience stores, street and train station kiosks, small independent retailers and vending machines. Key channels are different depending on the market and we develop win-win relationships with them to increase the availability of our products.
  - Strengthen relationship with key accounts, leveraging our trained sales forces
  - Develop trade marketing initiatives for each market, taking into account channel development as well as consumer trends and competitors' actions

Pharmaceutical Business

Results for the fiscal year ended December 31, 2018

In 2018, the pharmaceutical business grew both revenue and adjusted operating profit by 8.9% and 18.0%, respectively. This result was achieved by higher royalty revenues as well as milestone revenue, thus contributing to JT Group's overall profit growth.

Strategy

- Promote R&D for next-generation strategic compounds and seek optimum timing to license them out
- Maximize the value of each product

Performance Overview

- Both revenue and adjusted operating profit increased 9.3 billion yen and 4.3 billion yen, respectively, driven by higher royalty revenues from increased sales of original JT compounds and milestone revenue.
- In-house development (2018 progress)
  - Entered the clinical trial stage: JTT-662 (SGLT1 inhibitor) - Phase 1 (Overseas)
  - Advanced to the next stage: JTT-751 (Oral iron replacement) - Phase 3 (Japan)

Please visit
https://www.jt.com/investors/results/S_information/pharmaceuticals/pdf/2018/20190207_12.pdf
for further details

Roadmap to Sustainable Growth

In 2019, we will enter a challenging period as our forecast for revenue and adjusted operating profit is expected to decrease 28.9% and 82.4%, respectively, due to the termination of the exclusive rights of six Anti-HIV Drugs in Japan and a decline of HIV-related royalty revenues following weaker sales of original JT compounds.

However, our pipeline in non-virus areas is steadily growing more robust. A New Drug Application was filed for JTE-052 Ointment (atopic dermatitis) in Japan on January 31, 2019. In addition, JTZ-951 (anemia associated with chronic kidney disease) and JTT-751 (iron-deficiency anemia/additional indication) are in Phase 3.

We will continue to enhance our R&D capability to discover new drugs, maximize the value of each product, and explore strategic in-licensing opportunities. With the aim of contributing to the Group's mid- to long-term sustainable profit growth, we are building an R&D-led business, aiming at first-in-class internationally competent compounds, to increase our market presence.

In addition, Torii Pharmaceutical Co., Ltd. announced its new mid-term strategic plan on February 6, 2019. Under the plan,

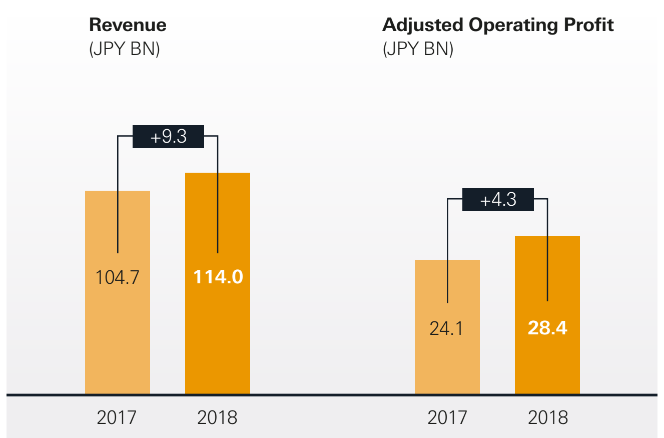
Revenue and adjusted operating profit are forecast to decrease in 2019 with the termination of exclusive rights agreements for six Anti-HIV Drugs in Japan and a decline in HIV-related royalty revenues accompanying weaker sales of original JT compounds. As we face this challenging period, we will rebuild our business foundation and aim to contribute to the Group's mid- to long-term sustainable profit growth by promoting R&D for next-generation strategic products and maximizing the value of each product.

Muneaki Fujimoto

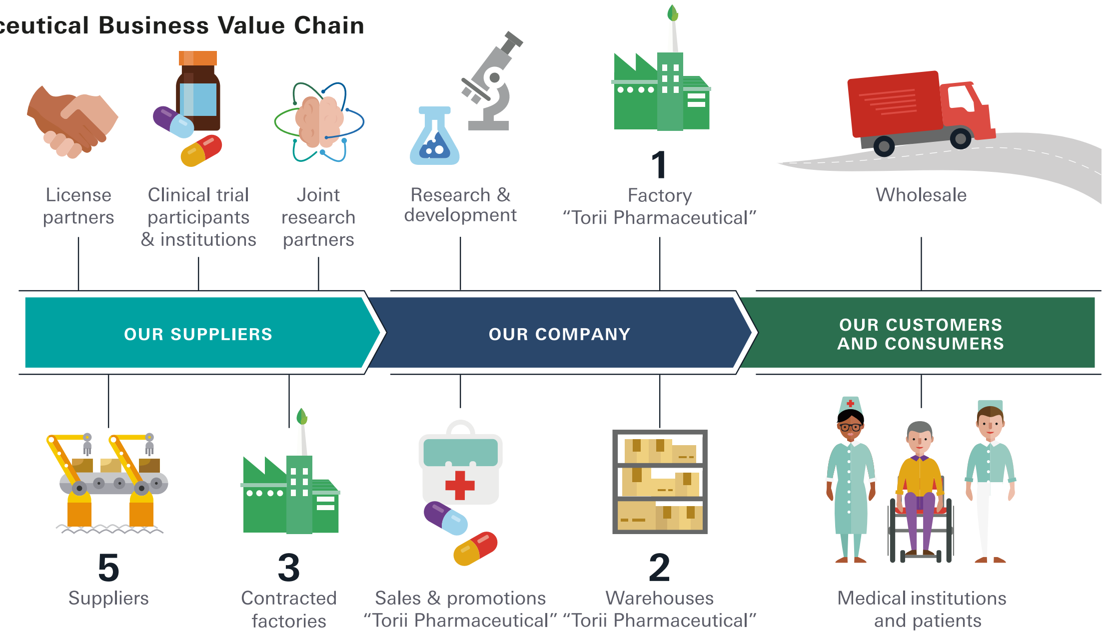
President, Pharmaceutical Business

Key Highlights

Revenue (JPY BN)	Adjusted Operating Profit (JPY BN)
114.0	28.4
+9.3 Year-on-Year Change	+4.3 Year-on-Year Change



Pharmaceutical Business Value Chain



Note: This diagram represents the value chain of products manufactured and/or developed by JT and sold and promoted by Torii Pharmaceutical.

Torii Pharmaceutical will undertake the comprehensive reform of its business structure, including optimization of organization, functions and workforce as well as a revised resource allocation strategy. Furthermore, its new growth strategy is embedded in the plan, with an emphasis on product value maximization, pursuit of in-licensing and further collaboration between JT Group. Through these initiatives, Torii Pharmaceutical aims to improve profitability and sustainably generate profit.

R&D

- We continue to strengthen our R&D capability which enables us to create innovative drugs by focusing our resources on specific therapeutic areas.
- We have established in-house regulations on animal testing based on government legislation. Our Institutional Animal Care and Use Committee ensures that we follow the 3R* concept. Our animal-testing practices are certified by the Japan Health Sciences Foundation, an external authority.

* 3R: (1) Replacing laboratory animals with other research materials where possible; (2) Reducing the number of animals used; and (3) Refining tests so that animals do not suffer unnecessary pain and distress.

Manufacturing

- We establish a sustainable supply chain that delivers high quality products to patients.
- Products marketed in Japan are mainly produced by Torii Pharmaceutical to maximize intra-group synergies, while outsourcing to contract manufacturers where appropriate.
- We have developed guidelines outlining how to conduct annual inspections to confirm consistency between government-registered and actual production methods. To guarantee the product quality, we are now making sure that our own factories and our contracted factories fully adhere to these guidelines.

Sales & Promotion

- Torii Pharmaceutical is marketing our products in Japan.
- Outside Japan, we receive royalties based on sales performance from our license partners for the compounds for which we license out the rights to develop and market.

Yokohama Research Center (completed in January 2019)

Processed Food Business

Results for the fiscal year ended December 31, 2018

In 2018, both revenue and adjusted operating profit decreased. The positive performance of staple food* and seasoning products, as well as an increase in the prices of some products, could not offset the lower sales of other products and higher raw material costs. While the environment remains challenging, we will achieve continuous top-line growth by establishing the Food Business Planning Division within JT in 2019. Under the new structure, we will continue to strive to provide high value-added products by focusing on staple foods.

* Staple food: Frozen noodles, frozen rice, packed cooked rice and frozen baked bread.

Strategy

- Increase the attractiveness of our offerings with a particular emphasis on staple food products with our own expertise.
- Strive to develop high value-added products to respond to changing consumer needs.
- Minimize the negative impact of rising raw material costs.

Performance Overview

We primarily engage in business concerning frozen and ambient processed food, notably staple food products, seasonings including yeast extracts and oyster sauce, and products for bakery chain outlets mainly in the Tokyo metropolitan area.

- Revenue decreased 1.1% as the positive performance of staple food and seasoning products could not offset the lower sales of other products.
- Adjusted operating profit declined 23.6% mainly due to higher raw material costs.

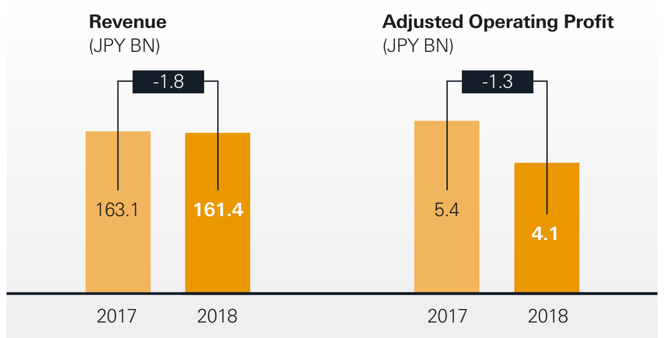
In 2019, both revenue and adjusted operating profit are forecast to grow due to increasing sales of staple products and the improvement of profitability through productivity enhancements in spite of higher raw material costs. We will focus on staple foods, as well as pursue a robust operating base through optimization of production to complement the Group's profit growth.

Atsuhiro Kawamata

Food Business

Key Highlights

Revenue (JPY BN)	Adjusted Operating Profit (JPY BN)
161.4	4.1
-1.8 Year-on-Year Change	-1.3 Year-on-Year Change



Roadmap to Sustainable Growth

Revenue for 2019 is forecast to increase 0.4% versus the prior year, due to increasing sales of staple products. Adjusted operating profit is also expected to grow 21.3% or 0.9 billion yen to 5.0 billion yen, led by the improvement of profitability through productivity enhancements in spite of higher raw material costs. Under the new structure, we aim to achieve mid- to long-term sustainable profit growth focused on continuous top-line growth.

Processed Food Business Value Chain

Notes: This diagram represents the value chain of products for frozen and ambient foods.
We do not deal directly with raw material producers - such as growers - who provide raw materials to the trading firms or to the contracted factories that supply us.

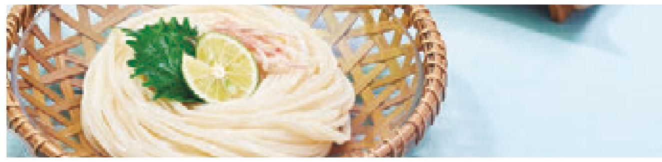
With our desire to "cordially prepare food with care for those who matter to us the most," we are dedicated to delivering safe and high-quality food products to our consumers by thoroughly managing food safety.

Procurement: Ensure procurement of safe and quality raw materials

- Review of quality assurance certificates submitted by our suppliers.
- Inspections and monitoring of agrochemical residues and regular inspection at processing plants, in compliance with JT Group's internal standards, the Food Sanitation Act and other relevant laws.
- Examination of safety of production sites for raw materials sourced abroad.
- As for agricultural farms, inspections include soil and water and extend to how products are cultivated and how agrochemicals are handled. Breeding farms are also inspected.

Production: Prioritize safety and follow established quality control procedures

- JT Group is pursuing the adoption of the HACCP system and FSSC22000 in our own factories and those of our business partners. Under the FSSC22000 standard, continuous improvements are made following effective rules to control sanitation and other key issues. These rules are based on the HACCP concept, and their effectiveness is tested using scientific evidence.
- All of JT Group's 31 factories in and outside Japan have achieved FSSC22000 certification, which is recognized by the Global Food Safety Initiative, the food industry's global body that promotes food safety management. In addition, all of the factories that are contracted to manufacture frozen food products on our behalf have also achieved the ISO22000 or FSSC22000 certification.



Sales & Distribution: Increase penetration to retail outlets

- Enhance profitability through our initiatives to increase our presence in supermarkets and convenience stores by offering a wider range of products while also seeking better shelf space.
- Our products are also sold to restaurants and other public facilities. We are always willing to provide details about our food products. On the product labels, we disclose the factory where the products were made, as well as the country of origin of the main ingredients. We also have toll-free numbers on our product labels for consumers to call for extra information. In addition, in order to ensure the products' safety, we implement a system that records information on each step of the value chain, starting from raw materials procurement to the product sales, and also can trace back our products if necessary.

Reducing Our Environmental Impact

- Thai Foods International, a JT group company focusing on the manufacture and sale of seasonings, is building a biomass co-generation system that uses rice husks as fuel in its Thai factory.
- This factory uses electricity procured from a local electric company, and once the system starts operating in 2019, it is expected that purchased electricity usage and the resultant Scope 2* greenhouse gas (GHG) emissions could be significantly reduced (by 7,000 tons of CO_2e** annually).
- This project, which has been adopted by the Joint Crediting Mechanism of the Ministry of the Environment in Japan, will not only help us to address environmental issues and reduce energy costs, but will contribute to GHG emissions reduction in Thailand.

* Scope 2 GHG emissions: Emissions relating to the consumption of purchased energy, such as electricity, steam, or other energy sources.
** CO_2e: "Carbon dioxide equivalent" emissions, a standard unit for measuring carbon dioxide footprints.

The JT Group operates diverse businesses, namely tobacco, pharmaceutical and processed food. In addition, we conduct our business on a global basis, extending to Europe, CIS countries, Africa, the Middle East and others. Due to this diversity and these changing environments, we are exposed to various risks.

Considering such circumstances, we have put in place a risk management framework. Under the framework, relevant divisions are assigned to carefully monitor the development of events that may adversely impact us and prevent their materialization where possible.

When risks materialize, we promptly respond in order to minimize their unfavorable impacts. In reviewing risks, the magnitude of potential impact and likelihood of occurrence are most prudently assessed among other factors. Material risks, which could have a significant impact on our sustainable profit growth and business continuity, are reported to the CEO together with the request for approval to implement countermeasures against them.

The following section describes certain risks which potentially have a material impact on our business operations and financial results, but is not intended to be an exhaustive list of the risks we face. In addition, it is possible that risks that are currently considered immaterial or even unknown could turn out to be material in the future, as the business environment changes.

This section should be read together with the forward-looking statements in this Annual Report.

1 Disruptive Tax Increases

Tobacco products are subject to excise or similar taxes in addition to value-added tax. Excise taxes are increasing in most markets where the JT Group operates as governments seek to secure their revenue or promote public health.

In general, value-added tax is also increasing. As a general principle, we fully pass on any tax increase to consumers by adjusting our sales prices. In addition, to the extent possible, we increase our prices more than the tax increase, considering the financial impact of an expected volume decline. A tax increase within a reasonable range is manageable through such a price increase as well as our efforts to support the top-line and pursue efficiency. Most governments are aware that a substantial tax increase or repeated tax increases can reduce their revenue and they take a rational approach.

However, in the past we have experienced tax increases in some markets that have disrupted our business.

Risk Description and Potential Impact

A disruptive tax increase on tobacco products could result in a large industry volume decline due to lower consumption and, in many cases, increased illicit trade. In addition, down-trading to lower priced products could be initiated or accelerated. Our shipment volume, revenue and profit could decrease due to these negative reactions by consumers.

Measures to Address the Risk

- Promote the understanding of relevant authorities that a disruptive tax increase does not necessarily serve their purpose.
- Optimize our product offerings to capture the potential changes in consumer preference.
- Enhance our geographical portfolio to limit the negative impact of a disruptive tax increase in a specific market.
- Further improve efficiency to protect revenue and earnings.
- If a disruptive tax increase takes place, find an optimal price for each product which minimizes the unfavorable influence in the market.

2 Pressure from Illicit Trade

Illicit trade is a major concern not only for the tobacco industry, but for wider society. For the tobacco industry, it undermines legitimate tobacco business. For society, illicit trade reduces excise revenue for the government, often fuels organized crime, and may increase health concerns due to poor manufacturing standards and improper product handling. The tobacco industry has been fighting against illicit trade, which takes the forms of contraband, counterfeit and illicit whites.

Illegally traded products in a market tend to increase after a substantial tax increase or a repeated tax increase. Regulatory actions seeking to commoditize packages and products could also trigger the acceleration of illicit trade because such commoditization could make counterfeit manufacturing easier and detection of illicit products more difficult. The JT Group takes a zero tolerance approach towards all these criminal activities with an emphasis on eliminating contraband products.

Risk Description and Potential Impact

An increase in illicit trade could reduce legitimate industry volume, leading to a decline in our shipment volume, revenue and profit. In addition, the industry bears the cost to combat illicit trade, resulting in pressure on its earnings. Furthermore, it is possible that low quality counterfeits and improperly handled smuggled products may damage the credibility of genuine brands, as well as the reputation of their owners.

Measures to Address the Risk

- Engage with governments, regulatory bodies and law enforcement agencies to eradicate illicit trade.
- Ensure we buy from and sell to only reputable business partners following our rigorous compliance initiatives.
- Raise awareness among individual consumers of the negative consequences of purchasing illegally traded products.

Working together with authorities

JT International Holding B.V. and JT International S.A., two JT Group subsidiaries, have entered a cooperation agreement with the European Commission, the executive branch of the European Union (EU), and EU Member States as part of efforts to combat illicit trade.

Under the terms of the agreement, we contributed US$50 million annually in the first five years from its execution and will contribute US$15 million annually in the subsequent ten years. This financial contribution is to be used to support anti-smuggling and anti-counterfeiting initiatives led by the EU or EU Member States.

In 2010, JTI-Macdonald Corp., our Canadian subsidiary, also signed a similar agreement with the Government and Provinces of Canada.

In Russia, the introduction of a tobacco products track and trace system has been mandated since March 2019, and we have completed preparations for its introduction.

In FOCUS – Tackling the Illegal Trade of Our Products on p. 18

3 Tightening Tobacco Regulations

The tobacco industry is highly regulated in various aspects, and regulations could influence the business performance of the JT Group and financial results. Among the regulations on products, for example, we may incur additional costs in order to comply with ingredients and packaging requirements.

Furthermore, the regulatory attempt to commoditize tobacco products could lead to an increase in illicit trade and negatively influence our legitimate business.

Business activities of tobacco companies are also restricted. With more prohibitive regulations on communication with consumers, our ability to effectively market products becomes further limited, and our top-line performance may be adversely impacted.

As a responsible organization, we comply with applicable laws and regulations wherever we operate. That said, we believe that laws and regulations should differ country by country, reflecting legal, social and cultural background. We endeavor to hold constructive dialogues with governments and regulators for a reasonable and balanced approach towards tobacco regulation.

Risk Description and Potential Impact

Further tightening of tobacco regulations on marketing activities could undermine our strategy for top-line growth as we lose opportunities to enhance brand equity. Moreover, certain regulations may impose additional compliance costs on us. These may negatively influence our volume, revenue and profit.

Measures to Address the Risk

- Identify ongoing regulatory initiatives as early as possible by promptly collecting accurate information.
- Endeavor to hold constructive dialogues with governments and regulators for reasonable and balanced regulations that meet their objectives.

Regulation and Other Relevant Laws on p. 64

4 Country Risks

The tobacco business of the JT Group has consistently expanded its earnings base to secure long-term growth by making acquisitions, entering new markets and increasing share in markets where we had limited presence. Geographical expansion may increase our exposure to country risks. In any market where we operate, we may face economic, political or social turmoil which may negatively affect our operations and financial results.

Risk Description and Potential Impact

Political instability, economic downturn, social unrest or other unfavorable developments in a certain market could disrupt our business, leading to lower volume, revenue and profit in the market.

Measures to Address the Risk

- Avoid overdependence on a small number of markets as sources of profits by expanding the pool of highly profitable markets.

5 Instability in the Procurement of Key Materials

Across its businesses, the JT Group procures raw and processed materials for product manufacturing.

In particular, we strive to procure key materials in the required quantity and at reasonable costs. Our key materials include agricultural products: most notably, tobacco leaf for the tobacco business, and grains for the processed food business. Availability of agricultural products is often affected by natural phenomena, such as weather conditions. In addition, there is a growing concern that agricultural production costs may rise due to the high demand for energy resources, global population increases, and economic growth in emerging countries.

Risk Description and Potential Impact

Insufficient supply of key materials could lead to inability to manufacture our products, subsequently resulting in the loss of revenue and profit. Furthermore, the increase in procurement costs driven by higher production costs for agricultural products would directly pressure our earnings.

Measures to Address the Risk

- Reinforce ability to procure key materials by building a strong relationship with suppliers. In the case of tobacco leaf, further promote internal sourcing.
- Promote efficient use of materials by continuously reviewing the manufacturing process and product specifications where possible.

6 Unfavorable Developments in Litigation

JT and some of its subsidiaries are defendants in lawsuits filed by plaintiffs seeking damages for harm allegedly caused by smoking, the marketing of tobacco products, or exposure to tobacco smoke. As of December 31, 2018, 21 smoking and health-related cases were pending in which one or more members of the JT Group were named as defendant or for which JT may have certain indemnity obligations pursuant to the agreement such as for JT's acquisition of RJR Nabisco Inc.'s overseas (non-U.S.) tobacco operations. JT and its subsidiaries, who are defendants in such lawsuits, believe that we have valid grounds to defend the claims in such lawsuits; however, we cannot predict the outcome of any pending or future litigation.

In addition to these smoking and health-related cases, JT and its subsidiaries may be a party to other lawsuits in the future, such as product liability claims in the event of a product quality problem.

Risk Description and Potential Impact

A decision unfavorable to us could materially affect our financial performance due to the payment of monetary compensation. Moreover, critical media coverage of any lawsuit may reduce social tolerance about our products and lead to additional regulations. Such media coverage may also prompt the filing of a number of similar lawsuits against JT or its subsidiaries, resulting in increased litigation costs.

Measures to Address the Risk

- Continue to build well-organized teams coordinating with external legal counsel to defend ourselves against these lawsuits.
- Continue legitimate and appropriate business operations.

Litigation on P. 67

7 Natural Disasters

The operations of the JT Group may be disturbed by natural disasters such as earthquakes, typhoons, floods, volcanic eruptions and others. Japan is one of the most important markets for our businesses and subject in particular to various natural disasters. The Great East Japan Earthquake was devastating. The impacts on us included casualties among our employees, physical damage to our factories, and supply shortages of certain tobacco product materials. Our tobacco business was forced to temporarily suspend product shipment and limit shipment volume for an extended period.

We have developed a Business Continuity Plan to minimize the impact of such disasters, with a particular emphasis on the optimization of the global supply chain.

Risk Description and Potential Impact

Natural disasters could cause damage to us as well as our suppliers, trade partners and consumers, leading to disruption of our business and negatively impacting financial results.

Measures to Address the Risk

- Continuously review the Business Continuity Plan and revise it as necessary.
- Carry out emergency drills to increase employees' preparedness against disasters.
- Insure key assets such as buildings, machinery, equipment and inventory to recover financial losses as appropriate.

8 Climate Change

Climate change due to global warming could cause various damages, including flooding and landslide disasters caused by abnormal weather conditions, such as concentrated torrential rains. Severe heat, heavy snowfall and drought due to unseasonable weather changes, water resources depletion, and loss of biodiversity could also be expected to arise from climate change.

Risk Description and Potential Impact

The effects of climate change could adversely affect our results of operations by damaging the JT Group and our Group's value chain.

Measures to Address the Risk

- Work to reduce greenhouse gas emissions, efficient use of water resources, and waste reduction in order to reduce environmental impact.
- Establish a system to better understand the impacts of climate change on businesses and respond appropriately, such as formulating a scientifically based plan to reduce greenhouse gas emissions (SBT: Science Based Targets) and investigating scenario analyses.

9 Currency Fluctuations

As the JT Group is operating globally, it is exposed to risks associated with currency fluctuations. The reporting currency of our consolidated financial statements is Japanese yen, while the financial statements of our international subsidiaries are reported in other currencies such as the Russian ruble, Euro, British pound, Taiwanese dollar, US dollar, and Swiss franc.

Therefore, exchange rate fluctuations in these currencies against the Japanese yen influence our reported financial results. As for the financial reporting of the international tobacco business, JT International Holding B.V. consolidates the financial results of the international tobacco subsidiaries and reports its consolidated financial statements in US dollars. We often communicate the financial performance of our international tobacco business in US dollars, which is affected by exchange rate fluctuations against the US dollar. In principle, we do not hedge these risks which arise from the translation of financial statements.

However, we hedge against risks which arise when equity denominated in each functional currency is translated into Japanese yen to be consolidated by using foreign currency-denominated interest-bearing debt and part of these are designated as net investment hedges. In addition, many companies make transactions in currencies other than their reporting currencies for day-to-day operations. Such transactions also involve the risk of exchange rate fluctuations. We mitigate these transaction risks through hedging activities; however, it is not possible to completely eliminate them.

Furthermore, if we liquidate or sell a Group subsidiary which we acquired in a currency other than Japanese yen or impair a substantial value of such a subsidiary, the gain or loss from the transaction includes the currency fluctuation impact. Specifically, the impact comes from the difference in the exchange rates of the relevant currency against Japanese yen at the time of the acquisition and at the time of such transaction.

Risk Description and Potential Impact

Fluctuations in exchange rates against the Japanese yen affect our reported financial results. The reported financial results of our international tobacco business in US dollars are similarly influenced by the fluctuations in exchange rates against the US dollar. In addition, we are exposed to the exchange rate fluctuation risks when a Group company makes a transaction in a currency other than its reporting currency.

Measures to Address the Risk

- Mitigate the risk through hedging activities such as derivative contracts, possession of interest-bearing debt in foreign currencies and others.

10 Competition

The JT Group competes fiercely in both the domestic and international tobacco business with our competitors.

In the Japanese domestic tobacco market, import of tobacco products was deregulated in 1985, followed by the provisional suspension of customs duties on imported tobacco in 1987. Since then, competition has intensified each year, as smokers' preferences diversify and as our competitors pursue aggressive promotional activities.

In the overseas tobacco markets, we expanded our own business organically as well as through M&A, by acquiring the non-U.S. tobacco operations of RJR Nabisco Inc. and thereafter acquiring Gallaher Group Plc. As a result, we are in competition with global players in the international tobacco business or with local competitors with strength in specific markets.

Market share can fluctuate due to a number of factors, including increasing regulations, rising health awareness, changes in smokers' preferences or changes to economic conditions of each market. It can also fluctuate due to competitors' pricing strategies or strength of brand equity. Moreover, market share can fluctuate in the short-term due to new product launches by each market player and the accompanying promotional activities.

Risk Description and Potential Impact

Fluctuation in our market share may affect our business performance. In addition, price competition (price reductions or brand repositioning, among others) aimed at increasing market share, may negatively affect our profit margins.

Measures to Address the Risk

- Optimize our product portfolio by:
  - developing and providing products that can capture changing consumer preferences and needs.
  - placing brands with strong brand equity in each price category.
- Provide product support by enhancing trade marketing capability and effective promotional initiatives.
- Further improve efficiency to protect revenue and earnings.
- Avoid overdependence on a small number of markets as sources of profits by expanding the pool of highly profitable markets.

Decision-Making, Business Execution, Supervision

Corporate Governance at JT

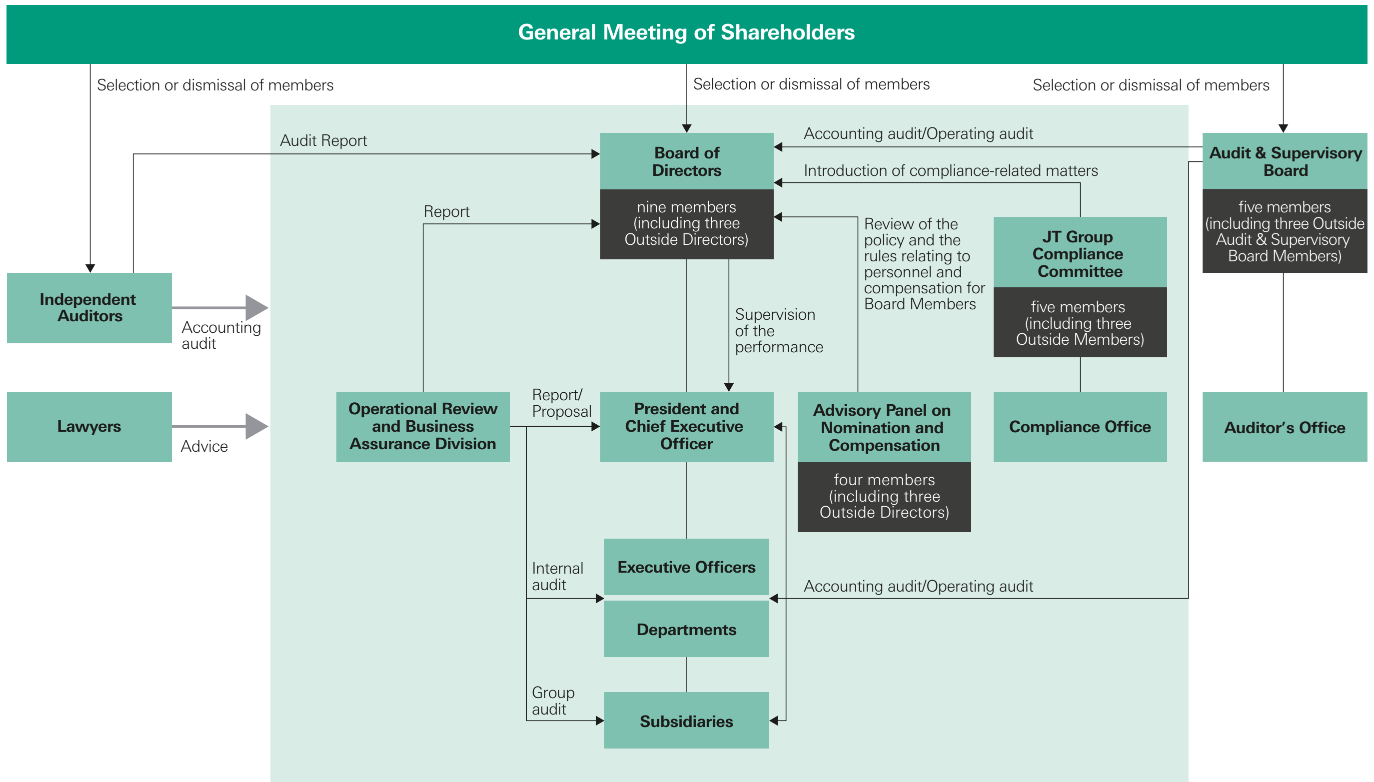
Our belief is that corporate governance is the means for conducting transparent, fair, timely and decisive decision-making for pursuing our management principle, the "4S model." Specifically the 4S model aims "to fulfill our responsibilities to our valued consumers, shareholders, employees and the wider society, carefully considering the respective interests of these four key stakeholder groups, and exceeding their expectations wherever we can." We have set out the "JT Corporate Governance Policy" and strive to make enhancements based on its belief that it will enable us to achieve mid- to long-term sustainable profit growth and increase corporate value, which will contribute to the development of our stakeholders and eventually the economy and society as a whole. We will continue to strive to make enhancing corporate governance one of the key challenges for its management.

Initiatives to enhance corporate governance

Rigorous supervisory and advisory function	Quality and prompt decision-making	Efficient business execution
Set up the Compliance Committee FY2000	Reduced number of Directors FY2000	Introduced Executive Officer system FY2001
Set up the Advisory Committee* FY2001	Promoted the delegation of business execution to the Executive Officers FY2000, FY2008 and FY2011	
Set up the Compensation Advisory Panel FY2006**	Invited Outside Directors FY2012	
Set up the Advisory Panel on Nomination and Compensation 2019		

* Abolition of the Advisory Committee on June 30, 2014.
** Merger of the Compensation Advisory Panel into the Advisory Panel on Nomination and Compensation on March 20, 2019.

Our Corporate Governance System (As of March 20, 2019)



The "JT Corporate Governance Policy" is available at: **https://www.jt.com/about/corporate_governance/**

General Meeting of Shareholders

A general meeting of shareholders resolves the matters stipulated by law and our Articles of Incorporation. Under the Companies Act, certain matters are required to be resolved at a shareholder meeting including, most notably, the appointment and dismissal of the Directors, Audit & Supervisory Board Members and external accounting auditors, dividend amount, loss compensation, as well as change in the Articles of Incorporation. Our Articles of Incorporation do not stipulate any additional matter to be resolved at our shareholders' meeting other than matters legally required. The Annual General Shareholders' Meeting is held in March, and a special meeting of shareholders shall be called by the Board of Directors, as necessary. The President chairs the shareholders' meetings.

Within the extent as permitted by law, requirements for resolutions at our shareholders' meeting were lowered by amending our Articles of Incorporation. A resolution at a general meeting of shareholders can be adopted by a majority of the voting rights present or represented at the meeting. A resolution for the appointment of the Company's Director and Audit & Supervisory Board Members additionally requires a quorum, which is one-third of the total number of voting rights. A special resolution as stipulated under Section 2, Article 309 of the Companies Act, such as amendment to the Articles of Incorporation, requires the quorum of one-third of the total number of voting rights and the approval of at least two-thirds of the voting rights present or represented at the meeting. Certain matters resolved at our shareholders' meetings need further approval by the Minister of Finance in Japan.

The Japan Tobacco Inc. Act

JT was established pursuant to the Japan Tobacco, Inc. Act ('the JT Act') for the purpose of managing businesses related to the manufacturing, sale and import of tobacco products. The JT Act provides that the Government of Japan must continue to hold over one-third of all of the issued shares except for the class shares, which have no voting rights against all matters that can be resolved at our shareholders' meeting. The JT Act also states that the issuance of new shares and stock acquisition rights requires the approval of the Minister of Finance. In the case of a share-for-share exchange, the same approval is required for issuance of new shares, stock acquisition rights and bonds with stock acquisition rights. Under the JT Act, subject to the approval by the Minister of Finance, JT is allowed to engage in businesses other than manufacturing, sales and imports of tobacco products or tobacco-related business, provided that our engagement in such businesses serves the purpose of the Company. JT is also required to obtain approval from the Minister of Finance for certain matters, including the appointment or dismissal of Directors, Executive Officers and Audit & Supervisory Board Members as well as amendments to our Articles of Incorporation, distributions of surplus (excluding loss compensation), mergers, corporate splits, or dissolution. In addition, within three months after the end of each fiscal year, we are required to issue a statement of financial position, a statement of income, and a business report to the Minister of Finance.

The supplementary provisions of the Reconstruction Financing Act,* which came into effect on December 2, 2011, states that the Government shall study by the fiscal year ending March 31, 2023 the possibility of full disposal of government-owned JT shares by reassessing the Government's holding in JT shares considering the Government's involvement in the tobacco-related industries based on the Tobacco Business Act.

* Reconstruction Financing Act: Act on Special Measures for Securing Financial Resources Necessary for Reconstruction from the Great East Japan Earthquake.

The Board of Directors

The Board of Directors assumes responsibility in making decisions for important issues including the Group strategy as well as supervising all the activities of the Group. In view of the point that the Board of Directors determines company-wide management strategy and important matters and effectively assumes roles and responsibilities as the body exercising supervision over all business activities,
the concept concerning the composition of the Board of Directors shall be set forth as follows.

- The number of Members of the Board in the Board of Directors shall be fifteen (15) or less, within necessary and appropriate scope, composed of diverse people with a high-integrity sense of ethics as professionals, knowledge, experience and skills.
- JT shall appoint two (2) or more Independent Outside Members of the Board with qualities that will contribute to its sustainable profit growth and increase of corporate value in the mid- to long-term from the viewpoint of strengthening supervisory functions and transparency of business.

A board meeting, in principle, is held every month and a special board meeting may be called, as necessary. The Board of Directors decides those matters required to be resolved by the Board of Directors under the Companies Act, such as important business plans, disposal or acquisition of important assets, significant amount of borrowings, and conclusion of important agreements. For the purpose of supervising the Company's activities, the Board of Directors requires Directors to deliver a report on the progress of operations at least on a quarterly basis. In the fiscal year ended December 31, 2018, we had 15 board meetings to discuss important issues including the management plan.

Members

9 (including three Independent Outside Directors)
The Directors marked with * are also the Executive Officers.

Yasutake Tango

Chairman of the Board

Date of birth:
March 21, 1951
Term of office:
2 years since March 2018
Number of shares held: 9,100

April 1974
Entered Ministry of Finance
October 2006
Director-General of the Financial Bureau
July 2007
Deputy Vice Minister
July 2008
Director-General of the Budget Bureau
July 2009
Administrative Vice Minister
December 2010
Corporate Auditor, The Yomiuri Shimbun Holdings
December 2012
Special Advisor to the Cabinet
June 2014
Chairman of the Board of the Company (Current Position)
Significant Concurrent Positions outside the Company
Outside Director, The Ogaki Kyoritsu Bank, Ltd.

Masamichi Terabatake*

Representative Director and President, Chief Executive Officer

Date of birth:
November 26, 1965
Term of office:
2 years since March 2018
Number of shares held: 19,000

April 1989
Joined the Company
July 2005
Vice President, Secretary's Office
July 2008
Vice President, Corporate Strategy Division
June 2011
Senior Vice President, Chief Strategy Officer and in charge of Food Business, Vice President, Corporate Strategy Division
March 2012
Senior Vice President, Chief Strategy Officer and in charge of Food Business
June 2012
Senior Vice President and Chief Strategy Officer
June 2013
Member of the Board Executive Vice President, JT International S.A.
January 2018
President and Chief Executive Officer
March 2018
Representative Director and President, Chief Executive Officer (Current Position)

Mutsuo Iwai*

Representative Director and Executive Vice President

Date of birth:
October 29, 1960
Term of office:
2 years since March 2018
Number of shares held: 23,800

April 1983
Joined the Company (Japan Tobacco and Salt Public Corporation)
June 2003
Vice President, Corporate Planning Division
July 2004
Vice President, Corporate Strategy Division
June 2005
Senior Vice President and Vice President, Food Business Division, Food Business
June 2006
Member of the Board and Executive Vice President, President, Food Business
June 2008
Executive Vice President, Chief Strategy Officer
June 2010
Member of the Board and Senior Vice President, Chief Strategy Officer and President, Food Business
June 2011
Member of the Board Executive Vice President, JT International S.A.
June 2013
Senior Executive Vice President, Chief Strategy Officer
January 2016
Senior Executive Vice President, President, Tobacco Business
March 2016
Representative Director and Executive Vice President (Current Position)
Significant Concurrent Positions outside the Company
Chairman and Managing Director, JT International Group Holding B.V.

Naohiro Minami*

Representative Director and Executive Vice President

Date of birth:
January 21, 1964
Term of office:
2 years since March 2018
Number of shares held: 12,600

April 1986
Joined the Company
December 2005
Controller
July 2010
Deputy Chief Financial Officer and Controller
June 2012
Senior Vice President, Chief Financial Officer and Controller
July 2012
Senior Vice President, Chief Financial Officer
January 2018
Executive Vice President
March 2018
Representative Director and Executive Vice President (Current Position)
Significant Concurrent Positions outside the Company
Supervisory Board Member, JT International Holding B.V.

Kiyohide Hirowatari*

Representative Director and Executive Vice President

Date of birth:
November 11, 1965
Term of office:
2 years since March 2018
Number of shares held: 5,800

April 1989
Joined the Company
July 2010
Vice President, Legal Division
June 2012
Senior Vice President, Chief Legal Officer and Vice President, Legal Division
July 2014
Senior Vice President, Chief Legal Officer
January 2015
Senior Vice President, Head of Tobacco Business Planning Division, Tobacco Business
January 2017
Senior Vice President, Human Resources
January 2018
Executive Vice President
March 2018
Representative Director and Executive Vice President (Current Position)

Kazuhito Yamashita*

Director

Date of birth:
February 4, 1963
Term of office:
1 year since March 2019
Number of shares held: 6,400

April 1986
Joined the Company
May 2007
Vice President, Corporate, Scientific & Regulatory Affairs Division, Tobacco Business
July 2009
Vice President, Corporate Affairs Division, Tobacco Business
June 2010
Senior Vice President, Chief Corporate, Scientific & Regulatory Affairs Officer, Tobacco Business
January 2015
Senior Vice President, Head of China Division, Tobacco Business
January 2019
Senior Vice President, Compliance, Sustainability Management and General Affairs
March 2019
Member of the Board (Current Position)

Main Kohda

Outside Director of the Company

Date of birth:
April 25, 1951
Term of office:
2 years since March 2018
Number of shares held: 0

September 1995
Started independently as Novelist
January 2003
Member of Financial System Council, Ministry of Finance Japan
April 2004
Visiting professor, Faculty of Economics, Shiga University
March 2005
Member of the Council for Transport Policy, Ministry of Land, Infrastructure, Transport and Tourism
November 2006
Member of the Tax Commission, Cabinet Office, Government of Japan
June 2010
Member of the Board of Governors, Japan Broadcasting Corporation
June 2012
Outside Director of the Company (Current Position)
Significant Concurrent Positions outside the Company
Novelist
Outside Director, LIXIL Group Corporation
Outside Director, Japan Exchange Group, Inc.
Outside Member of the Board, Mitsubishi Motors Corporation

Koichiro Watanabe

Outside Director of the Company

Date of birth:
April 16, 1953
Term of office:
2 years since March 2018
Number of shares held: 0

April 1976
Joined The Dai-ichi Mutual Life Insurance Company
July 2001
Director, The Dai-ichi Mutual Life Insurance Company
April 2004
Managing Director, The Dai-ichi Mutual Life Insurance Company
July 2004
Managing Executive Officer, The Dai-ichi Mutual Life Insurance Company
July 2007
Director and Managing Executive Officer, The Dai-ichi Mutual Life Insurance Company
April 2008
Director and Senior Managing Executive Officer, The Dai-ichi Mutual Life Insurance Company
April 2010
Representative Director and President, The Dai-ichi Life Insurance Company, Limited
October 2016
Representative Director and President, Dai-ichi Life Holdings, Inc.
April 2017
Representative Director and Chairman of the Board, Dai-ichi Life Holdings, Inc.
Representative Director and Chairman of the Board, The Dai-ichi Life Insurance Company, Limited
March 2018
Outside Director of the Company (Current Position)
Significant Concurrent Positions outside the Company
Representative Director and Chairman of the Board, Dai-ichi Life Holdings, Inc.
Representative Director and Chairman of the Board, The Dai-ichi Life Insurance Company, Limited

Yukiko Nagashima

Outside Director of the Company

Date of birth:
April 4, 1961
Term of office:
1 year since March 2019
Number of shares held: 0

April 1985
Joined Recruit Co., Ltd. (Current Recruit Holdings Co., Ltd.)
April 2006
Corporate Executive Officer, Recruit Co., Ltd.
January 2008
President and Representative Director, Recruit Staffing Co., Ltd.
October 2012
Corporate Executive Officer, Recruit Holdings Co., Ltd.
June 2016
Standing Audit and Supervisory Board Member, Recruit Holdings Co., Ltd.
April 2018
Standing Audit and Supervisory Board Member, Recruit Co., Ltd.
March 2019
Outside Director of the Company (Current Position)
Significant Concurrent Positions outside the Company
Standing Audit and Supervisory Board Member, Recruit Holdings Co., Ltd.
Standing Audit and Supervisory Board Member, Recruit Co., Ltd.

Interviews with Outside Directors

Main Kohda
Outside Director of the Company

Koichiro Watanabe
Outside Director of the Company

Japan Tobacco Inc. (JT) has been appointing Outside Directors with qualities that contribute to its sustainable profit growth and increase of corporate value in the mid- to long-term from the viewpoint of enhancing the supervisory functions and transparency of business. We asked Main Kohda and Koichiro Watanabe, who have served as JT's Outside Directors since 2012 and 2018, respectively, about their view of JT's corporate governance.

What do you think your role is as Outside Director?

Director Watanabe

Contributing to the pursuit of the 4S model by taking advantage of the experience of working on both the investor and corporate sides

My career background in life insurance business means that I was originally in a position responsible for calling for actions to enhance corporate governance as an institutional investor based on the Stewardship Code. However, as a result of the conversion of my company into a joint stock company and its stock listing in 2010, I also experienced being in the position of being called on to enhance corporate governance as well as the position of calling for action. Confronted with the responsibilities associated with these two opposite positions as an insurance company's president, I had to think hard about questions on business management, the enhancement of governance and sustainable corporate growth.

In particular, going forward, although management emphasizing ROE is naturally important, I wonder whether that approach is really sufficient. I have the sense that an approach like JT's 4S model, as represented by the traditional Japanese concept of *sanpo yoshi* (benefits for all three sides—business, customers and society) has been becoming a global mainstream, particularly since the collapse of Lehman Brothers triggered the global financial crisis. I hope that my own experience will contribute to what JT aims to achieve under the 4S model.

Director Kohda

Continuing to inject fresh air in order to promote better decision-making on how to cope with change and crisis

JT is a company with an assiduous and conscientious culture, and it has the strength to move forward as an organization with solid unity. However, the company should develop greater diversity if it is to better cope with change and crisis. If different elements within a company shake it up when it is confronted with an external change, the company will emerge as a much stronger organization after the dust has settled. Having served as Outside Director for around seven years, I believe that JT has

significant potential, so I would like to continue to inject fresh air into the company as an outsider.

Before starting an independent career as a novelist, I worked for a US financial institution, where I often served as an in-between for people with different business cultures because of the nature of the company's business. I feel that the questions I used to ask myself and the solutions that I arrived at in those days have been useful when performing my duties as Outside Director.

What is your view of JT's governance system?

Director Watanabe

A governance system which is based on the 4S model and which has the ability to change

In my view, JT's governance system has the ability to change. While doing business globally, JT has established a new governance system under which the governance system of the Japanese parent company coordinates and collaborates with the group's global governance system. This is a governance model which works successfully on a global scale while leveraging what is good about Japan and the strengths of the Japanese market. In that respect, it is one of the few successful models developed by Japanese companies. The ability to change is one of JT's strengths that can be taken advantage of in order to continue to further enhance governance in the future.

Director Kohda

The resolve to overcome enables JT to move forward and make bold decisions

JT has been implementing M&A. Implementing M&A is somewhat like embracing a crisis. I believe that the driving force of the M&A initiative is a sense of crisis. After the privatization of Japan Tobacco and Salt Public Corporation that created JT, the company continued to be exposed to, but survived, several shockwaves, including the impacts of the elimination of tobacco import tariffs and the expiry of the licensing contract for Marlboro.

Since then, JT has continued to turn change in the surrounding environment into opportunity while maintaining an appropriate sense of crisis and sense of responsibility to overcome the change. In my view, JT's perpetual sense of urgency gives it the energy to take action as an organization to overcome difficulties and make bold decisions. JT may pride itself on having taken advantage of crises and difficulties as opportunities to move forward.

What are the JT Group's must-dos in order to increase its corporate value?

Director Kohda

JT should enhance public communication to ensure genuine understanding of its various activities

As the public's view of the tobacco industry becomes more critical year after year, there is a strong need to consider how best to get stakeholders to understand the company and

make efforts to that end. I have the impression that JT is a little too modest, and passive in reaching out to stakeholders. Since I took office as Outside Director, I have continued to mention the need for JT to make increased efforts to enable stakeholders to more accurately understand the true worth of JT's various activities.

Devoting effort to implementation is naturally essential, but now is the time when an equal amount of effort should be devoted to communication as well. The reality is that the headwinds against JT have become that strong. Enhancing public communication is what JT should do now.

Director Watanabe

JT should continue to realize sustainable growth and cultivate the ability to take advantage of change

As things stand now, JT's management is surrounded by risks. Change generates friction and friction creates progress. It is essential to consider what innovations to create and, in a broader sense, how to cultivate the ability to take advantage of change through the approach of backcasting from the future. The Society 5.0 for SDGs initiative is a vision of a desirable society that Japan has proposed in order to enhance human elements, such as creativity based on diversity, at a time when digitalization is proceeding further and social structures are undergoing dramatic change of an unforeseen scale. This initiative has something to do with JT's management principle that explicitly incorporates human elements in the form of the 4S model. I expect that in a world aiming to realize Society 5.0, the ability to cope with change and the human resource capacity that JT has until now developed can be more easily put to good use. To realize sustainable growth, I would like JT to always be cognizant of what first step should be taken to create a business model that can cope with a new age. I am sure that this is what JT has done until now, and RRP (Reduced-Risk Products) can be promoted only when JT maintains that viewpoint. Sustainable growth springs from the ability to take advantage of change.

The Audit & Supervisory Board

Entrusted by shareholders and ensured of its autonomy, the Audit & Supervisory Board conducts accounting audits as well as operating audits. Currently, we have five Audit & Supervisory Board Members including three Outside Audit & Supervisory Board Members. Collectively, they have experience in management, legal, finance and accounting among other areas. The Audit & Supervisory Board Members have various statutory rights in order to accomplish their roles and responsibilities, including making requests to deliver reports to the Directors, Executive Officers and employees, issuing an injunction to prevent illegal activities by Directors, and representing the Company in case of litigation between any Director and the Company. In addition, the Audit & Supervisory Board has a right to dismiss the auditing firm which conducts accounting audit. The Audit & Supervisory Board Members' report containing the results of both the accounting and operating audits is submitted to the annual general meeting of shareholders.

Ryoko Nagata

Standing Audit & Supervisory Board Member

Date of birth:
July 14, 1963
Term of office:
4 years since March 2019
Number of shares held: 12,400

April 1987
Joined the Company
April 2001
Vice President, Products Division, Food Business Division, Food Business
June 2008
Senior Vice President, Head of Beverage Business Division and Vice President, Product Division, Food Business Division, Food Business
July 2008
Senior Vice President, Head of Beverage Business, Food Business
July 2010
Senior Vice President, Head of Beverage Business
June 2013
Senior Vice President, CSR
January 2018
Senior Vice President, Assistant to President
March 2018
Standing Audit & Supervisory Board Member of the Company (Current Position)

Hiroshi Yamamoto

Standing Audit & Supervisory Board Member

Date of birth:
November 29, 1963
Term of office:
4 years since March 2019
Number of shares held: 0

April 1987
Joined the Company
July 2008
Vice President, NTM Procurement Division, Tobacco Business
June 2012
Vice President, Operational Review and Business Assurance
March 2019
Standing Audit & Supervisory Board Member of the Company
(Current Position)

Toru Mimura

Standing Audit & Supervisory Board Member (Outside Audit & Supervisory Board Member)

Date of birth:
December 26, 1955
Term of office:
4 years since March 2019
Number of shares held: 0

April 1979
Entered Ministry of Finance
July 2010
Deputy Director-General of the Planning and Coordination Bureau, and Secretary-General of the Executive Bureau, Certified Public Accountants and Auditing Oversight Board, Financial Services Agency
July 2011
Director General, Kinki Local Finance Bureau, Ministry of Finance
January 2012
Deputy Director-General, Minister's Secretariat, Ministry of Defense
September 2012
Director General, Bureau of Personnel and Education, Ministry of Defense
July 2013
Director General, National Institute for Defense Studies, Ministry of Defense
July 2014
Director General, Bureau of Finance and Equipment, Ministry of Defense
October 2015
Vice-Minister of Defense for International Affairs, Ministry of Defense
September 2016
Chairman, Sompo Japan Nipponkoa Research Institute Inc.
October 2017
Director, Eltes Co.,Ltd.
March 2018
Registered as Attorney at Law
March 2019
Standing Audit & Supervisory Board Member of the Company (Current Position)
Significant Concurrent Positions outside the Company
Attorney at Law, Shiba International Law Offices

Hiroshi Obayashi

Audit & Supervisory Board Member (Outside Audit & Supervisory Board Member)

Date of birth:
June 17, 1947
Term of office:
4 years since March 2019
Number of shares held: 0

April 1970
Judicial Apprentice
April 1972
Appointed as Public Prosecutor
May 2001
Director-General of the Rehabilitation Bureau, Ministry of Justice
January 2002
Deputy Vice-Minister of Justice, Ministry of Justice
June 2004
Director-General of the Criminal Affairs Bureau, Ministry of Justice
June 2006
Vice-Minister of Justice, Ministry of Justice
July 2007
Superintending Prosecutor, Sapporo High Public Prosecutors' Office
July 2008
Superintending Prosecutor, Tokyo High Public Prosecutors' Office
June 2010
Prosecutor-General
March 2011
Registered as Attorney at Law
March 2015
Audit & Supervisory Board Member of the Company (Current Position)
Significant Concurrent Positions outside the Company
Attorney at Law, Obayashi Law Office
Outside Audit & Supervisory Board Members, Daiwa Securities Co. Ltd.
Outside Director, Mitsubishi Electric Corporation
Outside Audit & Supervisory Board Members, Nippon Steel & Sumitomo Metal Corporation

Koji Yoshikuni

Audit & Supervisory Board Member (Outside Audit & Supervisory Board Member)

Date of birth:
September 7, 1952
Term of office:
4 years since March 2019
Number of shares held: 0

April 1975
Joined Japan Broadcasting Corporation
June 2003
Director Responsible for Finance of News Department, Japan Broadcasting Corporation
June 2005
Executive Director, Yokohama Broadcasting Station, Japan Broadcasting Corporation
June 2007
Chief of Secretariat for Board of Governors, Japan Broadcasting Corporation
February 2010
Senior Director, Japan Broadcasting Corporation
April 2012
Executive Director, Japan Broadcasting Corporation
April 2017
Vice President, the Graduate School of Project Design (Current position)
Auditor, Hosei University (Current position)
March 2019
Audit & Supervisory Board Member of the Company (Current Position)

If Directors and Executive Officers find any issue that may cause a substantial damage to the Company, they are obliged to report it to the Audit & Supervisory Board, along with other relevant matters that could affect the Company. Audit & Supervisory Board Members are authorized to attend the meetings of the Board of Directors and other important meetings. Our Directors and Executive Officers respond in a prompt and appropriate manner, when requested by Audit & Supervisory Board Members to deliver documents for their inspection, to arrange field audits and to submit reports. The Operational Review and Business Assurance Division, which conducts internal audits, as well as the Compliance Office, exchanges necessary information and works together with Audit & Supervisory Board Members.

Members

5 (including three Outside Audit & Supervisory Board Members)

Independence of Outside Directors and Outside Audit & Supervisory Board Members

JT reports to the securities exchange on which it is listed that the three Outside Directors and two Outside Audit & Supervisory Board Members are designated as Independent Executives. We have a criteria list to assess the independence of an Executive. Based on the criteria, the independence of the five Executives has been confirmed.

From the viewpoint of strengthening the supervisory functions, we have designated Ms. Main Kohda, Mr. Koichiro Watanabe, Ms. Yukiko Nagashima, who are Outside Directors, and Mr. Hiroshi Obayashi and Mr. Koji Yoshikuni, who are Outside Audit & Supervisory Board Members as Independent Officers as defined by financial instruments exchanges. Mr. Toru Mimura, Outside Audit & Supervisory Board Member, meets the requirements for Independent Executives stipulated by the financial instruments exchanges. However, since he has worked at the Ministry of Finance in the past, he is not designated as an Independent Executive in light of our criteria list for independence. More than seven years have elapsed since he resigned from his post at the Ministry of Finance.

Criteria List for Independence of An Executive

At the Board of Directors on April 26, 2012, the Company established the Criteria for Evaluating the Independence of Outside Executives. According to the Criteria, Independent Directors/Audit & Supervisory Board Members must not fall under any of the following categories.

1. A person who belongs or belonged to JT or an affiliate or sister company of JT
2. A person who belongs to a company or any other form of organization of which JT is a major shareholder
3. A person who is a major shareholder of JT or who belongs to a company or any other form of organization which is a major shareholder of JT
4. A person who is a major supplier or customer of JT (if the supplier or customer is a company or any other form of organization, a person who belongs thereto)
5. A major creditor of JT including a major loan lender (if the creditor is a company or any other form of organization, a person who belongs thereto)
6. A certified public accountant who serves as an accounting auditor or an audit advisor of JT, or a person who belongs to an auditing firm which serves as an accounting auditor or an audit advisor of JT
7. A person who receives a large amount of fees from JT in exchange for providing professional services for legal, financial and tax affairs or business consulting services (if the recipient of such fee is a company or any other form of organization, a person who belongs thereto)
8. A person who receives a large amount of donation from JT (if the recipient of such donation is a company or any other form of organization, a person who belongs thereto)
9. A person who has fit any of the descriptions in 2 to 8 above in the recent past
10. A close relative of a person who fits any of the following descriptions:
    a) A person who fits any of the descriptions in 2 to 8 above (if such descriptions apply to a company or any other form of organization, a person who performs important duties thereof)
    b) A Director, Audit & Supervisory Board Member, audit advisor, Executive Officer or employee of JT or an affiliate or sister company of JT
    c) A person who has fit the descriptions in a) or b) in the recent past

The Advisory Panel on Nomination and Compensation

The Advisory Panel on Nomination and Compensation is a voluntary advisory body to the Board of Directors, which was newly established on March 20, 2019 by merging the functions of the existing Meeting for Talent Development and the Compensation Advisory Panel. This panel was established to aim to further enhance objectiveness and transparency by playing a role in supporting executive candidates, deliberating the selection of candidates for the Directors and the Audit & Supervisory Board Members, deliberating the dismissal of Executive Directors and Members of the Board who execute the business, and making reports after deliberating matters related to remuneration of the Directors and the Executive Officers, thereby enhancing the supervisory function of the Board of Directors. The Advisory Panel on Nomination and Compensation consists of the Chairman of the Board, who chairs the panel, and three Independent Outside Directors. The panel meets at least once a year.

Support for Outside Directors and Outside Audit & Supervisory Board Members

We provide support to Outside Directors and Outside Audit & Supervisory Board Members. The Corporate Strategy Division or Secretary Division explains the agendas for board meetings in advance, submits requested documents and delivers necessary information to Outside Directors for them to contribute to the quality of board discussion. As an independent body entrusted by shareholders, the Audit & Supervisory Board is expected to monitor the performance of the Directors and Executive Officers, with an aim to underpin the Company's healthy and sustainable growth as well as increase its credibility. For Outside Audit & Supervisory Board Members to perform their expected roles, we are supporting them by making necessary information available and allocating adequate human resources to the Auditor Office which assists Audit & Supervisory Board Members.

Executive Officer System

JT employs the Executive Officer System to ensure effective and efficient management by promptly responding to the changing environment, and thus aims to increase its company value. Executive Officers are appointed by the Board of Directors. At the same time, the Board assigns certain responsibilities and delegates relevant authorities to the Executive Officers in accordance with the Rules Defining the Extent of Responsibility and Authority. In addition, we have the structure for quick decision-making about plans and strategy relevant to all business execution except the matters which are submitted to the Board of Directors. This structure has been established by an articulate decision-making process based on the Rules Defining the Extent of Responsibility and Authority.

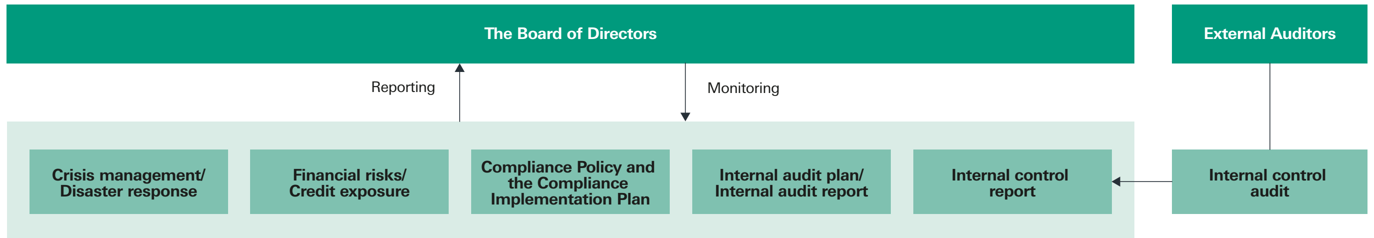
The list of Executive Officers on p. 68

Internal Control System & Risk Management System

Overview

JT devotes its efforts to ensure appropriate business operation by reinforcing internal control such as compliance, internal audit and risk management among other matters. The developments of these internal control focuses are reported regularly to the Board of Directors. In addition, we have the Auditor Office, a department dedicated to support the Audit & Supervisory Board, for our Audit & Supervisory Board Members to effectively perform their duties. JT works with the Group companies to enhance the framework for compliance (including the reporting concerns system), reliable financial reporting, internal audit and risk management.

Internal Control Framework



Compliance

A Code of Conduct has been created based on our internal guidelines approved by the Board of Directors. Under the Code of Conduct, all Directors and employees are expected to fully comply with applicable laws, our Articles of Incorporation, social norms and other compliance standards. In addition, the Board of Directors has established a fair and effective compliance framework as described below.

- Set up the JT Group Compliance Committee, which reviews and discusses compliance-related matters, reporting directly to the Board of Directors
- Appoint an Executive Officer responsible for the Compliance Office
- Discuss and approve the Annual Compliance Plan as well as the Annual Compliance Action Plans
- Report the status of implemented compliance initiatives to the Board of Directors

The Compliance Office is in charge of enhancing the compliance framework, while identifying any issues in the framework. The Compliance Office also promotes compliance by conducting various training programs to Board Members and employees.

The JT Group has both internal and external hotlines through which employees may consult or report any violations or possible violations of the JT Group Code of Conduct. The Compliance Office is responsible for investigating reported cases and implementing corrective measures after discussing it with the divisions concerned. Significant cases are reviewed by the JT Group Compliance Committee, and further reported to the Board of Directors as necessary.

The JT Group Compliance Committee is headed by the Chairman of the Board, with the majority of the members consisting of external members. The JT Group Compliance Committee met three times in the fiscal year ended December 31, 2018, and discussed initiatives to promote compliance throughout the Group among other matters.

Reliable Financial Reporting

In order to ensure the reliability of its financial reporting, JT has introduced a relevant internal control system in accordance with the Financial Instruments and Exchange Act and other standards. In addition, a dedicated division has been created which reviews the internal control system and reports the result of the assessment. Reliability of our financial reporting is confirmed by the external accounting auditor who makes an assessment of our internal control system based on the Internal Control Report we prepare.

Risk Management

Financial risk management

JT has put in place the internal guidelines for financial risk management and ensures that relevant reports are made to the CEO and the Board of Directors on a quarterly basis via the CFO.

Crisis Management and Disaster Control

In order to deal with possible crises or disasters, JT has produced a manual for crisis management and disaster control so that we can make a proper initial response. In the event of a crisis or a disaster, a project team led by the President is immediately assembled. In the project team, the Corporate Strategy Division assumes the key role to support the CEO. Under the leadership of the President, we respond promptly and properly, ensuring close cooperation across the organization. Crisis or disaster incidents shall be reported to the Board of Directors.

Management of Other Risks

In accordance with the Rules Defining the Extent of Responsibility and Authority, management of other risks is delegated to relevant divisions, which identify and monitor the risks in their areas of responsibility. Significant risks are reported to the CEO, together with the request for approval to implement countermeasures against them, where necessary.

Risk factors on p. 48

Internal Audit System

JT has an Operational Review and Business Assurance Division, which is thoroughly independent of other JT Group divisions and organizations engaging in operations. Under such a capacity, it conducts internal audits and directly reports to the CEO. The Operational Review and Business Assurance Division has unlimited access to all activities, records and employees Group-wide to accomplish its roles and responsibilities. The head of the division is required to report to the CEO the results of internal audits along with their analysis and assessment, and also reports to the Board of Directors. The head of the division has the right to contact the management of JT and the Group companies regularly and as frequently as needed.

Executive Remuneration

Structure of Executive Remuneration

The Compensation Advisory Panel reviews and provides advice on the policy, framework and calculation method for remuneration of our Directors and Executive Officers in response to inquiries. It also monitors whether our executive remuneration level is reasonable.

Based on the recommendation by the Compensation Advisory Panel, the key policy for our executive remuneration is as follows:

- Set the remuneration at an adequate level to retain personnel with superior capabilities.
- Link the remuneration to company performance so as to motivate executives to achieve their performance targets.
- Link the remuneration to company value in the mid- to long-term.
- Ensure transparency by implementing an objective and quantitative framework.

In accordance with the above policy, remuneration for our executive comprises:

1. **base salary** paid monthly,
2. **executive bonus** linked to our business performance in the relevant year, and
3. **stock option* grants**, the value of which is linked to our mid- to long-term company value.

In 2007, we introduced a stock option program as an incentive linked to the mid- to long-term company value.

Remuneration for Directors is structured as follows:

Remuneration for the Directors who also serve as Executive Officers comprises 'base salary', 'executive bonus' and 'stock option grants'. 'Executive bonus' is included, as they are responsible for the achievement of assigned annual targets through their day-to-day management.

The combined amount of 'executive bonus' at a 100% grant basis and 'stock option grants' is targeted at approximately 80% of respective annual base salary. Excluding Outside Directors, remuneration for the Directors not serving as Executive Officers comprises 'base salary' and 'stock option grants', as they focus on decision-making on the Group strategies in addition to supervision of business and corporate activities. Remuneration for Outside Directors consists solely of 'base salary' and does not include performance linked compensation from the perspective of sustaining their independence.

Remuneration for the Audit & Supervisory Board Members is also composed of 'base salary' alone, in light of their key responsibility to conduct audits.

The maximum amount of the annual aggregate remuneration excluding 'stock option grants' for the Directors and Audit & Supervisory Board Members was approved at our 34th Annual General Shareholders' Meeting in March 2019. The maximum remuneration for all the Directors combined is 1.2 billion yen and 240 million yen for all the Audit & Supervisory Board Members combined. In addition, the ceiling for annual 'stock option grants' for the Directors was approved at the same shareholders' meeting. The ceiling is 960 options in number and 240 million yen in value. The number of the stock options granted to the Directors and the Executive Officers who are not Directors is decided each year by the Board of Directors.

The amount of remuneration for Directors is determined by resolution of the Board of Directors within the approved upper limits, in light of deliberations by the Compensation Advisory Panel. These processes are carried out after benchmarking is undertaken, based on third-party research, into remuneration for corporate executives at major Japanese manufacturers that operate globally and possess comparable levels of size and profits with JT. The amount of remuneration for Audit & Supervisory Board Members is benchmarked in the same way, and determined through discussions among Audit & Supervisory Board Members, within the approved upper limits.

In addition, we merged the function of Compensation Advisory Panel into the Advisory Panel on Nomination and Compensation which was newly established on March 20, 2019. As a result, the functions of the Compensation Advisory Panel described above will be assumed by the Advisory Panel on Nomination and Compensation. During the fiscal year ended December 31, 2018, the Compensation Advisory Panel met 2 times to discuss the level of remuneration among other matters.

* Subscription rights to shares holder may exercise his/her subscription rights to shares only if he/she loses his/her all position as Directors, Audit & Supervisory Board Members and Executive Officers. We do not intend to change this exercise condition in the future.

Total remuneration payments to the Directors and the Audit & Supervisory Board Members, for the fiscal year ended December 31, 2018 are as follows:

Category	Total remuneration and other payments (millions of yen)	Total amount of remuneration and other payments by type (millions of yen)			Number to be paid (people)
		Basic remuneration	Director's bonus*	Stock option grants	
Directors (excluding Outside Directors)	655	369	176	109	8
Audit & Supervisory Board Members (excluding Outside Audit & Supervisory Board Members)	94	94	–	–	3
Outside Directors and Outside Audit & Supervisory Board Members	70	70	–	–	5
Total	**818**	**533**	**176**	**109**	**16**

* Amounts to be paid.

Total remuneration payments to the Directors and the Audit & Supervisory Board Members whose total remuneration exceeds 100 million yen for the fiscal year ended December 31, 2018 are as follows:

Name	Category	Company	Amount of consolidated remuneration and other payments by type (millions of yen)			Total (millions of yen)
			Basic remuneration	Director's bonus	Stock option grants	
Masamichi Terabatake	Representative Director	JT	89	65	25	**179**
Mutsuo Iwai	Representative Director	JT	63	45	19	**126**

The stock options granted for the fiscal year ended December 31, 2018 are as follows:

Resolution date	June 15, 2018
Positions and number of people grants	Directors (excluding Outside Directors): 5 persons Executive Officers (excluding persons serving as Directors): 18 persons
Number of shares	68,800 shares to Directors (excluding Outside Directors) 109,400 shares to Executive Officers (excluding persons serving as Directors) Total 178,200 shares (200 shares per stock acquisition right)

Tobacco Business

Regulation in the International Markets

The regulatory environment for tobacco is getting stricter year by year, in the wake of the Framework Convention on Tobacco Control ("FCTC"), which came into force in February 2005 (Government of Japan accepted it in June 2004).

The purpose of the FCTC is to continuously and substantively control the proliferation of smoking.

Its provisions include price and tax measures to reduce tobacco demand, non-price measures to reduce the demand for tobacco (such as protection from exposure to tobacco smoke, regulation of contents and emissions of tobacco products, regulation of disclosure of tobacco products, regulations on packaging and labeling of tobacco products, regulations on tobacco advertising, promotion and sponsorship, among others), and measures relating to the reduction of the supply of tobacco (such as prevention of illicit trade, prohibition of sale of tobacco products to minors, among others). All Parties to the FCTC are generally obligated to develop, implement, periodically update and review strategies, plans and programs for tobacco control. However the content, scope, and method of specific controls undertaken in the Parties are ultimately legislated by each Party. After entry into force of the FCTC, the Conferences of the Parties (COP) are regularly held and continue discussions of the topics such as those to develop the protocols (for which additional ratification, acceptance, accession and other are required to the FCTC Parties) and guidelines in view of implementation of each FCTC provision.

As examples of specific regulations undertaken in each country, in Russia, an important market for the JT Group, the comprehensive tobacco control law, which includes a retail display ban, restrictions on sales of tobacco products in certain retail stores, a ban on advertising, sponsorship and promotions, the introduction of minimal pricing, a ban on smoking in public places, and anti-illicit trade measures, was adopted in February 2013 and has gradually been implemented since June 2013.

In addition, in the EU, the 'EU Tobacco Product Directive (EU TPD)' was revised from the earlier Directive, promulgated in July 2001, and entered into force in May 2014. The revised Directive includes, among others, strengthening of packaging and labeling regulations, restrictions on the use of additives including menthol for cigarettes and fine cut, regulations related to electronic cigarettes, and anti-illicit trade measures. Each Member State has legislated their national laws based on the revised Directive.

Furthermore, the Australian government has introduced plain packaging regulation which prohibits displaying logos and brand images on the tobacco packages except only for displaying product names in the prescribed color, font, font size, and font color in December 2012. Similar regulations have also been introduced in France, UK, Norway, Ireland and New Zealand and have been legislated or been in the discussion in some other countries.

Although it is difficult to predict the content of future laws and regulations relating to sales activities, marketing, packaging/labeling, contents and emissions of tobacco products, and smoking, the JT Group expects regulations like the above and various new regulations will be spread across Japan and other countries.

Regulation in Japan

The Tobacco Business Act, related acts and statutes, and voluntary standards set forth the regulations for the sale and promotion activities of tobacco products in Japan that include the indication of warning labels on tobacco product advertisements and packages that urge caution over the relationship between the consumption of tobacco products and health.

In November 2003, the Ordinance for Enforcement of the Tobacco Business Act was revised including the wording of the cautions over the relationship between the consumption of tobacco products and health indicated on tobacco product packages and, starting July 2005, all tobacco products sold in Japan have been in conformity to the revised regulations. In addition, the Japanese Minister of Finance has indicated a "Guideline for Advertising of Tobacco Products" based on the Tobacco Business Act which, in March 2004, was revised with tougher language. The Tobacco Institute of Japan has established voluntary standards regarding the advertising and sales promotion activities for tobacco products. All member companies, including JT, comply with these standards. In December 2018, the Tobacco Business Subcommittee of the Fiscal System Council of the Ministry of Finance compiled a report entitled "Revision of Restrictions on Cautionary Statements and Advertising Regulations." According to these guidelines, it is appropriate to completely switch to a new labeling method by July 1, 2020, such as by adding and revising the wording of the cautions based on the latest scientific findings and expanding the area of the wording for the cautions to 50% or more of tobacco product packages. Regarding advertising regulations, the industry is required to revise voluntary standards based on the Advertising Guidelines, which will be reviewed in the future. For example, the industry is required to take more effective measures to prevent Internet advertising from targeting minors, and to impose new restrictions on the size and methods of posting in-store advertising. We intend to comply with the industry's uniform standards in the future.

Furthermore, from the perspective of preventing passive smoking, the Health Promotion Act was amended in July 2018, and will be enforced in stages by April 2020. Despite the exceptional measures for eating and drinking establishments, the number of facilities that apply full smoking cessation may increase at the discretion of facility managers. In addition, an increasing number of municipalities have established their own ordinances to prevent passive smoking, and we expect these trends to continue in the future.

Tobacco Business Act

Importers and wholesalers of tobacco products must register with the Minister of Finance and, retailers of tobacco products must obtain the license of the Minister of Finance. The retailers of tobacco products are required to sell the tobacco products manufactured by JT and imported tobacco products at the fixed retail price which is approved by the Minister of Finance. The Minister of Finance must approve the filed retail sales prices unless otherwise considered unfairly prejudicial to consumers. The Tobacco Business Act requires JT to annually enter into purchase contracts with tobacco growers regarding the aggregate cultivation area for specific varieties of leaf tobacco and the prices for leaf tobacco by variety and grade. JT must purchase all leaf tobacco produced pursuant to such contracts, except for any not suited for the manufacture of tobacco products. When JT decides the aggregate cultivation area and the prices of leaf tobacco for its contracts with tobacco growers, it is required to respect the opinion of the Leaf Tobacco Deliberative Council *(hatabako shingi kai)*, which consists of members appointed by JT with the approval of the Minister of Finance from among the representatives of domestic leaf tobacco growers and academic appointees. Much like many other agricultural products in Japan, production costs for domestically grown leaf tobacco are higher than those of foreign-grown leaf tobacco to the extent that the purchasing price for the former (before re-drying) is approximately three times that of the latter (after re-drying).

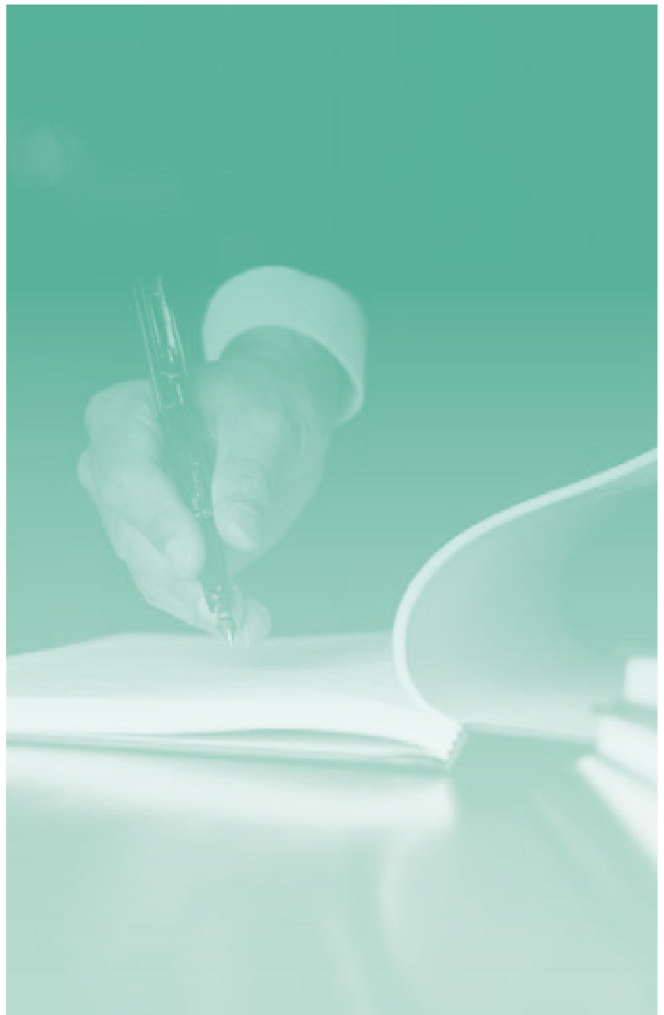
In November 2003, the Ordinance for Enforcement of the Tobacco Business Act was revised and the wording of warnings concerning tobacco consumption and health indicated on the tobacco product package was changed. In addition, the Ordinance stipulated that when wording like "mild" and "light" is used on the package, they must be accompanied by a warning that clarifies that such words do not mean that the risk to their health is lower than other tobacco products so as to prevent consumers from misunderstanding the relationship between the consumption of tobacco products and health. JT has been adhering to this rule since July 1, 2005.

Self-regulation on Marketing

JT Global Marketing Principles

The JT Group complies with all regulations of the respective countries in which we operate. At the same time, we pursue our business based on the "JT Global Marketing Principles (the Principles)". The Principles place importance on responsible marketing of tobacco products and outline our thoughts on advertising and promotions or health warnings, among others. Moreover, we recognize that youth smoking prevention is an issue which must be addressed by society as a whole. Based on the Principles, we govern our business and marketing activities, while working with government and other relevant organizations to take steps towards preventing youth smoking.

For further details, please refer to the JT websites:
https://www.jt.com/about/division/tobacco/marketing/



Pharmaceutical Business

The pharmaceutical industry operates in a highly regulated environment. In many countries, R&D, manufacturing and sales promotion activities are strictly regulated. Moreover, in recent years, the approval process for new drugs has been tightening due to the increased requirements to promote public health and safety. Compared with the past, pharmaceutical companies are now required to spend more time examining pharmaceutical safety issues and conducting a greater number of clinical trials on subjects to collect more data on the efficacy of new compounds. Consequently, clinical trials are growing in scale, cost and time. Meanwhile, the standards governing the reliability and quantity of research data have been globally harmonized, creating a more efficient and reasonable development process that allows data to be utilized internationally.

In Japan, the marketing of pharmaceutical products is subject to the supervision of the Ministry of Health, Labor and Welfare, or MHLW, primarily under the Act on Securing Quality, Efficacy and Safety of Pharmaceuticals, Medical Devices, Regenerative and Cellular Therapy Products, Gene Therapy Products, and Cosmetics, while part of its supervisory authority is undertaken by the relevant prefecture. Under the act, in order to conduct the marketing business of pharmaceuticals, a person is required to obtain from the relevant prefecture a renewable, generally five-year marketing business license. In addition, under the act, in order to market pharmaceuticals, it is necessary to obtain marketing approval from the MHLW for each kind of product.

The national health insurance system covers virtually the entire Japanese population. To sell a pharmaceutical product in Japan, a marketing business license holder of pharmaceutical products must first have a new pharmaceutical product listed on the National Health Insurance Pharmaceutical Price List for coverage under the national health insurance system. The drug pricing reform package would then apply, which includes mandating annual drug price revisions, limiting the number of price maintenance premium drugs and requiring a price reduction of long-listed drugs according to replacement rate.

Processed Food Business

As a producer and seller of food products, the JT Group's processed food business is subject to regulations mainly under the Food Safety Basic Act, the Food Sanitation Act and the Food Labeling Act.

The Food Safety Basic Act requires food-related companies to take necessary measures to ensure food safety in each process of the supply chain, as well as to make efforts to provide accurate information about foods and food-related goods in an appropriate manner.

The Food Sanitation Act concentrates on prevention of sanitary problems arising from consumption of food and beverages. This Act requires food companies to take necessary measures under their own responsibility to ensure the safety of food, additives, appliances and packages. The measures discussed in the Act include the acquisition of knowledge and skills, assurance of the safety of raw materials and voluntary inspection. The Food Labeling Act sets the standards for the labeling of food that is intended for sale and defines the labeling requirements such as allergens, expiration date, materials or origin. Persons and others engaged in food-related business must comply with the standards in preparing their product labels.

The JT Group is striving to establish a high level of food safety control from the above-mentioned four perspectives – "food safety," "food defense," "food quality" and "food communication" – in addition to complying with these laws and regulations and ensuring thorough awareness about them.

JT and/or some of its subsidiaries are defendants in lawsuits filed by plaintiffs seeking damages for harm allegedly caused by smoking, the marketing of tobacco products, or exposure to tobacco smoke. As of the fiscal year-end date, there were a total of 21 smoking and health-related cases pending in which one or more members of the JT Group were named as a defendant or for which JT may have certain indemnity obligations pursuant to the agreement such as for JT's acquisition of RJR Nabisco Inc.'s overseas (non-U.S.) tobacco operations. We believe it is possible that other similar smoking and health-related lawsuits may be filed in the future.

In addition, JT and some of its subsidiaries are also defendants in lawsuits other than the smoking and health-related cases. Please refer to the consolidated financial statements (Contingencies – Contingent Liabilities) for major lawsuits to which JT and some of its subsidiaries are named as defendants. Similar lawsuits involving us may be filed and contested in courts in the future.

To date, we have never lost a case or paid any settlement award in connection with smoking and health-related litigation. However, we are unable to predict the outcome of currently pending or future lawsuits. If a court ruling is unfavorable for us, in such cases whether lawsuits are smoking and health related or not, our financial results, production, sales and imports/exports of tobacco products may be adversely affected.

As of the fiscal year-end date, there are 10 ongoing health-care cost recovery cases in Canada pending against JTI-Macdonald Corp. and JT's indemnitees (RJR Nabisco Inc.'s affiliates), brought by Canadian provinces. In addition, there are 8 pending class actions in Canada, of which 6 are currently dormant, where plaintiffs are seeking damages for harm allegedly caused by smoking of cigarettes. Damages claimed in some of these cases reach sums in the multi-billion dollar range. We will continue to take all appropriate actions to defend such claims vigorously, and believe there are a number of valid defenses.

In recent decades, numerous, large-scale, smoking and health-related cases have been brought against tobacco product manufacturers in the USA, and some of the cases initially resulted in verdicts with massive damage awards. JT and its subsidiaries are not defendants in any of these lawsuits, nor are they subject to any indemnity claims with respect to them. The tobacco business which JT acquired from RJR Nabisco Inc. in 1999 and the Natural American Spirit business which JT acquired from the Reynolds American Inc. group of companies in January 2016 did not include brands in the USA, and even now, our historic and current tobacco business scale in the USA remains small. Accordingly, we consider potential exposure to smoking and health-related litigation in the USA to be low, and we thus believe that litigation in the USA will not materially affect our businesses in the near future.

Following the 2015 acquisition of Logic Technology Development LLC, JT Group operates an e-cigarette business in the USA. We are not aware of any related ongoing litigation alleging chronic effects on health associated with e-cigarette use. However, cases were filed against e-cigarette manufacturers in the USA alleging harm caused to consumers by misleading representations and advertising for which plaintiffs are seeking damages and/or demanding health warnings. Neither JT nor any of its subsidiaries are a party to these cases as of December 31, 2018.

As a tobacco product manufacturer, we continue to monitor closely the developments and trends of litigation involving tobacco companies in the USA, Canada, and elsewhere, with particular interest and attention.

As of March 20, 2019

The Board of Directors

Chairman of the Board

Yasutake Tango

Representative Directors

Masamichi Terabatake

Mutsuo Iwai

Naohiro Minami

Kiyohide Hirowatari

Directors

Kazuhito Yamashita

Main Kohda*

Koichiro Watanabe*

Yukiko Nagashima*

* Outside Directors under the Companies Act of Japan.

The Audit & Supervisory Board

Standing Audit & Supervisory Board Members

Ryoko Nagata

Hiroshi Yamamoto

Toru Mimura**

Audit & Supervisory Board Members

Hiroshi Obayashi**

Koji Yoshikuni**

** Outside Audit & Supervisory Board Members under the Companies Act of Japan.

Executive Officers

President

Masamichi Terabatake
Chief Executive Officer

Executive Vice Presidents

Mutsuo Iwai
President, Tobacco Business

Naohiro Minami
Chief Financial Officer and Communications

Kiyohide Hirowatari
Legal, Corporate Strategy, Digitalization, Human Resources, Operation Review & Business Assurance, Pharmaceutical Business and Food Business

Senior Vice Presidents

Kazuhito Yamashita
Compliance, Sustainability Management and General Affairs

Chito Sasaki
President, Japanese Domestic Tobacco Business, Tobacco Business

Junichi Fukuchi
Tobacco Business Planning, Corporate, Scientific & Regulatory Affairs, Tobacco Business

Eiichi Kiyokawa
Sales, Tobacco Business

Senior Vice Presidents

Kenji Ogura
Leaf Procurement, Tobacco Business

Hiroyuki Ikuma
Quality Assurance, Tobacco Business

Yasuhiro Nakajima
RRP Development, Tobacco Business

Shuichi Hirosue
Marketing, Tobacco Business

Hiroyuki Miki
R&D, Tobacco Business

Akihiro Koyanagi
Manufacturing, Tobacco Business

Toru Oguchi
Head of China Division, Tobacco Business

Muneaki Fujimoto
President, Pharmaceutical Business

Shigenori Ohkawa
Head of Central Pharmaceutical Research Institute, Pharmaceutical Business

Atsuhiro Kawamata
Food Business

Haruhiko Yamada
Legal

Yuki Maeda
Corporate Strategy

Takehiko Tsutsui
Business Development

Kei Nakano
Communications

Takehisa Shibayama
Digitalization

Takanori Kikuchi
General Affairs

Chigusa Ogawa
Sustainability Management

Koichi Mori
Human Resources

As of January 1, 2019

Eddy Pirard
President and Chief Executive Officer

Koji Shimayoshi
Deputy CEO and Executive Vice President, Business Development and Corporate Strategy

Roland Kostantos
Chief Operating Officer

Vassilis Vovos
Senior Vice President, Finance, IT, and Chief Financial Officer

Howard Parks
Senior Vice President, Human Resources and Chief Compliance Officer

Daniel Torras
Senior Vice President, Reduced-Risk Products

Suzanne Wise
Senior Vice President, Corporate Development

Wade Wright
Senior Vice President, Legal and Regulatory Affairs

Bilgehan Anlas
Regional President, Middle East, Near East, Africa, Turkey and Worldwide Duty-Free

Yves Barbier
Senior Vice President, Marketing and Sales

Antoine Ernst
Senior Vice President, Chief Transformation Officer

Stefan Fitz
Regional President, Western Europe

Marchant Kuys
Regional President, Americas

Hiroyuki Miki
Senior Vice President, Research and Development, Chief Quality Officer

Jorge da Motta
Regional President, Asia Pacific

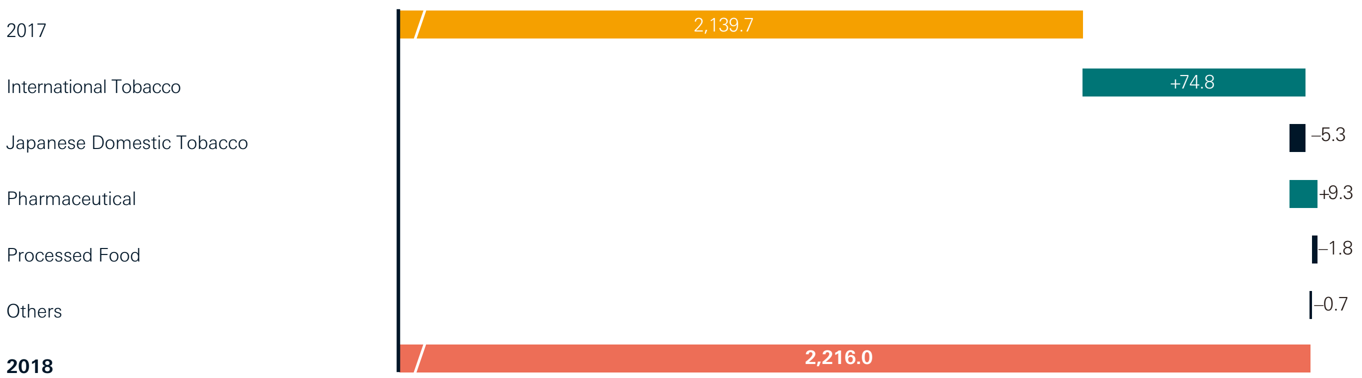
Andrew Newton
Senior Vice President, Global Supply Chain

Kevin Tomlinson
Regional President, Eastern Europe

Analysis of the Results

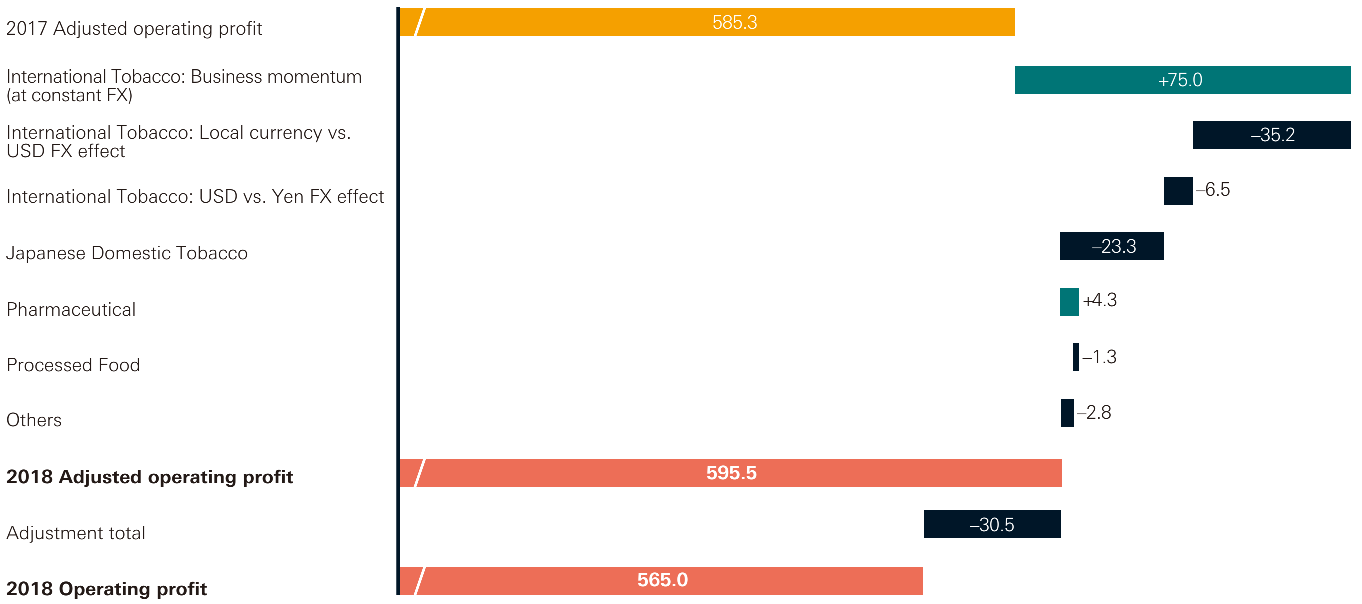
Results for the fiscal year ended December 31, 2018

Revenue[1] Billions of yen



- Revenue grew ¥76.3 billion or 3.6% year-on-year to ¥2,216.0 billion.
- Driven by pricing benefits and volume contribution led by acquisitions in the international tobacco business, as well as increased RRP contribution combined with a positive cigarette price/mix in the Japanese domestic tobacco business.
- An increase in royalty revenue in the pharmaceutical business also added to revenue growth.
- These benefits were partially offset by the negative currency movements caused by weaker emerging market currencies and the contraction of cigarette sales volume in the Japanese domestic tobacco business.

Adjusted Operating Profit[2]/Operating Profit Billions of yen



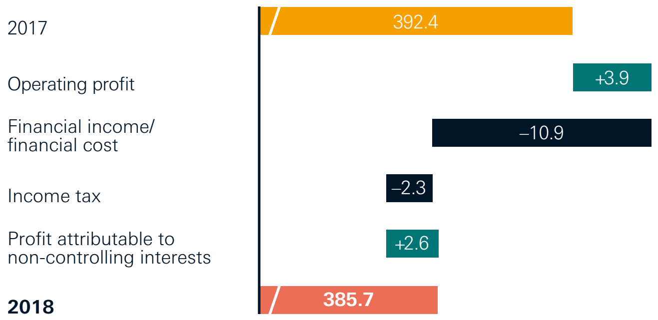
Adjusted operating profit increased ¥10.2 billion or 1.7% year-on-year to ¥595.5 billion.

- In the international tobacco business, adjusted operating profit, both including or excluding the impact of the one-time loss in the previous year, increased driven by revenue growth despite negative currency movements and investments to strengthen the business in the markets where we made acquisitions.
- In the Japanese domestic tobacco business, adjusted operating profit declined due to the negative cigarette volume contribution and increase of sales promotion expenses, partially offset by an increase in RRP-related profit, and a favorable cigarette price/mix variance.
- In the pharmaceutical business, despite increased R&D investment, adjusted operating profit grew, driven by the revenue growth.

Adjusted operating profit at constant foreign currency increased 8.9% year-on-year.

Operating profit increased 0.7% year-on-year to ¥565.0 billion driven by growth in adjusted operating profit and increase in the sale of real estate-related assets. This was despite an increase in trademark amortization expenses related to acquisitions.

Profit[3] Billions of yen



Profit decreased ¥6.7 billion or 1.7% year-on-year to ¥385.7 billion.

- Financial costs increased (reducing profit in the graph) mainly due to foreign exchange loss caused by weaker emerging market currencies and the increase of interest expenses resulted from funding acquisitions.
- Income tax expenses increased (reducing profit in the graph) due to growth in profit before income tax.

Revenue by Business Segment

Billions of yen	2017	2018
Revenue	2,139.7	**2,216.0**
International Tobacco	1,237.6	**1,312.3**
Core revenue[4]	1,177.0	**1,250.7**
Japanese Domestic Tobacco	626.8	**621.4**
Core revenue[5]	590.6	**582.4**
Pharmaceutical	104.7	**114.0**
Processed Food	163.1	**161.4**
Others	7.5	**6.8**

Average Exchange Rate

	2017	2018
USD/JPY	112.16	**110.44**
USD/RUB	58.35	**62.68**
USD/GBP	0.78	**0.75**
USD/EUR	0.89	**0.85**

Adjusted Operating Profit and Operating Profit by Business Segment

Billions of yen	2017	2018
Consolidated: Operating profit	561.1	**565.0**
International Tobacco	325.6	**339.5**
Japanese Domestic Tobacco	215.8	**192.5**
Pharmaceutical	24.1	**26.3**
Processed Food	5.4	**2.9**
Others/Elimination	(9.8)	**3.8**
Adjustments, total[6]	(24.2)	**(30.5)**
International Tobacco	(25.7)	**(45.0)**
Japanese Domestic Tobacco	(16.4)	**(16.5)**
Pharmaceutical	—	**(2.1)**
Processed Food	0.0	**(1.2)**
Others/Elimination	18.0	**34.4**
Consolidated: Adjusted operating profit	585.3	**595.5**
International Tobacco	351.3	**384.5**
Japanese Domestic Tobacco	232.3	**209.0**
Pharmaceutical	24.1	**28.4**
Processed Food	5.4	**4.1**
Others/Elimination	(27.8)	**(30.6)**

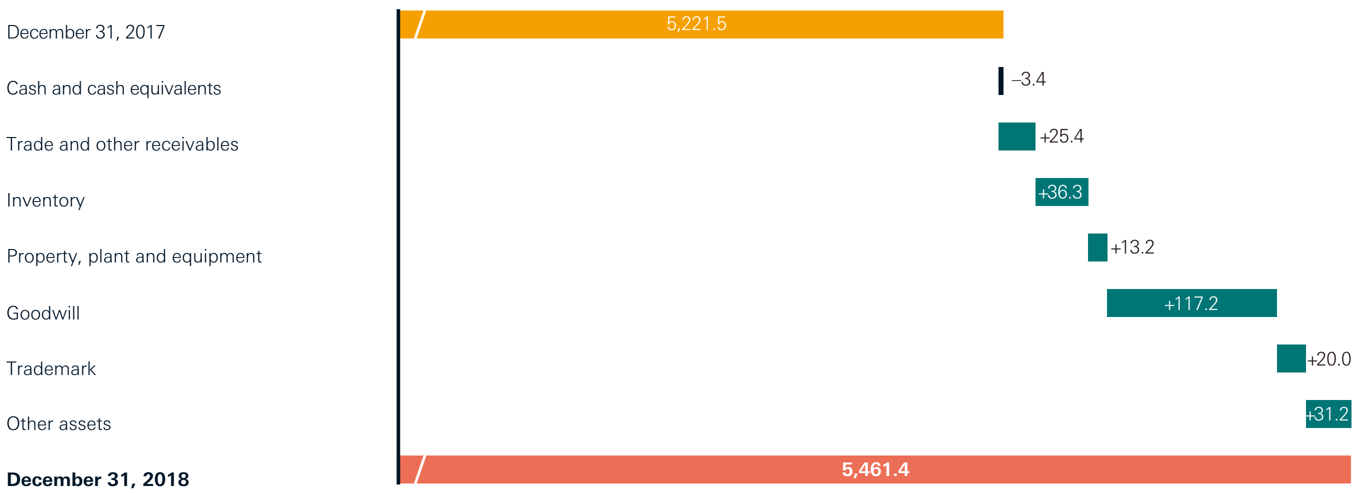
- For analysis of revenue, core revenue and adjusted operating profit of each business segment, please refer to the "Review of Operations."

1. Excludes tobacco excise taxes and agency transactions. In addition, from 2018, in accordance with the application of IFRS 15, certain items formerly treated as selling, general and administrative expenses are accounted for as reductions of revenue.
2. Adjusted operating profit = Operating profit + amortization cost of acquired intangibles arising from business acquisitions + adjusted items (income and costs).*
3. Profit attributable to owners of the parent
4. Excludes revenues from distribution, contract manufacturing and other peripheral businesses, but includes revenue from waterpipe tobacco and RRP.
5. Excludes revenue from distribution of imported tobacco in the Japanese domestic tobacco business, among other factors, but includes revenue from domestic duty free and the China business, as well as RRP-related revenue.
6. Amortization cost of acquired intangibles arising from business acquisitions ± adjusted items (income and costs).*
* Adjusted items (income and costs) = Impairment losses on goodwill ± restructuring income and costs ± others

Analysis of the Results

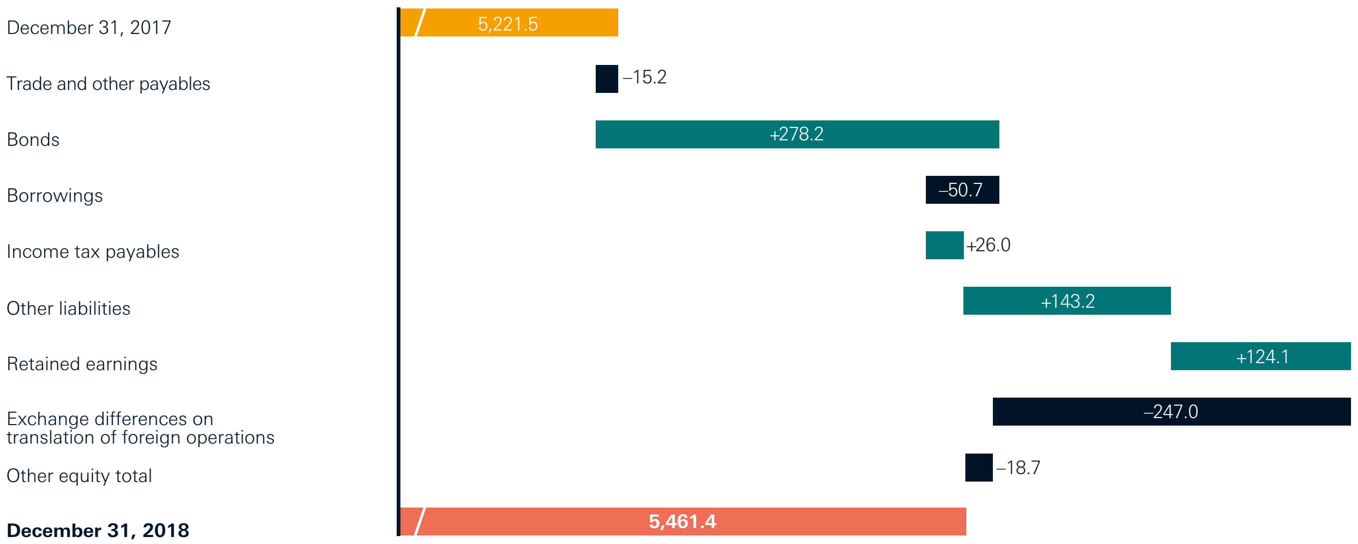
Results for the fiscal year ended December 31, 2018

Consolidated Statement of Financial Position (Assets) — Billions of yen



Total assets increased ¥239.9 billion to ¥5,461.4 billion, mainly due to the increase in goodwill, trademark and other assets, which is related to the acquisitions in the international tobacco business.

Consolidated Statement of Financial Position (Debt and Equity) — Billions of yen



Total liabilities increased ¥381.5 billion to ¥2,761.0 billion mainly due to an increase in bonds to fund acquisitions in the international tobacco business.

Total equity decreased ¥141.6 billion to ¥2,700.4 billion mainly because of a decrease in the exchange differences on translation of foreign operations.

1. Significant Accounting Policies

Having acquired RJR Nabisco's non-U.S. tobacco operation in 1999 and Gallaher Group Plc in the UK in 2007, the JT Group has been growing steadily as a global company with operations in more than 70 countries and products sold in more than 130 countries and regions around the world. In this context, the JT Group has adopted IFRS from the year ended March 31, 2012 to improve international comparability of financial information in capital markets and to diversify the Group's sources of financing through international capital markets.

From 2018, in accordance with the application of IFRS 15, certain items formerly treated as selling, general and administrative expenses are accounted for as reductions of revenue or cost of sales.

For further details of significant accounting policies, please refer to Note 3 to the consolidated financial statements.

2. Non-GAAP Financial Measures

The JT Group discloses certain additional financial measures that are not required or defined under IFRS. These measures help grasp the underlying performance of each business and are used for internal performance management. We believe that they are useful information for users of our financial statements to assess the Group's performance.

For our international tobacco business, its consolidated financial statements reported in US dollars are internally reviewed and therefore revenue and adjusted operating profit are externally communicated in US dollars. These non-GAAP financial measures should be treated as supplementary information, rather than alternative measures to corresponding financial numbers prepared in accordance with IFRS.

Core revenue

For the tobacco business, core revenue is disclosed additionally as a breakdown of revenue. Specifically, the core revenue for the Japanese domestic tobacco business excludes revenue from distribution of imported tobacco, among other factors, but includes revenue from domestic duty free and the China business, as well as RRP related revenue.

Core revenue for the international tobacco business excludes the revenue from distribution, contract manufacturing and other peripheral businesses, but includes revenue from waterpipe tobacco and RRP.

Adjusted operating profit

In order to provide useful comparative information on our business performance, adjusted operating profit is presented as operating profit plus amortization cost of acquired intangibles arising from business acquisitions and adjusted items (income and costs). Adjusted items (income and costs) are impairment losses on goodwill and restructuring income and costs, and other items.

Furthermore, for the international tobacco business, adjusted operating profit at constant rates of exchange which excludes foreign exchange effects, is also presented as additional information. Adjusted operating profit at constant exchange rate for a relevant period in the international tobacco business is calculated using the foreign exchange rates of the prior year.

3. Analysis of Consolidated Financial Results for 2018

For analysis of 'Revenue', 'Adjusted operating profit', 'Operating profit' and 'Profit attributable to owners of the parent company' from continuing operations, please refer to pages 70 and 71. For analysis of 'Assets', 'Debt' and 'Equity', please refer to page 72. For analysis of financial results by business segment, please refer to 'Review of Operations'.

Results and plans of capital expenditures

Capital expenditures include outlays on property, plant and equipment such as land, buildings, and structures; machinery; vehicles and others; and intangible assets such as goodwill, trademark, software, and others that are necessary for enhancing the productivity of our factories and other facilities; strengthening our competitiveness, and operating in various business fields.

In 2018, total capital expenditures amounted to ¥159.8 billion.

Capital Expenditure — Billions of yen

	2017	2018
Total	140.9	**159.8**
International Tobacco	68.4	**75.7**
Japanese Domestic Tobacco	51.5	**55.4**
Pharmaceutical	6.2	**11.3**
Processed Food	10.4	**12.7**
Others/Elimination	4.3	**4.6**

In the international tobacco business, capital expenditures amounted to ¥75.7 billion which was spent on factory manufacturing facilities. In the Japanese domestic tobacco business, capital expenditures amounted to ¥55.4 billion which was mainly spent on the RRP-related manufacturing facilities. In the pharmaceutical business, capital expenditures amounted to ¥11.3 billion which was primarily spent on the construction of a joint facility of Toxicology Research Laboratories and Pharmaceutical Frontier Research Laboratories. In the processed food business, capital expenditures amounted to ¥12.7 billion, which was spent on constructing new buildings and facilities to enhance and maintain production capacity and the optimal production system. These capital expenditures were internally funded through cash generated by operations and borrowings.

Plans for new installations and disposal of facilities

Regarding the mid- to long-term resource allocation of the JT Group, we will place top priority on business investments that will lead to sustainable profit growth in the mid- to long-term based on our management principles. We position the international tobacco and Japanese domestic tobacco as the core business and profit growth engines, and place top priority on business investments that will lead to their sustainable profit growth. Meanwhile, regarding the pharmaceutical business and processed food business, we will strive to strengthen foundations that will lead to future profit contribution, and we will make investments to that end. Based on this policy, we plan capital expenditures totaling ¥156.0 billion for 2019.

As JT and the JT Group companies have wide-ranging plans for capital expenditure, figures are disclosed by segment. Our actual capital expenditures may differ significantly from the planned figures mentioned above as a result of a number of factors, including those discussed in 'Risk Factors'.

4. Dividends

The year-end dividends for 2018 were ¥75 per share. The total annual dividends per share, including the interim dividends per share of ¥75, were ¥150 per share, with a ¥10 increase of dividend per share year-on-year.

The year-end dividends related to the current year are recognized in the following year for accounting purposes.

The year-end dividend related to 2017 (record date of December 31, 2017) and the interim dividends for 2018 (record date of June 30, 2018) are recorded in the financial statements for 2018. For more details, please refer to Note 24 to the consolidated financial statements "Dividends".

5. Capital Management

The JT Group's management principle is pursuit of the 4S model: we strive to fulfill our responsibilities to our valued consumers, shareholders, employees and the wider society, carefully considering the respective interests of these four key stakeholder groups, and exceeding their expectations wherever we can. The JT Group believes that sustainable profit growth in the mid- to long-term based on this principle will increase the JT Group's value in the mid- to long-term, and is consequently in the best interest of all stakeholders, including our shareholders.

As its financial policy, the JT Group maintains a solid balance sheet. This provides the capacity to withstand any adversity arising out of a volatile environment, such as an economic crisis. It also allows for sufficient flexibility to capture attractive investment opportunities. The JT Group monitors financial indicators in order to maintain a well-balanced capital structure that ensures an appropriate return on equity and a solid balance sheet for future investment. We monitor credit ratings for a solid balance sheet, and ROE (return on equity) for profitability, while focusing on changes in the domestic and overseas environment.

The JT Group manages net interest-bearing debt, where cash and cash equivalents are deducted from interest-bearing debt, and capital (the part attributable to owners of the parent company). The amounts as of each year-end are as follows:

Capital Management

	Billions of yen	
	As of Dec. 31, 2017	**As of Dec. 31, 2018**
Interest-bearing debt	755.8	**987.6**
Cash and cash equivalents	(285.5)	**(282.1)**
Net interest-bearing debt	470.3	**705.5**
Capital (equity attributable to owners of the parent company)	2,761.7	**2,630.6**

Capital Expenditure Plan

	2019 (Billions of yen)	Main purpose of investing	Funding
International Tobacco	80.0	RRP-related investment and improvement in product specifications	Internally funded
Japanese Domestic Tobacco	57.0	RRP- and IT-related investment	Same as above
Pharmaceutical	5.0	Maintenance and reinforcement of R&D	Same as above
Processed Food	8.0	Facility investment for optimal production system	Same as above

Share buy-back

As of December 31, 2018 JT held 208,576,641 common shares as treasury stock, amounting to 10.43% of the total number of shares issued.

A repurchase of our shares requires cash outlays. In order to repurchase our shares in a flexible manner, we amended the Articles of Incorporation at the general meeting of shareholders held on June 24, 2004 so that JT could repurchase shares based on a resolution made by the Board of Directors. We may continue to hold the repurchased shares as treasury stock or use them for other purposes. Stock repurchase provides our management with an additional option for increasing flexibility and speed in capital management in order to adopt to a rapidly changing business environment.

In addition, the JT Group announced a share buyback program of up to ¥50 billion or 23 million shares, based on the resolution made by the Board of Directors on February 7, 2019. The buyback program will be from February 8, 2019 to April 22, 2019 by purchase on the stock exchange via trust bank.

6. Financial Activities

Our Group Treasury Division provides Group-wide support to enable secure and efficient financing activities. The JT Group is exposed to financial risks (credit risks, liquidity risks, foreign exchange risks, interest rate risks, and market price fluctuation risks). Treasury operations are conducted pursuant to a set of Group-wide financial risk management policies and results are reported to the CEO and the Board of Directors of JT on a regular basis. For more details on financial risk management, please refer to "(2) Financial Risk Management" and to "(8) Market Price Fluctuation Risk" of Note 34 to the consolidated financial statements "Financial Instruments".

Cash Management Systems

To maximize the Group's overall cash efficiency, we give first priority to utilizing internal financing mainly by the Cash Management Systems (CMS) within our Group, where legally permissible and economically viable.

External financing

Short-term working capital needs are basically financed through short-term borrowings from financial institutions or through commercial paper, or a combination of both. Mid- to long-term capital needs are financed through long-term borrowings from financial institutions, bonds, equity, or a combination of those previously stated.

We continue to diversify our financing methods and correspondent financial institutions to secure stable and efficient funding sources through activities such as the establishment of committed facilities. The condition of Group-wide external debt is reported to the CEO and the Board of Directors of JT on a regular basis.

External investments

Our financial investments are always made taking into account safety, liquidity and optimal yield. Speculative dealings in pursuit of profit margin are not allowed. The results of the financial investment are reported to the CEO and the Board of Directors of JT on a regular basis.

7. Results of Cash Flows of 2018 and 2017

Cash and cash equivalents at the end of 2018 decreased by ¥3.4 billion from the end of 2017 to ¥282.1 billion. Cash and cash equivalents at the end of 2017 were ¥285.5 billion.

Cash flows from (used in) operating activities

Net cash flows from operating activities during 2018 were ¥461.4 billion. The main factors were the generation of a stable cash inflow from the tobacco business. Net cash flows from operating activities were ¥419.2 billion for 2017.

Cash flows from (used in) investing activities

Net cash flows used in investing activities during 2018 were ¥383.3 billion. This was mainly due to the acquisitions and an increase in property, plant and equipment in Russia and Bangladesh in the international tobacco business. Net cash flows used in investing activities were ¥352.6 billion for 2017.

Cash flows from (used in) financing activities

Net cash flows used in financing activities during 2018 were ¥62.4 billion. Bonds issued in 2018 partially offset the increase in dividends per share and repayments of borrowings. Net cash flows used in financing activities were ¥77.0 billion for 2017.

8. Liquidity

We have historically had, and expect to continue to have, significant cash flows from operating activities. We expect that cash generated from operating activities will continue to be stable and cover funds needed for ordinary business activities. On December 31, 2018, we had approximately ¥478.5 billion committed facilities for both domestic and international major financial institutions, of which 100% was unused. In addition, we have a domestic commercial paper program, uncommitted facilities, a domestic bond shelf registration and EMTN program.

Long-term debt

Bonds issued (including the current portion) as of December 31, 2017 and December 31, 2018 accounted for ¥332.2 billion and ¥610.4 billion respectively and long-term borrowings as loans from financial institutions (including the current portion) accounted for ¥71.9 billion and ¥129.3 billion respectively. Long-term lease obligations accounted for ¥9.3 billion as of December 31, 2017 and ¥8.8 billion as of December 31, 2018. Maturities of interest bearing debts are shown in the table below.

As of December 31, 2018, our long-term debt was rated Aa3 by Moody's Japan K.K. (Moody's), AA- by Standard & Poor's Ratings Japan K.K. (S&P), and AA by Rating and Investment Information Inc. (R&I), with a "negative" outlook from Moody's, a "negative" outlook from S&P and a "stable" outlook from R&I.

These ratings are affected by a number of factors such as developments in our major markets, our business strategies and general economic trends that are beyond control.
The ratings may be withdrawn or revised at any time.
Each rating should be evaluated separately from other ratings. Under the Japan Tobacco Inc. Act, the bondholders of JT can enjoy statutory preferential rights over unsecured creditors in seeking repayment, with the exception of national and local taxes and other statutory obligations.

Short-term debt

Short-term borrowings totaled ¥274.2 billion as of December 31, 2017 and ¥166.0 billion as of December 31, 2018. Commercial paper totaled ¥72.0 billion as of December 31, 2018.

Short-term lease obligations totaled ¥1.3 billion as of December 31, 2017 and ¥1.0 billion as of December 31, 2018.

Liquidity

Billions of yen

Year ended December 31, 2018	Book Value	Due within 1 year	Due after 1 year through 2 years	Due after 2 years through 3 years	Due after 3 years through 4 years	Due after 4 years through 5 years	Due after 5 years
Short-term borrowings as loans	166.0	166.0	—	—	—	—	—
Short-term lease obligations	1.0	1.0	—	—	—	—	—
Commercial paper	72.0	72.2	—	—	—	—	—
Long-term borrowings as loans (current portion)	12.4	12.4	—	—	—	—	—
Long-term borrowings as loans	116.9	—	12.0	11.6	41.6	11.6	40.3
Bonds	610.4	—	80.0	83.3	30.0	118.3	302.2
Long-term lease obligations	8.8	—	0.8	0.7	0.4	0.2	6.7
Total	**987.6**	**251.6**	**92.8**	**95.5**	**72.0**	**130.0**	**349.2**

Consolidated Statement of Financial Position

Japan Tobacco Inc. and Consolidated Subsidiaries
As of December 31, 2017 and 2018

		Millions of yen
Assets	2017	2018
Current assets		
Cash and cash equivalents (Note 7)	¥ 285,486	**¥ 282,063**
Trade and other receivables (Note 8)	431,199	**456,591**
Inventories (Note 9)	612,954	**649,238**
Other financial assets (Note 10)	14,016	**35,633**
Other current assets (Note 11)	361,715	**385,872**
Subtotal	1,705,370	**1,809,396**
Non-current assets held-for-sale (Note 12)	2,396	**10**
Total current assets	1,707,767	**1,809,406**
Non-current assets		
Property, plant and equipment (Note 13)	745,607	**758,841**
Goodwill (Notes 14, 38)	1,891,210	**2,008,416**
Intangible assets (Note 14)	479,175	**503,076**
Investment property (Note 16)	16,700	**17,558**
Retirement benefit assets(Note 22)	51,377	**57,140**
Investments accounted for using the equity method	81,253	**66,807**
Other financial assets (Note 10)	114,970	**115,046**
Deferred tax assets (Note 17)	133,425	**125,109**
Total non-current assets	3,513,717	**3,651,993**
Total assets	¥5,221,484	**¥5,461,400**

		Millions of yen
Liabilities and equity	2017	2018
Liabilities		
Current liabilities		
Trade and other payables (Note 18)	¥ 395,733	**¥ 380,516**
Bonds and borrowings (Note 19)	398,182	**250,466**
Income tax payables	46,452	**72,449**
Other financial liabilities (Note 19)	6,906	**4,486**
Provisions (Note 20)	13,028	**6,078**
Other current liabilities (Note 21)	618,322	**716,190**
Total current liabilities	1,478,623	**1,430,185**
Non-current liabilities		
Bonds and borrowings (Note 19)	346,955	**727,314**
Other financial liabilities (Note 19)	11,013	**10,067**
Retirement benefit liabilities (Note 22)	330,762	**321,838**
Provisions (Note 20)	4,005	**3,780**
Other non-current liabilities (Note 21)	120,779	**179,274**
Deferred tax liabilities (Note 17)	87,319	**88,497**
Total non-current liabilities	900,833	**1,330,770**
Total liabilities	2,379,456	**2,760,955**
Equity		
Share capital (Note 23)	100,000	**100,000**
Capital surplus (Note 23)	736,400	**736,400**
Treasury shares (Note 23)	(443,636)	**(442,829)**
Other components of equity (Note 23)	(167,338)	**(423,357)**
Retained earnings	2,536,262	**2,660,381**
Equity attributable to owners of the parent company	2,761,687	**2,630,594**
Non-controlling interests	80,340	**69,851**
Total equity	2,842,027	**2,700,445**
Total liabilities and equity	¥5,221,484	**¥5,461,400**

Consolidated Statement of Income

Japan Tobacco Inc. and Consolidated Subsidiaries
Years Ended December 31, 2017 and 2018

	Millions of yen	
	2017	2018
Revenue (Notes 6, 25)	¥2,139,653	**¥2,215,962**
Cost of sales (Notes 14, 22)	(843,558)	**(933,034)**
Gross profit	1,296,094	**1,282,928**
Other operating income (Note 26)	45,724	**48,532**
Share of profit in investments accounted for using the equity method	6,194	**3,931**
Selling, general and administrative expenses (Notes 12, 13, 14, 16, 22, 27, 33, 38)	(786,911)	**(770,407)**
Operating profit (Note 6)	561,101	**564,984**
Financial income (Notes 28, 34)	4,780	**5,754**
Financial costs (Notes 22, 28, 34)	(27,349)	**(39,252)**
Profit before income taxes	538,532	**531,486**
Income taxes (Note 17)	(141,783)	**(144,055)**
Profit for the period	¥ 396,749	**¥ 387,431**
Attributable to:		
Owners of the parent company	¥ 392,409	**¥ 385,677**
Non-controlling interests	4,340	**1,755**
Profit for the period	¥ 396,749	**¥ 387,431**
Earnings per share		
Basic (Yen) (Note 30)	¥ 219.10	**¥ 215.31**
Diluted (Yen) (Note 30)	218.97	**215.20**

Reconciliation from "Operating profit" to "Adjusted operating profit"

	Millions of yen	
	2017	2018
Operating profit	¥561,101	**¥564,984**
Amortization cost of acquired intangibles arising from business acquisitions	50,414	**61,772**
Adjustment items (income)	(37,569)	**(40,447)**
Adjustment items (costs)	11,354	**9,154**
Adjusted operating profit (Note 6)	¥585,300	**¥595,463**

Consolidated Statement of Comprehensive Income

Japan Tobacco Inc. and Consolidated Subsidiaries
Years Ended December 31, 2017 and 2018

	Millions of yen	
	2017	2018
Profit for the period	¥396,749	**¥387,431**
Other comprehensive income		
Items that will not be reclassified to profit or loss:		
Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income (Notes 29, 34)	9,402	**(8,215)**
Remeasurements of defined benefit plans (Notes 22, 29)	20,028	**(3,195)**
Total of items that will not be reclassified to profit or loss	29,430	**(11,410)**
Items that may be reclassified subsequently to profit or loss:		
Exchange differences on translation of foreign operations (Notes 29, 34)	128,073	**(247,731)**
Net gain (loss) on derivatives designated as cash flow hedges (Notes 29, 34)	(54)	**1,012**
Total of items that may be reclassified subsequently to profit or loss	128,019	**(246,719)**
Other comprehensive income (loss), net of taxes	157,449	**(258,129)**
Comprehensive income (loss) for the period	¥554,198	**¥129,302**
Attributable to:		
Owners of the parent company	¥549,309	**¥128,340**
Non-controlling interests	4,889	**962**
Comprehensive income (loss) for the period	¥554,198	**¥129,302**

Consolidated Statement of Changes in Equity

Japan Tobacco Inc. and Consolidated Subsidiaries
Years Ended December 31, 2017 and 2018

Millions of yen

	Equity attributable to owners of the parent company						
				Other components of equity			
	Share capital	Capital surplus	Treasury shares	Subscription rights to shares	Exchange differences on translation of foreign operations	Net gain (loss) on derivatives designated as cash flow hedges	Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income
As of January 1, 2017	¥100,000	¥736,400	¥(443,822)	¥1,794	¥(335,642)	¥ 440	¥29,854
Profit for the period	—	—	—	—	—	—	—
Other comprehensive income (loss)	—	—	—	—	127,758	(54)	9,276
Comprehensive income (loss) for the period	—	—	—	—	127,758	(54)	9,276
Acquisition of treasury shares (Note 23)	—	—	(1)	—	—	—	—
Disposal of treasury shares (Note 23)	—	—	187	(166)	—	—	—
Share-based payments (Note 33)	—	—	—	336	—	—	—
Dividends (Note 24)	—	—	—	—	—	—	—
Changes in the scope of consolidation	—	—	—	—	—	—	—
Changes in the ownership interest in a subsidiary without a loss of control	—	—	—	—	—	—	—
Transfer from other components of equity to retained earnings	—	—	—	—	—	—	(461)
Other increase (decrease)	—	—	—	—	—	(475)	—
Total transactions with the owners	—	—	186	170	—	(475)	(461)
As of December 31, 2017	100,000	736,400	(443,636)	1,964	(207,884)	(88)	38,670
Profit for the period	—	—	—	—	—	—	—
Other comprehensive income (loss)	—	—	—	—	(247,034)	1,012	(8,239)
Comprehensive income (loss) for the period	—	—	—	—	(247,034)	1,012	(8,239)
Acquisition of treasury shares (Note 23)	—	—	(0)	—	—	—	—
Disposal of treasury shares (Note 23)	—	—	807	(691)	—	—	—
Share-based payments (Note 33)	—	—	—	274	—	—	—
Dividends (Note 24)	—	—	—	—	—	—	—
Changes in the scope of consolidation	—	—	—	—	—	—	—
Changes in the ownership interest in a subsidiary without a loss of control	—	—	—	—	—	—	—
Transfer from other components of equity to retained earnings	—	—	—	—	—	—	(860)
Other increase (decrease)	—	—	—	—	—	(480)	—
Total transactions with the owners	—	—	807	(417)	—	(480)	(860)
As of December 31, 2018	**¥100,000**	**¥736,400**	**¥(442,829)**	**¥1,547**	**¥(454,918)**	**¥ 443**	**¥29,570**

Millions of yen

	Equity attributable to owners of the parent company					
	Other components of equity					
	Remeasurements of defined benefit plans	Total	Retained earnings	Total	Non-controlling interests	Total equity
As of January 1, 2017	¥ —	¥(303,554)	¥2,367,067	¥2,456,091	¥71,950	¥2,528,041
Profit for the period	—	—	392,409	392,409	4,340	396,749
Other comprehensive income (loss)	19,919	156,900	—	156,900	550	157,449
Comprehensive income (loss) for the period	19,919	156,900	392,409	549,309	4,889	554,198
Acquisition of treasury shares (Note 23)	—	—	—	(1)	—	(1)
Disposal of treasury shares (Note 23)	—	(166)	(21)	0	—	0
Share-based payments (Note 33)	—	336	—	336	5	341
Dividends (Note 24)	—	—	(243,572)	(243,572)	(1,547)	(245,119)
Changes in the scope of consolidation	—	—	—	—	4,884	4,884
Changes in the ownership interest in a subsidiary without a loss of control	—	—	(1)	(1)	159	158
Transfer from other components of equity to retained earnings	(19,919)	(20,380)	20,380	—	—	—
Other increase (decrease)	—	(475)	—	(475)	—	(475)
Total transactions with the owners	(19,919)	(20,684)	(223,214)	(243,713)	3,501	(240,212)
As of December 31, 2017	—	(167,338)	2,536,262	2,761,687	80,340	2,842,027
Profit for the period	—	—	385,677	385,677	1,755	387,431
Other comprehensive income (loss)	(3,075)	(257,337)	—	(257,337)	(792)	(258,129)
Comprehensive income (loss) for the period	(3,075)	(257,337)	385,677	128,340	962	129,302
Acquisition of treasury shares (Note 23)	—	—	—	(0)	—	(0)
Disposal of treasury shares (Note 23)	—	(691)	(116)	0	—	0
Share-based payments (Note 33)	—	274	2	275	36	311
Dividends (Note 24)	—	—	(259,724)	(259,724)	(1,914)	(261,638)
Changes in the scope of consolidation	—	—	—	—	139	139
Changes in the ownership interest in a subsidiary without a loss of control	—	—	495	495	(9,713)	(9,218)
Transfer from other components of equity to retained earnings	3,075	2,215	(2,215)	—	—	—
Other increase (decrease)	—	(480)	—	(480)	—	(480)
Total transactions with the owners	3,075	1,318	(261,558)	(259,433)	(11,452)	(270,885)
As of December 31, 2018	**¥ —**	**¥(423,357)**	**¥2,660,381**	**¥2,630,594**	**¥69,851**	**¥2,700,445**

Consolidated Statement of Cash Flows

Japan Tobacco Inc. and Consolidated Subsidiaries
Years Ended December 31, 2017 and 2018

	Millions of yen	
	2017	**2018**
Cash flows from operating activities		
Profit before income taxes	¥538,532	**¥531,486**
Depreciation and amortization	145,407	**158,671**
Impairment losses	3,427	**8,454**
Reversal of impairment losses on investments in associates	(8,848)	**—**
Interest and dividend income	(4,381)	**(5,751)**
Interest expense	11,604	**16,343**
Share of profit in investments accounted for using the equity method	(6,194)	**(3,931)**
(Gains) losses on sale and disposal of property, plant and equipment, intangible assets and investment property	(21,221)	**(34,905)**
(Increase) decrease in trade and other receivables	(28,810)	**(30,818)**
(Increase) decrease in inventories	(41,102)	**(53,058)**
Increase (decrease) in trade and other payables	15,655	**(4,618)**
Increase (decrease) in retirement benefit liabilities	(15,296)	**(8,864)**
(Increase) decrease in prepaid tobacco excise taxes	(10,281)	**(36,662)**
Increase (decrease) in tobacco excise tax payables	(60,250)	**53,408**
Increase (decrease) in consumption tax payables	1,117	**(11,026)**
Other	12,228	**8,969**
Subtotal	531,587	**587,697**
Interest and dividends received	11,250	**11,743**
Interest paid	(11,035)	**(13,685)**
Income taxes paid	(112,591)	**(124,366)**
Net cash flows from operating activities	419,212	**461,389**
Cash flows from investing activities		
Purchase of securities	(11,479)	**(36,705)**
Proceeds from sale and redemption of securities	4,893	**10,159**
Purchase of property, plant and equipment	(123,726)	**(138,605)**
Proceeds from sale of investment property	21,195	**46,868**
Purchase of intangible assets	(16,412)	**(20,205)**
Payments into time deposits	(84)	**(878)**
Proceeds from withdrawal of time deposits	101	**812**
Payments for business combinations (Note 38)	(212,707)	**(247,632)**
Purchase of investments in associates	(5,253)	**—**
Other	(9,160)	**2,878**
Net cash flows from investing activities	(352,632)	**(383,307)**
Cash flows from financing activities		
Dividends paid to owners of the parent company (Note 24)	(243,552)	**(259,671)**
Dividends paid to non-controlling interests	(1,502)	**(1,747)**
Capital contribution from non-controlling interests	15	**109**
Increase (decrease) in short-term borrowings and commercial paper (Note 32)	116,371	**(133,849)**
Proceeds from long-term borrowings (Note 32)	70,861	**59,135**
Repayments of long-term borrowings (Note 32)	(669)	**(2,710)**
Proceeds from issuance of bonds (Note 32)	—	**341,516**
Redemption of bonds (Note 32)	(20,000)	**(54,086)**
Proceeds from sale and leaseback transactions	2,819	**—**
Repayments of finance lease obligations (Note 32)	(1,373)	**(1,637)**
Acquisition of treasury shares	(1)	**(0)**
Payments for acquisition of interests in subsidiaries from non-controlling interests	—	**(9,421)**
Other	0	**0**
Net cash flows from financing activities	(77,032)	**(62,360)**
Net increase (decrease) in cash and cash equivalents	(10,452)	**15,721**
Cash and cash equivalents at the beginning of the period	294,157	**285,486**
Effect of exchange rate changes on cash and cash equivalents	1,782	**(19,145)**
Cash and cash equivalents at the end of the period (Note 7)	¥285,486	**¥282,063**

Notes to Consolidated Financial Statements

Japan Tobacco Inc. and Consolidated Subsidiaries
Years Ended December 31, 2017 and 2018

1. Reporting Entity

Japan Tobacco Inc. (hereinafter referred to as the "Company") is a joint stock corporation under the Companies Act of Japan, pursuant to the Japan Tobacco Inc. Act, with its principal places of business located in Japan since its incorporation. The addresses of the Company's registered head office and principal business offices are available on the Company's website (https://www.jt.com/).

The details of businesses and principal business activities of the Company and its subsidiaries (hereinafter referred to as the "Group") are stated in "6. Operating Segments."

The Group's consolidated financial statements for the year ended December 31, 2018 were approved on March 20, 2019 by Masamichi Terabatake, President and Chief Executive Officer.

2. Basis of Preparation

(1) Compliance with IFRS

The Group's consolidated financial statements are prepared in accordance with International Financial Reporting Standards (hereinafter referred to as "IFRS").

(2) Basis of Measurement

Except for the financial instruments, stated in "3. Significant Accounting Policies," the Group's consolidated financial statements are prepared on the historical cost basis.

(3) Functional Currency and Presentation Currency

The Group's consolidated financial statements are presented in Japanese yen, which is the functional currency of the Company. The units are in millions of yen, and figures less than one million yen are rounded to the nearest million yen.

3. Significant Accounting Policies

(1) Basis of Consolidation

The consolidated financial statements include financial statements of the Company and its subsidiaries, and interests in investments in associates and joint arrangements.

A. Subsidiaries

A subsidiary is an entity that is controlled by the Group and the Group has control over the entity if it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. The acquisition date of a subsidiary is the date on which the Group obtains control of the subsidiary, and the subsidiary is included in the consolidation from the date of acquisition until the date on which the Group loses control.

In cases where the accounting policies applied by a subsidiary are different from those applied by the Group, adjustments are made to the subsidiary's financial statements, if necessary.

All intergroup balances, transactions, income and expenses are eliminated on consolidation.

Comprehensive income for subsidiaries is attributed to owners of the parent company and non-controlling interests even if this results in the non-controlling interests having a deficit balance.

B. Associates

An associate is an entity over which the Group has significant influence. The Group has significant influence over the entity if it has the power to participate in the financial and operating policy decisions of the investee but it does not have control or joint control over the investee. Investments in associates are accounted for using the equity method from the date on which the Group has the significant influence until the date on which it ceases to have the significant influence.

C. Joint Arrangements

A joint arrangement is a contractual arrangement in which two or more parties have joint control. Depending upon the rights and obligations of the parties to the arrangement, the Group classifies a joint arrangement into a joint operation whereby the Group has rights to the assets and obligations for the liabilities relating to the arrangement, and a joint venture whereby the Group has rights to the net assets of the arrangement only. The Group recognizes the assets, liabilities, revenues and expenses relating to its interest in a joint operation while a joint venture is accounted for using the equity method.

(2) Business Combination

Business combinations are accounted for using the acquisition method. Consideration transferred in a business combination is measured as the sum of the acquisition-date fair value of the assets transferred, the liabilities assumed and equity instruments issued by the Company in exchange for control over an acquiree. Any excess of the consideration of acquisition over the fair value of identifiable assets and liabilities is recognized as goodwill in the consolidated statement of financial position. If the consideration of acquisition is lower than the fair value of the identifiable assets and liabilities, the difference is immediately recognized as profit in the consolidated statement of income. If the amount of initial accounting for a business combination is not determined by the end of the reporting period in which the combination occurs, the provisional amounts for the items for which the accounting is incomplete are reported and are adjusted during the measurement period, which is one year from the acquisition date. Acquisition-related costs incurred are recognized as expenses. The additional acquisition of non-controlling interests after obtaining control is accounted for as a capital transaction. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognized directly in retained earnings and no goodwill is recognized with respect to such transaction.

(3) Foreign Currency Translation

Consolidated financial statements of the Group are presented in Japanese yen, which is the functional currency of the Company. Each company in the Group specifies its own functional currency and measures transactions based on it.

Foreign currency transactions are translated into the functional currency at the rates of exchange prevailing at the dates of transactions or an approximation of the rate. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the rates of exchange prevailing at year end. Differences arising from the translation and settlement are recognized as profit or loss. However, exchange differences arising from the translation of financial instruments designated as hedging instruments for net investment in foreign operations (foreign subsidiaries), financial assets measured at fair value through other comprehensive income, and cash flow hedges are recognized as other comprehensive income.

The assets and liabilities of foreign operations are translated into Japanese yen at the rates of exchange prevailing at year end, while income and expenses of foreign operations are translated into Japanese yen at the rates of exchange prevailing at the dates of transactions or an approximation of the rate. The resulting translation differences are recognized as other comprehensive income. In cases where foreign operations are disposed of, the cumulative amount of translation differences related to the foreign operations is recognized as profit or loss in the period of disposition.

(4) Financial Instruments

A. Financial Assets

(i) Initial Recognition and Measurement

Financial assets are classified into financial assets measured at fair value through profit or loss, fair value through other comprehensive income, and amortized cost. The Group determines the classification at initial recognition.

Financial assets are classified as financial assets measured at amortized cost if both of the following conditions are met. Otherwise, they are classified as financial assets measured at fair value.

- The asset is held within a business model whose objective is to hold assets in order to collect contractual cash flows
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding

For financial assets measured at fair value, each equity instrument is designated as measured at fair value through profit or loss or as measured at fair value through other comprehensive income, except for equity instruments held for trading purposes that must be measured at fair value through profit or loss. Such designations are applied consistently.

All financial assets are measured at fair value plus transaction costs that are attributable to the financial assets, except for the case of being classified in the category of financial assets measured at fair value through profit or loss.

(ii) Subsequent Measurement

After initial recognition, financial assets are measured based on the following classifications:

(a) Financial Assets Measured at Amortized Cost

Financial assets measured at amortized cost are measured at amortized cost using the effective interest method.

(b) Other Financial Assets

Financial assets other than those measured at amortized cost are measured at fair value.

Changes in the fair value of financial assets measured at fair value are recognized as profit or loss.

However, changes in the fair value of equity instruments designated as measured at fair value through other comprehensive income are recognized as other comprehensive income and the amount in other comprehensive income is transferred to retained earnings when equity instruments are derecognized or the decline in its fair value compared to its acquisition cost is significant. Dividends on the financial assets are recognized in profit or loss for the year.

(iii) Derecognition

Financial assets are derecognized when the rights to receive benefits from them expire or are transferred, or when substantially all the risks and rewards of the ownership are transferred.

B. Impairment of Financial Assets

With respect to financial assets measured at amortized cost, the Group recognizes an allowance for doubtful accounts for expected credit losses. The expected credit losses are calculated based on historical loss experience or future recoverable amounts.

An allowance for doubtful accounts for trade receivables is always recognized in an amount equal to the full lifetime expected credit losses. In principle, with respect to financial assets except for trade receivables, an allowance for doubtful accounts is measured at an amount equal to the 12-month expected credit losses. However, the allowance for doubtful accounts is measured at an amount equal to the full lifetime expected credit losses if a credit risk on the financial asset has increased significantly since initial recognition.

The Group assesses whether a credit risk on a financial asset has increased significantly based on a change of the default risk considering past due information, financial difficulties of obligors or downgrades of the internal credit rating.

The Group assesses a whole or part of the financial asset which is deemed extremely difficult to be collected as a default and recognizes it as a credit-impaired financial asset. If the Group reasonably determines that a whole or part of the financial asset is uncollectible, the carrying amounts of financial assets are written-off directly.

The expected credit losses on trade receivables which are not assessed as credit-impaired financial assets are measured collectively by an asset group consisting of a number of homogeneous counterparties.

An allowance for doubtful accounts for financial assets is recognized in profit or loss. If an event which causes a reduction in the allowance for doubtful accounts occurs, a reversal of an allowance for doubtful accounts is recognized in profit or loss.

C. Financial Liabilities

(i) Initial Recognition and Measurement

Financial liabilities are classified into financial liabilities measured at fair value through profit or loss and financial liabilities measured at amortized cost. The Group determines the classification at initial recognition.

All financial liabilities are measured at fair value at initial recognition. However, financial liabilities measured at amortized cost are measured at cost after deducting transaction costs that are directly attributable to the financial liabilities.

(ii) Subsequent Measurement

After initial recognition, financial liabilities are measured based on the following classifications:

(a) Financial Liabilities Measured at Fair Value through Profit or Loss

Financial liabilities measured at fair value through profit or loss include financial liabilities held for trading and financial liabilities designated as measured at fair value through profit or loss at initial recognition.

(b) Financial Liabilities Measured at Amortized Cost

After initial recognition, financial liabilities measured at amortized cost are measured at amortized cost using the effective interest method. Amortization under the effective interest method and gains or losses on derecognition are recognized as profit or loss in the consolidated statement of income.

After initial recognition, financial guarantee contracts are measured at the higher of:

- The amount of an allowance for doubtful accounts calculated in accordance with "B Impairment of Financial Assets" above, and
- The amount initially measured less cumulative revenue recognized in accordance with IFRS 15 "Revenue from Contracts with Customers."

(iii) Derecognition

Financial liabilities are derecognized when the obligation is discharged, canceled or expired.

D. Offsetting of Financial Instruments

Financial assets and financial liabilities are offset and presented as a net amount in the consolidated statement of financial position only when there is a legally enforceable right to set off the recognized amounts and the Group intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

E. Derivatives and Hedge Accounting

The Group utilizes derivatives, including forward foreign exchange contracts and interest rate swap contracts, to hedge foreign exchange and interest rate risks. These derivatives are initially measured at fair value when the contract is entered into, and are subsequently remeasured at fair value. Changes in the fair value of derivatives are recognized as profit or loss in the consolidated statement of income. However, the gains or losses on the hedging instrument relating to the effective portion of cash flow hedges and hedges of net investment in foreign operations are recognized as other comprehensive income in the consolidated statement of comprehensive income.

At the inception of the hedge, the Group formally designates and documents the hedging relationship to which hedge accounting is applied and the objectives and strategies of risk management for undertaking the hedge. The documentation includes identification of the hedging instruments, the hedged items, the nature of the risks being hedged and how the hedging relationship's effectiveness is assessed. These hedges are assessed on an ongoing basis to determine whether the hedging relationship is effective prospectively, even though it is expected that there is an economic relationship between the hedged item and the hedging instrument, that the effect of credit risk does not dominate the value changes that result from that economic relationship, and that the hedge ratio of the hedging relationship is the same as that resulting from the quantity of the hedged item that the Group actually hedges and the quantity of the hedging instrument that the Group actually uses to hedge that quantity of the hedged item.

If a hedging relationship ceases to meet the hedge effectiveness requirement relating to the hedge ratio due to changes in an economic relationship between the hedged item and the hedging instrument but the risk management objective remains the same, the Group would adjust the hedge ratio so that it meets the qualifying criteria again. The Group discontinues hedge accounting for the portion that does not meet the requirement when the hedging relationship ceases to meet the qualifying criteria even after adjusting the hedge ratio.

Hedges that meet the stringent requirements for hedge accounting are classified in the following categories and accounted for in accordance with IFRS 9 "Financial Instruments."

(i) Fair Value Hedge

The gain or loss on the hedging instrument is recognized as profit or loss in the consolidated statement of income. However, changes in the fair value of the hedging instrument are recognized as other comprehensive income in the consolidated statement of comprehensive income if the hedging instrument hedges an equity instrument designated as at fair value through other comprehensive income. Regarding the hedging gain or loss on the hedged item, the carrying amount of the hedged item is adjusted and the change is recognized as profit or loss in the consolidated statement of income. However, changes in the fair value of an equity instrument which the Group elected to present in other comprehensive income are recognized as other comprehensive income.

(ii) Cash Flow Hedge

The effective portion of gains or losses on hedging instruments is recognized as other comprehensive income in the consolidated statement of comprehensive income, while the ineffective portion is recognized immediately as profit or loss in the consolidated statement of income.

The amounts of hedging instruments recognized in other comprehensive income are reclassified to profit or loss when the transactions of the hedged items affect profit or loss. In cases where hedged items result in the recognition of non-financial assets or liabilities, the amounts recognized as other comprehensive income are accounted for as adjustments to the original carrying amount of non-financial assets or liabilities.

If the hedged future cash flows are no longer expected to occur, any related cumulative gain or loss that has been recognized in equity as other comprehensive income is reclassified to profit or loss. If the hedged future cash flows are still expected to occur, amounts that have been recognized in other comprehensive income are continued to be recognized in other comprehensive income until the future cash flows occur.

(iii) Hedge of Net Investment in Foreign Operations

Translation differences resulting from the hedge of net investment in foreign operations are accounted for similarly to a cash flow hedge. The effective portion of gains or losses on hedging instruments is recognized as other comprehensive income in the consolidated statement of comprehensive income, while the ineffective portion is recognized as profit or loss in the consolidated statement of income. At the time of the disposal of the foreign operations, any related cumulative gain or loss that has been recognized in equity as other comprehensive income is reclassified to profit or loss.

F. Fair Value of Financial Instruments

Fair value of financial instruments that are traded in active financial markets at year end refers to quoted prices or dealer quotations.

If there is no active market, fair value of financial instruments is determined using appropriate valuation models.

(5) Cash and Cash Equivalents

Cash and cash equivalents consist of cash on hand, demand deposits, and short-term investments that are readily convertible to known amounts of cash and subject to insignificant risk of change in value and due within three months from the date of acquisition.

(6) Inventories

The cost of inventories includes all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Inventories are measured at the lower of cost or net realizable value, and the costs are determined by using the weighted-average method. Net realizable value is determined as the estimated selling price in the ordinary course of business less the estimated costs of completion and estimated costs necessary to make the sale.

Leaf tobacco which is stored for more than 12 months before being used for production is included in current assets since it is held within the normal operating cycle.

(7) Property, Plant and Equipment

Property, plant and equipment is measured by using the cost model and is stated at cost less accumulated depreciation and accumulated impairment losses.

The acquisition cost includes any costs directly attributable to the acquisition of the asset and dismantlement, removal and restoration costs, as well as borrowing costs eligible for capitalization.

Except for assets that are not subject to depreciation such as land, assets are depreciated using the straight-line method over their estimated useful lives. The estimated useful lives of major asset items are as follows:

- Buildings and structures: 38 to 50 years
- Machinery and vehicles: 10 to 15 years

The estimated useful lives and depreciation method are reviewed at each year end and if there are any changes made to the estimated useful lives and depreciation method, such changes are applied prospectively as changes in estimate.

(8) Goodwill and Intangible Assets

A. Goodwill

Goodwill is stated at acquisition cost less accumulated impairment losses.

Goodwill is not amortized. It is allocated to cash-generating units that are identified according to locations and types of businesses and tested for impairment annually or whenever there is any indication of impairment. Impairment losses on goodwill are recognized in the consolidated statement of income and no subsequent reversal is made.

B. Intangible Assets

Intangible assets are measured by using the cost model and are stated at cost less accumulated amortization and accumulated impairment losses.

Intangible assets acquired separately are measured at cost at the initial recognition, and the costs of intangible assets acquired through business combinations are recognized at fair value at the acquisition date. Expenditures on internally generated intangible assets are recognized as expense in the period when incurred, except for development expenses that satisfy the capitalization criteria.

Intangible assets with finite useful lives are amortized using the straight-line method over their estimated useful lives and are tested for impairment whenever there is any indication of impairment. The estimated useful lives and amortization method of intangible assets with finite useful lives are reviewed at each year end, and the effect of any changes in estimate would be accounted for on a prospective basis.

The estimated useful lives of major intangible assets with finite useful lives are as follows:

- Trademarks: 10 to 20 years
- Software: 5 years

Intangible assets with indefinite useful lives and intangible assets that are not ready to use are not amortized, but they are tested for impairment individually or by cash-generating unit annually or whenever there is any indication of impairment.

(9) Leases

Leases are classified as finance leases whenever substantially all the risks and rewards incidental to ownership are transferred to the Group. All other leases are classified as operating leases.

In finance lease transactions, leased assets and lease obligations are recognized in the consolidated statement of financial position at the lower of the fair value of the leased property or the present value of the minimum lease payments, each determined at the inception of the lease. Lease payments are apportioned between the financial cost and the reduction in the lease obligations based on the effective interest method. Financial costs are recognized in the consolidated statement of income. Leased assets are depreciated using the straight-line method over their estimated useful lives or lease terms, whichever is shorter.

In operating lease transactions, lease payments are recognized as an expense using the straight-line method over the lease terms in the consolidated statement of income. Contingent rents are recognized as an expense in the period when they are incurred.

Determining whether an arrangement is, or contains, a lease is based on the substance of the arrangement in accordance with IFRIC 4 "Determining Whether an Arrangement Contains a Lease," even if the arrangement does not take the legal form of a lease.

(10) Investment Property

Investment property is property held to earn rentals or for capital appreciation or both.

Investment property is measured by using the cost model and is stated at cost less accumulated depreciation and accumulated impairment losses.

(11) Impairment of Non-financial Assets

The Group assesses for each year whether there is any indication that an asset may be impaired. If any such indication exists, or in cases where the impairment test is required to be performed each year, the recoverable amount of the asset is estimated. In cases that the recoverable amount cannot be estimated for each asset, it is estimated by the cash-generating unit to which the asset belongs. The recoverable amount of an asset or a cash-generating unit is determined at the higher of its fair value less costs of disposal or its value in use. If the carrying amount of the asset or cash-generating unit exceeds the recoverable amount, impairment losses are recognized and the carrying amount is reduced to the recoverable amount. In determining the value in use, estimated future cash flows are discounted to the present value, using pretax discount rates that reflect current market assessments of the time value of money and the risks specific to the asset. In determining the fair value less costs of disposal, the Group uses an appropriate valuation model supported by available fair value indicators.

The Group assesses whether there is any indication that an impairment loss recognized in prior years for an asset other than goodwill may no longer exist or may have decreased, such as any changes in assumptions used for the determination of the recoverable amount. If any such indication exists, the recoverable amount of the asset or cash-generating unit is estimated. In cases that the recoverable amount exceeds the carrying amount of the asset or cash-generating unit, impairment losses are reversed up to the lower of the estimated recoverable amount or the carrying amount (net of depreciation) that would have been determined if no impairment losses had been recognized in prior years.

(12) Non-current Assets Held-for-Sale

An asset or asset group for which the value is expected to be recovered through a sales transaction rather than through continuing use is classified into a non-current asset or disposal group held-for-sale when the following conditions are met: it is highly probable that the asset or asset group will be sold within one year, the asset or asset group is available for immediate sale in its present condition, and the Group management commits to the sale plan. In such cases, the non-current asset is not depreciated or amortized and is measured at the lower of its carrying amount or its fair value less costs of disposal.

(13) Post-employment Benefits

The Group sponsors defined benefit plans and defined contribution plans as employee retirement benefit plans.

The Company is obligated to bear pension expenses for a mutual assistance association incurred with respect to services in or before June 1956 (prior to the enforcement of the Act on the Mutual Aid Association of Public Corporation Employees). Such obligations are calculated and included in liabilities related to the retirement benefits.

For each plan, the Group calculates the present value of defined benefit obligations, related current service cost and past service cost using the projected unit credit method. For a discount rate, a discount period is determined based on the period until the expected date of benefit payment in each year, and the discount rate is determined by reference to market yields for the period corresponding to the discount period at the end of the year on high quality corporate bonds or government bonds. Liabilities or assets for defined benefit plans are calculated by the present value of the defined benefit obligation, deducting the fair value of any plan assets (including adjustments for the asset ceiling for defined benefit plans and minimum funding requirements, if necessary). Expected interest costs and interest income are recognized as financial costs.

Remeasurements of defined benefit plans are recognized in full as other comprehensive income in the period when they are incurred and transferred to retained earnings immediately. Past service costs are recognized as profit or loss in the period when incurred.

The cost for retirement benefits for defined contribution plans is recognized as an expense at the time of contribution.

(14) Share-based Payments

The Group has a share option plan as an equity-settled share-based payment plan. Share options are estimated at fair value at grant date and are recognized as an expense over the vesting period in the consolidated statement of income after considering the number of share options that are expected to be eventually vested. The corresponding amount is recognized as an increase in equity in the consolidated statement of financial position.

(15) Provisions

The Group has present obligations (legal or constructive) resulting from past events and recognizes provisions when it is probable that the obligations are required to be settled and the amount of the obligations can be estimated reliably.

Where the effect of the time value of money is material, the amount of provisions is measured at the present value of the expenditures expected to be required to settle the obligations. In calculating the present value, the Group uses the pretax discount rate reflecting current market assessments of the time value of money and the risks specific to the liability.

In accordance with IAS 37 "Provisions, Contingent Liabilities and Contingent Assets," the Group recognizes a provision for restructuring when it has a detailed formal plan for the restructuring and has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan or announcing its main scheme to those affected by it. Restructuring provisions include only the direct expenditures arising from the restructuring, which meet both of the following criteria:

- necessarily entailed by the restructuring;
- not associated with the ongoing activities of the entity.

(16) Revenue

A. Revenue from Contracts with Customers

Revenue is recognized based on the following five-step approach.

Step 1: Identify the contract with a customer
Step 2: Identify the performance obligations in the contract
Step 3: Determine the transaction price
Step 4: Allocate the transaction price to the performance obligations in the contract
Step 5: Recognize revenue when the entity satisfies a performance obligation

The Group mainly engages in the sale of tobacco products, prescription drugs, and processed foods. Revenue is recognized upon delivery of the products because the customer obtains control of the products upon delivery, by which the Group evaluates that the performance obligation is satisfied. Revenue is measured at the consideration promised in a contract with a customer, less discounts, rebates and taxes, including consumption tax.

The tobacco excise taxes and other transactions in which the Group is involved as an agency are excluded from revenue. The amount after deducting the tobacco excise taxes and other transactions is presented as "Revenue" in the consolidated statement of income.

B. Interest Income

Interest income is recognized using the effective interest rate method.

C. Dividend Income

Dividend income is recognized when the shareholders' right to receive payment is established.

(17) Government Grants

Government grants are recognized at fair value when there is a reasonable assurance that the Group will comply with the conditions attached to them and receive the grants.

In the case that the government grants are related to expense items, they are recognized in profit or loss on a systematic basis over the period in which the related costs for which the grants are intended to compensate are recognized. With regard to government grants for assets, the amount of the grants is deducted from the acquisition cost of the assets.

(18) Borrowing Costs

With respect to assets that necessarily take a substantial period of time to get ready for their intended use or sale, the borrowing costs that are directly attributable to the acquisition, construction or production of the assets are capitalized as part of the acquisition cost of the assets. Other borrowing costs are recognized as an expense in the period when they are incurred.

(19) Income Taxes

Income taxes in the consolidated statement of income are presented as the total of current income taxes and deferred income taxes.

Current income taxes are measured at the amount that is expected to be paid to or refunded from the taxation authorities. For the calculation of the tax amount, the Group uses the tax rates and tax laws that have been enacted or substantively enacted by the end of the year. The current income taxes are recognized in profit or loss, except for taxes arising from items that are recognized in other comprehensive income or directly in equity and taxes arising from business combinations.

Deferred income taxes are calculated based on the temporary differences between the tax base for assets and liabilities and the carrying amount at year end. Deferred tax assets are recognized for deductible temporary differences, carryforward of unused tax credits and unused tax losses to the extent that it is probable that future taxable profit will be available against which they can be utilized. Deferred tax liabilities are recognized for taxable temporary differences.

The deferred tax assets or liabilities are not recognized for the following temporary differences:

- the initial recognition of goodwill
- the initial recognition of assets or liabilities in transactions that are not business combinations and at the time of transaction, affect neither accounting profit nor taxable profit or tax loss
- deductible temporary differences arising from investments in subsidiaries and associates, and interests in joint ventures to the extent that it is probable that the timing of the reversal of the temporary difference in the foreseeable future and it is not probable that future taxable profits will be available against which they can be utilized

• taxable temporary differences arising from investments in subsidiaries and associates, and interests in joint ventures to the extent that the timing of the reversal of the temporary difference is controlled and that it is probable the temporary difference will not reverse in the foreseeable future.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realized or the liability is settled, based on tax rates that have been enacted or substantively enacted by year end.

In the year ended December 31, 2018, the Company and certain domestic subsidiaries applied for approval of the adoption of the consolidated taxation system, and it is to be adopted from the following year. Therefore, from the year ended December 31, 2018, deferred tax assets and liabilities are accounted for assuming the adoption of the consolidated taxation system.

(20) Treasury Shares

Treasury shares are recognized at cost and deducted from equity. No gain or loss is recognized on the purchase, sale or cancellation of the treasury shares. Any difference between the carrying amount and the consideration paid is recognized in capital surplus.

(21) Earnings per Share

Basic earnings per share are calculated by dividing profit or loss attributable to ordinary shareholders of the parent company by the weighted-average number of ordinary shares outstanding during the year, adjusted by the number of treasury shares. Diluted earnings per share are calculated by adjusting the effects of dilutive potential ordinary shares.

(22) Dividends

Dividend distributions to the shareholders of the Company are recognized as liabilities in the period in which, for year end dividends, the Annual Shareholders' Meeting approves the distribution and, for interim dividends, the Board of Directors approves the distribution.

(23) Contingencies

A. Contingent Liabilities

The Group discloses contingent liabilities in the notes to consolidated financial statements if it has possible obligations at year end, whose existence cannot be confirmed at that date, or if the obligations do not meet the recognition criteria of a provision described in "20. Provisions."

B. Contingent Assets

The Group discloses contingent assets in the notes to consolidated financial statements if an inflow of future economic benefits to the Group is probable, but not virtually certain at year end.

(24) Adjusted Financial Measures

The adjusted financial measures are calculated by adding certain adjustment items to the non-adjusted financial data or by deducting the items from the non-adjusted financial data.

The adjustment items are determined by management's judgment, taking into consideration the nature and frequency of the income and costs such that they provide effective comparative information on the Group performance and that they reflect the way of managing our business appropriately. Adjusted financial measures are presented in the consolidated statement of income and "6. Operating Segments."

The adjusted financial measures are not defined under IFRS and are not comparable with equivalent indicators for other entities.

(Changes in Accounting Policies)

The Group has adopted the following new accounting standards, amended standards and new interpretations from the year ended December 31, 2018.

IFRS		Description of new standards and amendments
IFRS 9	Financial Instruments	Limited changes to classification and measurement of financial assets, and introduction of an expected credit loss impairment model
IFRS 15	Revenue from Contracts with Customers	Amendments to accounting treatment for recognizing revenue

The effect of adopting IFRS 9 on the consolidated financial statements is immaterial.

In adopting IFRS 15, the Group used a transition method by which the cumulative effect of initially applying this Standard was recognized at the date of initial application.

As a result of identification of performance obligations under contracts with customers based on the five-step approach stated in "(16) Revenue A. Revenue from Contracts with Customers," the sales promotion and other expenses paid by the Group to customers, which have been previously accounted for as selling, general and administrative expenses, are partially deducted from revenue from the year ended December 31, 2018. In addition, shipping and warehousing expenses and other expenses necessary for satisfying performance obligations that have been previously accounted for as selling, general and administrative expenses are accounted for as cost of sales from the year ended December 31, 2018.

As a result, compared to the application of the former accounting standard, "Revenue" and "Selling, general and administrative expenses" decreased by ¥10,944 million and ¥70,905 million respectively, and "Cost of sales" increased by ¥59,962 million on the consolidated statement of income for the year ended December 31, 2018. The above effects include promotion expenses (¥9,028 million) accounted for as reductions in revenue, as well as shipping and warehousing expenses (¥28,000 million) accounted for as cost of sales.

These changes have no effect on operating profit and profit for the period.

4. Significant Accounting Estimates and Judgments

Preparation of consolidated financial statements of the Group requires management estimates and assumptions in order to measure income, expenses, assets and liabilities, and disclose contingencies as of the year end. These estimates and assumptions are based on the best judgment of management in light of historical experience and various factors deemed to be reasonable as of the year end. Given their nature, actual results may differ from those estimates and assumptions.

The estimates and assumptions are continuously reviewed by management. The effects of a change in estimates and assumptions are recognized in the period of the change or the period of the change and future periods.

Among the above estimates and assumptions, the following are items that may have a material effect on the amounts recognized in the consolidated financial statements of the Group:

A. Impairment of Property, Plant and Equipment, Goodwill, Intangible Assets and Investment Properties

With regard to property, plant and equipment, goodwill, intangible assets and investment properties, if there is any indication that the recoverable amount declines below the carrying amounts of the assets, the Group performs an impairment test.

The important indications include significant changes with adverse effect on the results of past or projected business performance, significant changes in the use of acquired assets or in overall business strategy, and significant deteriorations in industry trends and economic trends. With regard to goodwill, an impairment test is conducted at least once a year, regardless of any indication of impairment, in order to ensure that the recoverable amount exceeds the carrying amount.

The impairment test is performed by comparing the carrying amount and the recoverable amount of assets. If the recoverable amount declines below the carrying amount, impairment losses are recognized. The recoverable amount is mainly calculated based on the discounted cash flow model. Certain assumptions are made for the useful lives and the future cash flows of the assets, discount rates and long-term growth rates. These assumptions are based on the best estimates and judgments made by management; however, there is a possibility that these assumptions may be affected by changes in uncertain future economic conditions, which may have a material impact on the consolidated financial statements in future periods.

The method for calculating the recoverable amount is described in "13. Property, Plant and Equipment," "14. Goodwill and Intangible Assets" and "16. Investment Property." With regard to goodwill, the sensitivity analysis is described in "14. Goodwill and Intangible Assets."

B. Post-employment Benefits

The Group has various types of retirement benefit plans, including defined benefit plans. In addition, the mutual pension benefits plan of the Company is one of the public pension systems under the jurisdiction of the government of Japan and the Company is legally obligated to bear a part of the pension costs of the plan.

The present value of defined benefit obligations on each of these plans and the related service costs are calculated based on actuarial assumptions. These actuarial assumptions require estimates and judgments on variables, such as discount rates and inflation rate.

The Group obtains advice from external pension actuaries with respect to the appropriateness of these actuarial assumptions including these variables.

The actuarial assumptions are determined based on the best estimates and judgments made by management; however, there is a possibility that these assumptions may be affected by changes in uncertain future economic conditions, or by the publication or the amendment of related laws, which may have a material impact on the consolidated financial statements in future periods.

These actuarial assumptions and the related sensitivity analysis are described in "22. Employee Benefits."

C. Provisions

The Group recognizes various provisions, including provisions for asset retirement obligations and restructuring, in the consolidated statement of financial position.

These provisions are recognized based on the best estimates of the expenditures required to settle the obligations taking risks and uncertainty related to the obligations into account as of the year end.

Expenditures required to settle the obligations are calculated by taking possible results into account comprehensively; however, they may be affected by the occurrence of unexpected events or changes in conditions which may have a material impact on the consolidated financial statements in future periods.

The nature and amount of recognized provisions are described in "20. Provisions."

D. Income Taxes

The Group operates business activities around the world, and it recognizes current tax liabilities and income taxes as the estimated amounts to be paid to the tax authorities, based on the estimation in accordance with their laws and regulations.

Calculating current tax liabilities and income taxes requires estimates and judgment on various factors, including the interpretation of tax regulations by taxable entities and the tax authority in the jurisdiction or the experience of past tax audits.

Therefore, there may be differences between the amount recognized as tax liabilities and income taxes and the amount of actual tax liabilities and income taxes. These differences may have a material impact on the consolidated financial statements in future periods.

In addition, deferred tax assets are recognized to the extent that it is probable that taxable income will be available against which deductible temporary differences can be utilized.

In recognizing the deferred tax assets, when judging the possibility of the future taxable income, we reasonably estimate the timing and amount of future taxable income based on the business plan.

The timing when taxable income arises and the amount of such income may be affected by changes in uncertain future economic conditions. Therefore, this may have a material impact on the consolidated financial statements in future periods.

The content and amount related to income taxes are described in "17. Income Taxes."

E. Contingencies

With regard to contingencies, any items that may have a material impact on business in the future are disclosed in light of all the available evidence as of the year end and by taking into account the probability of these contingencies and their impact on financial reporting.

The content of contingencies is described in "39. Contingencies."

5. New Accounting Standards Not Yet Adopted by the Group

By the date of approval of the consolidated financial statements, new accounting standards, amended standards and new interpretations that have been issued, but have not been early adopted by the Group are as follows.

The implications from adoption of these standards and interpretations are assessed by the Group; however, we evaluate that none of them will have a material impact on our operating results and financial condition.

In relation to adoption of IFRS 16 "Leases," operating lease payments are previously recognized as expenses using the straight-line method over the lease term in "Cost of sales" and "Selling, general and administrative expenses" without recognizing as assets and obligations in the consolidated statement of financial position. Operating lease payments will be recognized as right-of-use assets and lease liabilities in the consolidated statement of financial position. The amount of depreciation would be recognized in "Cost of sales" and "Selling, general and administrative expenses" and the amount of interest cost would be recognized in "Financial costs." Due to adoption of the standard, "Assets" and "Liabilities" in the consolidated statement of financial position are expected to increase by ¥39,033 million. There will be immaterial impact on operating profit and profit for the period from this change.

IFRS		Mandatory adoption (From the year beginning)	To be adopted by the Group	Description of new standards and amendments
IFRS 3	Business Combinations	January 1, 2019	Year ending December 2019	Clarifying accounting treatment for previously held interests in a joint operation
		January 1, 2020	Year ending December 2020	Amendments to definition of "business"
IFRS 9	Financial Instruments	January 1, 2019	Year ending December 2019	Amendments to classification of financial assets included in prepayment features
IFRS 11	Joint Arrangements	January 1, 2019	Year ending December 2019	Clarifying accounting treatment for previously held interests in a joint operation
IFRS 16	Leases	January 1, 2019	Year ending December 2019	Amendments to accounting treatment for lease arrangements
IFRS 17	Insurance Contracts	January 1, 2021	Year ending December 2021	Amendments to accounting treatment for insurance contracts
IAS 1	Presentation of Financial Statements	January 1, 2020	Year ending December 2020	Amendments to definition of "materiality"
IAS 8	Accounting Policies, Changes in Accounting Estimates and Errors	January 1, 2020	Year ending December 2020	Amendments to definition of "materiality"
IAS 12	Income Taxes	January 1, 2019	Year ending December 2019	Clarifying accounting treatment for income tax consequences of dividends
IAS 19	Employee Benefits	January 1, 2019	Year ending December 2019	Clarifying treatment on a defined benefit plan curtailment or settlement
IAS 23	Borrowing Costs	January 1, 2019	Year ending December 2019	Clarifying the method for calculating the borrowing costs eligible for capitalization
IAS 28	Investments in Associates and Joint Ventures	January 1, 2019	Year ending December 2019	Clarifying accounting treatment for impairment loss of investments in associates and joint ventures
IFRIC 23	Uncertainty over Income Tax Treatments	January 1, 2019	Year ending December 2019	Clarifying accounting treatment for uncertainty over income tax treatments
IFRS 10 IAS 28	Sale or Contribution of Assets between an Investor and its Associate or Joint Venture	Not yet determined	Not yet determined	Amendments to accounting treatment for sale or contribution of assets between an investor and its associate or joint venture

6. Operating Segments

(1) Outline of Reportable Segments

The reportable segments of the Group are determined based on the operating segments that are components of the Group for which separate financial information is available and are evaluated regularly by the Board of Directors in deciding how to allocate resources and in assessing performance.

The Group is mainly engaged in the manufacture and sale of tobacco products, prescription drugs and processed foods. With respect to tobacco products, operations are managed separately for domestic and overseas markets. The reportable segments of the Group are composed of four segments: "Domestic Tobacco Business," "International Tobacco Business," "Pharmaceutical Business," and "Processed Food Business." They are determined by types of products, characteristics, and markets.

The "Domestic Tobacco Business" manufactures and sells tobacco products in domestic areas (which include duty-free shops in Japan and markets in China, Hong Kong, and Macau where the Company's China Division operates). The "International Tobacco Business" manufactures and sells tobacco products overseas mainly through JT International S.A., which controls manufacturing and sales operations. The "Pharmaceutical Business" consists of research and development, and the manufacture and sale of prescription drugs. The "Processed Food Business" consists of the manufacture and sale of frozen and ambient processed foods, bakery products and seasonings.

(2) Revenues and Performances of Reportable Segments

Revenues and performances of reportable segments are as follows. The Board of Directors assesses the segment performance and determines resource allocation after reviewing revenues and adjusted operating profit. Since financial income, financial costs and income taxes are managed by the Group head office, these income and expenses are excluded from segment performance. Transactions within the segments are based mainly on prevailing market prices.

Year ended December 31, 2017

Millions of yen

	Reportable Segments							
	Domestic Tobacco	International Tobacco	Pharmaceuticals	Processed Food	Total	Other (Note 2)	Elimination	Consolidated
Revenue								
External revenue (Note 3)	¥626,758	¥1,237,577	¥104,714	¥163,138	¥2,132,187	¥ 7,466	¥ —	¥2,139,653
Intersegment revenue	8,558	31,465	—	22	40,045	7,543	(47,588)	—
Total revenue	¥635,315	¥1,269,042	¥104,714	¥163,159	¥2,172,232	¥ 15,008	¥(47,588)	¥2,139,653
Segment profit (loss)								
Adjusted operating profit (Note 1)	¥232,275	¥ 351,302	¥ 24,094	¥ 5,397	¥ 613,069	¥(28,156)	¥ 388	¥ 585,300
Other items								
Depreciation and amortization	¥ 56,001	¥ 76,098	¥ 5,120	¥ 6,137	¥ 143,355	¥ 2,288	¥ (237)	¥ 145,407
Impairment losses on other than financial assets	53	2,599	—	286	2,938	489	—	3,427
Reversal of impairment losses on other than financial assets	—	455	—	—	455	—	—	455
Share of profit (loss) in investments accounted for using the equity method	22	6,102	—	17	6,140	53	—	6,194
Capital expenditures	51,549	68,427	6,230	10,424	136,631	4,838	(564)	140,905

Year ended December 31, 2018

	Reportable Segments							Millions of yen
	Domestic Tobacco	International Tobacco	Pharmaceuticals	Processed Food	Total	Other (Note 2)	Elimination	Consolidated
Revenue								
External revenue (Note 3)	**¥621,426**	**¥1,312,342**	**¥113,992**	**¥161,387**	**¥2,209,147**	**¥ 6,815**	**¥ —**	**¥2,215,962**
Intersegment revenue	**7,976**	**27,637**	**—**	**1**	**35,615**	**5,737**	**(41,353)**	**—**
Total revenue	**¥629,403**	**¥1,339,979**	**¥113,992**	**¥161,388**	**¥2,244,762**	**¥ 12,553**	**¥(41,353)**	**¥2,215,962**
Segment profit (loss)								
Adjusted operating profit (Note 1)	**¥208,977**	**¥ 384,524**	**¥ 28,438**	**¥ 4,123**	**¥ 626,062**	**¥(30,440)**	**¥ (159)**	**¥ 595,463**
Other items								
Depreciation and amortization	**¥ 55,044**	**¥ 89,887**	**¥ 5,071**	**¥ 6,708**	**¥ 156,710**	**¥ 2,193**	**¥ (233)**	**¥ 158,671**
Impairment losses on other than financial assets	**—**	**5,336**	**2,141**	**146**	**7,623**	**831**	**—**	**8,454**
Reversal of impairment losses on other than financial assets	**—**	**692**	**—**	**—**	**692**	**—**	**—**	**692**
Share of profit (loss) in investments accounted for using the equity method	**35**	**3,849**	**—**	**11**	**3,895**	**36**	**—**	**3,931**
Capital expenditures	**55,444**	**75,727**	**11,333**	**12,749**	**155,253**	**4,844**	**(289)**	**159,808**

Reconciliation from "Adjusted operating profit" to "Profit before income taxes"
Year ended December 31, 2017

	Reportable Segments							Millions of yen
	Domestic Tobacco	International Tobacco	Pharmaceuticals	Processed Food	Total	Other (Note 2)	Elimination	Consolidated
Adjusted operating profit (Note 1)	¥232,275	¥351,302	¥24,094	¥5,397	¥613,069	¥(28,156)	¥388	¥585,300
Amortization cost of acquired intangibles arising from business acquisitions	(16,245)	(34,170)	—	—	(50,414)	—	—	(50,414)
Adjustment items (income) (Note 4)	6	16,723	—	—	16,729	20,840	—	37,569
Adjustment items (costs) (Note 5)	(197)	(8,272)	—	(20)	(8,489)	(2,865)	—	(11,354)
Operating profit (loss)	¥215,839	¥325,584	¥24,094	¥5,377	¥570,894	¥(10,181)	¥388	¥561,101
Financial income								4,780
Financial costs								(27,349)
Profit before income taxes								¥538,532

Year ended December 31, 2018

	Reportable Segments							Millions of yen
	Domestic Tobacco	International Tobacco	Pharmaceuticals	Processed Food	Total	Other (Note 2)	Elimination	Consolidated
Adjusted operating profit (Note 1)	**¥208,977**	**¥384,524**	**¥28,438**	**¥4,123**	**¥626,062**	**¥(30,440)**	**¥(159)**	**¥595,463**
Amortization cost of acquired intangibles arising from business acquisitions	**(16,245)**	**(45,527)**	**—**	**—**	**(61,772)**	**—**	**—**	**(61,772)**
Adjustment items (income) (Note 4)	**9**	**1,711**	**—**	**37**	**1,757**	**38,691**	**—**	**40,447**
Adjustment items (costs) (Note 5)	**(288)**	**(1,195)**	**(2,141)**	**(1,240)**	**(4,864)**	**(4,290)**	**—**	**(9,154)**
Operating profit (loss)	**¥192,453**	**¥339,514**	**¥26,297**	**¥2,919**	**¥561,183**	**¥ 3,960**	**¥(159)**	**¥564,984**
Financial income								**5,754**
Financial costs								**(39,252)**
Profit before income taxes								**¥531,486**

(Note 1) For adjusted operating profit, amortization cost of acquired intangibles arising from business acquisitions, and adjustment items (income and costs) are excluded from operating profit (loss).

(Note 2) "Other" includes business activities relating to rent of real estate and corporate expenses relating to corporate communication and operation of the head office.

(Note 3) Core revenue as part of the "Domestic Tobacco Business" and the "International Tobacco Business" is as follows:

	2017	Millions of yen 2018
Domestic Tobacco	¥ 590,605	**¥ 582,379**
International Tobacco	1,176,956	**1,250,719**

(Note 4) The breakdown of "Adjustment items (income)" is as follows:

	2017	Millions of yen 2018
Restructuring incomes	¥21,645	**¥39,284**
Reversal of impairment losses on investments in associates	8,848	**—**
Gains on remeasurement related to the business combination	5,042	**—**
Other	2,034	**1,163**
Adjustment items (income)	¥37,569	**¥40,447**

Restructuring incomes for the year ended December 31, 2017 and 2018 mainly relate to gains on sale of real estate. The breakdown of restructuring incomes is described in "26. Other Operating Income."

(Note 5) The breakdown of "Adjustment items (costs)" is as follows:

	2017	Millions of yen 2018
Restructuring costs	¥ 8,398	**¥7,934**
Other	2,956	**1,220**
Adjustment items (costs)	¥11,354	**¥9,154**

Restructuring costs for the year ended December 31, 2017 mainly relate to rationalization of the production and distribution system in some markets in the "International Tobacco Business." Restructuring costs for the year ended December 31, 2018 mainly relate to disposal of real estate, business structure reform in the "Pharmaceutical Business" and rationalization of the production and distribution system in some markets in the "International Tobacco Business."

Restructuring costs included in "Cost of sales" were ¥84 million and ¥13 million, and those costs included in "Selling, general and administrative expenses" were ¥8,314 million and ¥7,921 million for the years ended December 31, 2017 and 2018, respectively. The breakdown of restructuring costs included in "Selling, general and administrative expenses" is described in "27. Selling, General and Administrative Expenses." Other for the year ended December 31, 2018 mainly relates to settlement of the litigation in September 2018.

(3) Geographic Information

The regional breakdown of non-current assets as of December 31 is as follows:

Non-current Assets

	2017	2018
		Millions of yen
Japan	¥ 830,838	**¥ 835,386**
Overseas	2,301,854	**2,452,505**
Consolidated	¥3,132,692	**¥3,287,891**

(Note) Non-current assets, exclusive of financial instruments, deferred tax assets and retirement benefits assets, are segmented by the location of the assets.

The regional breakdown of external revenue for each year is as follows:

External Revenue

	2017	2018
		Millions of yen
Japan	¥ 831,216	**¥ 822,070**
Overseas	1,308,437	**1,393,892**
Consolidated	¥2,139,653	**¥2,215,962**

(Note) Revenue is segmented by the sales destination.

(4) Major Customers Information

The "International Tobacco Business" of the Group sells products to the Megapolis Group that engages in distribution and wholesale business in Russia and other countries. The external revenues from the Megapolis Group were ¥248,881 million (11.6% of consolidated revenue) for the year ended December 31, 2017 and ¥249,797 million (11.3% of consolidated revenue) for the year ended December 31, 2018.

7. Cash and Cash Equivalents

The breakdown of "Cash and cash equivalents" as of December 31 is as follows:

	2017	2018
		Millions of yen
Cash and deposits	¥215,885	**¥234,263**
Short-term investments	69,601	**47,800**
Total	¥285,486	**¥282,063**

Cash and cash equivalents are classified as financial assets measured at amortized cost.

"Cash and cash equivalents" includes cash and cash equivalents of ¥24,772 million (IRR 18,595 billion) as of December 31, 2018 held by the Group's Iranian subsidiaries. Due to international sanctions and other factors imposed on Iran, the subsidiaries' ability to remit funds outside of Iran is restricted.

8. Trade and Other Receivables

The breakdown of "Trade and other receivables" as of December 31 is as follows:

	2017	2018
		Millions of yen
Note and account receivables	¥439,562	**¥449,863**
Other	15,226	**8,378**
Allowance for doubtful accounts	(23,589)	**(1,650)**
Total	¥431,199	**¥456,591**

Trade and other receivables are presented net of allowance for doubtful accounts in the consolidated statement of financial position.
Trade and other receivables are classified as financial assets measured at amortized cost.

9. Inventories

The breakdown of "Inventories" as of December 31 is as follows:

	2017	2018
		Millions of yen
Merchandise and finished goods (Note 1)	¥193,179	**¥209,491**
Leaf tobacco (Note 2)	352,803	**364,084**
Other	66,971	**75,662**
Total	¥612,954	**¥649,238**

(Note 1) For imported tobacco products (merchandise) that are sold by TS Network Co., Ltd., a subsidiary of the Company, commissions solely from wholesale are included in revenue. The amount of imported tobacco products (merchandise) that the company holds as of December 31 of each year is included in inventories and presented as "Merchandise and finished goods."
(Note 2) Leaf tobacco includes those products that will be used after 12 months from the end of each year, but they are included in inventories since they are held within the normal operating cycle.

10. Other Financial Assets

(1) The breakdown of "Other financial assets" as of December 31 is as follows:

	2017	2018
		Millions of yen
Derivative assets	¥ 5,978	**¥ 8,653**
Equity securities	77,642	**64,684**
Debt securities	11,352	**26,816**
Time deposits	977	**979**
Other	39,607	**55,656**
Allowance for doubtful accounts	(6,569)	**(6,108)**
Total	¥128,987	**¥150,679**
Current assets	¥ 14,016	**¥ 35,633**
Non-current assets	114,970	**115,046**
Total	¥128,987	**¥150,679**

Other financial assets are presented net of allowance for doubtful accounts in the consolidated statement of financial position.
Derivative assets are classified as financial assets measured at fair value through profit or loss excluding those to which hedge accounting is applied, equity securities are classified as financial assets measured at fair value through other comprehensive income, and time deposits and debt securities are classified as financial assets measured at amortized cost.

(2) Names of major securities held as financial assets measured at fair value through other comprehensive income and their fair values as of December 31 are as follows:

Company name	2017	2018
		Millions of yen
KT&G Corporation	¥35,141	**¥28,904**
Seven & i Holdings Co., Ltd.	4,005	**4,091**
DOUTOR・NICHIRES Holdings Co., Ltd.	3,715	**2,681**
Central Japan Railway Company	2,018	**2,317**
OKAMURA CORPORATION	1,986	**1,710**
KATO SANGYO CO., LTD.	2,325	**1,709**

Equity securities are held mainly for strengthening relationships with investees. Therefore, they are designated as financial assets measured at fair value through other comprehensive income.

In order to pursue the efficiency of assets held and to use them effectively, sales of financial assets measured at fair value through other comprehensive income have been carried out (derecognition).

The fair value at the time of sale and cumulative gain or loss that is recognized in equity through other comprehensive income for each year is as follows:

	2017	2018
		Millions of yen
Fair Value	¥1,545	**¥2,241**
Cumulative gain or loss recognized in equity as other comprehensive income (Note)	(461)	**(860)**

(Note) The figure represents the amount transferred to retained earnings.
The cumulative gain or loss recognized in equity as other comprehensive income is transferred to retained earnings when an equity instrument is sold or the decline in its fair value compared to its acquisition cost is significant.

11. Other Current Assets

The breakdown of "Other current assets" as of December 31 is as follows:

	2017	2018
		Millions of yen
Prepaid tobacco excise taxes	¥297,332	**¥308,815**
Prepaid expenses	19,339	**21,262**
Consumption tax receivables	19,496	**17,177**
Other	25,547	**38,618**
Total	¥361,715	**¥385,872**

12. Non-current Assets Held-for-Sale

The breakdown of "Non-current assets held-for-sale" as of December 31 is as follows:

Breakdown of Major Assets

	2017	2018
		Millions of yen
Non-current assets held-for-sale		
Property, plant and equipment	¥1,453	**¥ 4**
Investment property	943	**6**
Total	¥2,396	**¥10**

"Non-current assets held-for-sale" are mainly idle properties which are currently actively marketed for sale.

With regard to such assets and assets sold, impairment losses of ¥518 million and ¥74 million are recognized in "Selling, general and administrative expenses" in the consolidated statement of income for the years ended December 31, 2017 and 2018, respectively.

13. Property, Plant and Equipment

(1) Schedule of Property, Plant and Equipment

The schedules of the carrying amount, acquisition cost, and accumulated depreciation and accumulated impairment losses of "Property, plant and equipment" are as follows:

Carrying Amount	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	Construction in progress	Total
					Millions of yen
As of January 1, 2017	¥344,237	¥246,192	¥44,193	¥46,213	¥680,835
Individual acquisition	17,833	43,586	15,071	38,647	115,137
Acquisition through business combinations	12,401	14,424	315	1,599	28,739
Transfer to investment property	(1,721)	(5)	(6)	—	(1,732)
Transfer to non-current assets held-for-sale	(2,250)	—	—	—	(2,250)
Depreciation	(15,813)	(48,717)	(14,634)	—	(79,164)
Impairment losses	(699)	(1,108)	(46)	(37)	(1,891)
Reversal of impairment losses	—	451	3	—	455
Sale or disposal	(581)	(4,685)	(1,011)	(17)	(6,295)
Exchange differences on translation of foreign operations	3,230	5,056	1,002	(226)	9,061
Other	6,610	23,894	1,486	(29,277)	2,712
As of December 31, 2017	363,245	279,088	46,373	56,902	745,607
Individual acquisition	**18,972**	**56,901**	**14,873**	**48,735**	**139,480**
Acquisition through business combinations	**7,275**	**8,498**	**107**	**21**	**15,902**
Transfer to investment property	**(3,211)**	**(0)**	**(3)**	—	**(3,215)**
Transfer to non-current assets held-for-sale	**(1,945)**	**(4)**	—	—	**(1,949)**
Depreciation	**(16,647)**	**(50,794)**	**(14,987)**	—	**(82,428)**
Impairment losses	**(1,561)**	**(3,442)**	**(86)**	**(131)**	**(5,220)**
Reversal of impairment losses	**248**	**432**	—	**12**	**692**
Sale or disposal	**(764)**	**(3,221)**	**(773)**	**(82)**	**(4,841)**
Exchange differences on translation of foreign operations	**(14,716)**	**(22,895)**	**(2,162)**	**(4,208)**	**(43,981)**
Other	**11,691**	**24,025**	**991**	**(37,913)**	**(1,206)**
As of December 31, 2018	**¥362,586**	**¥288,587**	**¥44,333**	**¥63,335**	**¥758,841**

Acquisition Cost	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	Construction in progress	Total
					Millions of yen
As of January 1, 2017	¥643,073	¥693,378	¥147,223	¥46,213	¥1,529,888
As of December 31, 2017	664,779	761,581	156,169	56,902	1,639,431
As of December 31, 2018	**671,434**	**773,836**	**152,793**	**63,443**	**1,661,505**

Accumulated Depreciation and Accumulated Impairment Losses	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	Construction in progress	Total
					Millions of yen
As of January 1, 2017	¥298,836	¥447,187	¥103,030	¥ —	¥849,053
As of December 31, 2017	301,534	482,493	109,797	—	893,824
As of December 31, 2018	**308,847**	**485,249**	**108,460**	**107**	**902,664**

The carrying amount of property, plant and equipment as of December 31 includes the carrying amount of the following leased assets:

	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	Total
				Millions of yen
As of January 1, 2017	¥6,538	¥1,201	¥ 7	¥ 7,746
As of December 31, 2017	6,509	4,669	11	11,189
As of December 31, 2018	**6,386**	**5,846**	**271**	**12,503**

(2) Impairment Losses

The grouping of property, plant and equipment for impairment test is the smallest cash-generating unit that independently generates cash inflow.

The Group recognized impairment losses of ¥1,891 million for the year ended December 31, 2017, and ¥5,220 million for the year ended December 31, 2018 in "Selling, general and administrative expenses" in the consolidated statement of income.

Impairment losses recognized in the year ended December 31, 2017 represent the losses incurred to reduce the carrying amounts to the recoverable amounts of the buildings, structures, machinery and vehicles, such as due to the decision of closing down of a factory.

The recoverable amounts of these assets are calculated mainly by their values in use, which are set at "zero."

Impairment losses recognized in the year ended December 31, 2018 represent the losses incurred to reduce the carrying amounts to the recoverable amounts of the buildings, structures, machinery and vehicles, such as due to the decision of individual demolition.

The recoverable amounts of these assets are calculated mainly by their values in use.

14. Goodwill and Intangible Assets

(1) Schedule of Goodwill and Intangible Assets

The schedules of carrying amount, acquisition cost, and accumulated amortization and accumulated impairment losses of "Goodwill" and "Intangible assets" are as follows:

					Millions of yen
Carrying Amount	Goodwill	Trademarks	Software	Other	Total
As of January 1, 2017	¥1,601,987	¥364,896	¥27,078	¥31,996	¥2,025,957
Individual acquisition	—	257	7,724	17,482	25,462
Acquisition through business combinations	202,144	71,450	—	12,831	286,425
Amortization (Note)	—	(46,786)	(12,808)	(6,079)	(65,673)
Impairment losses	—	(940)	(75)	(4)	(1,019)
Sale or disposal	—	—	(89)	(43)	(132)
Exchange differences on translation of foreign operations	87,080	12,410	(153)	(108)	99,229
Other	—	—	1,546	(1,409)	136
As of December 31, 2017	1,891,210	401,286	23,223	54,666	2,370,385
Individual acquisition	**—**	**188**	**10,831**	**8,970**	**19,990**
Acquisition through business combinations	**279,606**	**104,833**	**163**	**6,758**	**391,360**
Amortization (Note)	**—**	**(57,539)**	**(11,242)**	**(6,888)**	**(75,669)**
Impairment losses	**—**	**—**	**(17)**	**(2,389)**	**(2,406)**
Reversal of impairment losses	**—**	**—**	**0**	**—**	**0**
Sale or disposal	**—**	**(70)**	**(124)**	**(1,556)**	**(1,750)**
Exchange differences on translation of foreign operations	**(162,240)**	**(27,423)**	**(271)**	**(1,099)**	**(191,033)**
Other	**(161)**	**—**	**9,355**	**(8,579)**	**615**
As of December 31, 2018	**¥2,008,416**	**¥421,276**	**¥31,919**	**¥49,882**	**¥2,511,492**

(Note) The amortization of intangible assets is included in "Cost of sales" and "Selling, general and administrative expenses" in the consolidated statement of income.

					Millions of yen
Acquisition Cost	Goodwill	Trademarks	Software	Other	Total
As of January 1, 2017	¥1,601,987	¥ 928,876	¥137,761	¥ 96,994	¥2,765,618
As of December 31, 2017	1,891,210	1,028,189	142,531	126,263	3,188,192
As of December 31, 2018	**2,008,416**	**1,078,596**	**157,191**	**94,698**	**3,338,901**

					Millions of yen
Accumulated Amortization and Accumulated Impairment Losses	Goodwill	Trademarks	Software	Other	Total
As of January 1, 2017	¥—	¥563,981	¥110,683	¥64,997	¥739,661
As of December 31, 2017	—	626,903	119,308	71,597	817,808
As of December 31, 2018	**—**	**657,320**	**125,272**	**44,817**	**827,409**

(2) Material Goodwill and Intangible Assets

Goodwill and intangible assets recognized in the consolidated statement of financial position are mainly composed of goodwill and trademarks in the JTIH Group. The carrying amounts of goodwill as of December 31, 2017 and 2018 were ¥1,599,950 million and ¥1,717,156 million, respectively. The carrying amounts of trademarks as of December 31, 2017 and 2018 were ¥269,453 million and ¥305,997 million, respectively.

The majority of goodwill and trademark in the JTIH Group was recognized as a result of the acquisitions of RJR Nabisco's non-U.S. tobacco operations in 1999 and Gallaher in 2007.

Other than the above, goodwill and trademark in Domestic Tobacco business were recognized as a result of the acquisition of Natural American Spirit's non-U.S. tobacco operations in 2016. The carrying amounts of goodwill as of December 31, 2017 and 2018 were ¥265,891 million and ¥265,891 million, respectively. The carrying amounts of trademarks as of December 31, 2017 and 2018 were ¥131,822 million and ¥115,274 million, respectively.

The trademarks are amortized using the straight-line method and the remaining amortization period is mainly from 7 to 8 years.

(3) Impairment Test for Goodwill

For the year ended December 31, 2018, the carrying amount of the majority of goodwill is allocated to the domestic tobacco cash-generating unit of ¥265,891 million (¥265,891 million for the year ended December 31, 2017), the international tobacco cash-generating unit of ¥1,717,156 million (¥1,599,950 million for the year ended December 31, 2017) and the processed food cash-generating unit of ¥25,368 million (¥25,368 million for the year ended December 31, 2017). Details of the result of impairment tests are as follows:

A. Domestic Tobacco Cash-generating Unit

The recoverable amount is calculated by the value in use based on the three-year business plan that was prepared by reflecting past experiences and external information and that was approved by management. After the three-year business plan, given the current domestic tobacco market situation, the Group calculates the value in use by using cash flows with a growth rate of 0% conservatively. For the previous year, the Group decreased a growth rate from 3.9% in the fourth year to 0% in the ninth year gradually, and calculated the value in use from the tenth year by using the same cash flows as the ninth year.

The discount rate before taxes is 4.9% (2017: 4.9%). The value in use sufficiently exceeds the carrying amount of the cash-generating unit. Therefore, even in cases where the discount rate and growth rate used in calculating the value in use fluctuate within reasonable ranges, the Group assumes that the value in use will not become less than the carrying amount.

B. International Tobacco Cash-generating Unit

The recoverable amount is calculated by the value in use based on the three-year business plan that was prepared by reflecting past experiences and external information and that was approved by management. After the three-year business plan, the Group sets a growth rate from 8.1% in the fourth year (2017: 6.4%) to 3.0% in the ninth year (2017: 2.8%), and the same growth rate as the ninth year from the tenth year as a continued growth rate for inflation.

The discount rate before taxes is 9.9% (2017: 9.8%). The value in use sufficiently exceeds the carrying amount of the cash-generating unit. Therefore, even in cases where the discount rate and growth rate used in calculating the value in use fluctuate within reasonable ranges, the Group assumes that the value in use will not become less than the carrying amount.

C. Processed Food Cash-generating Unit

The recoverable amount is calculated by the value in use based on the three-year business plan that was prepared by reflecting past experiences and external information and that was approved by management. After the three-year business plan, the Group sets a growth rate from 1.2% in the fourth year (2017: 1.6%) to 1.2% in the ninth year (2017: 1.0%), and the same growth rate as the ninth year from the tenth year as a continued growth rate for inflation.

The discount rate before taxes is 4.0% (2017: 3.9%). The value in use sufficiently exceeds the carrying amount of the cash-generating unit. Therefore, even in cases where the discount rate and growth rate used in calculating the value in use fluctuate within reasonable ranges, the Group assumes that the value in use will not become less than the carrying amount.

(4) Impairment Losses

Goodwill is allocated to cash-generating units that are identified according to locations and types of businesses. The grouping of intangible assets for impairment test is the smallest cash-generating unit that independently generates cash inflow.

The Group recognized impairment losses of ¥1,019 million for the year ended December 31, 2017, and ¥2,406 million for the year ended December 31, 2018 in "Selling, general and administrative expenses" in the consolidated statement of income.

Impairment losses recognized in the year ended December 31, 2018 represent the losses incurred to reduce the carrying amounts to the recoverable amounts of software and other intangible assets since the recoverable amounts were lower than the carrying amounts.

The recoverable amounts of these assets are calculated mainly by their values in use.

15. Lease Transactions

The Group leases factory sites, vehicles and other assets as a lessee. Some of the lease contracts have renewal options or escalation clauses. There are no restrictions on additional debt and further leasing imposed by the lease arrangements.

(1) Present Value of Finance Lease Obligations

The total of future minimum lease payments for leased assets recognized based on the finance lease contracts, their present value and future financial costs as of December 31 are as follows:

		Millions of yen
	2017	2018
Not later than 1 year		
Total of future minimum lease payments	¥ 1,630	**¥ 1,305**
Future financial costs	284	**263**
Present value	1,346	**1,042**
Later than 1 year and not later than five years		
Total of future minimum lease payments	3,503	**3,305**
Future financial costs	1,203	**1,191**
Present value	2,300	**2,114**
Later than 5 years		
Total of future minimum lease payments	9,626	**8,790**
Future financial costs	2,605	**2,139**
Present value	7,021	**6,651**
Total		
Total of future minimum lease payments	14,760	**13,401**
Future financial costs	4,092	**3,593**
Present value	10,667	**9,807**

(2) Future Minimum Lease Payments under Non-cancellable Operating Leases

The total of future minimum lease payments under non-cancellable operating leases as of December 31 is as follows:

		Millions of yen
	2017	2018
Not later than 1 year	¥ 8,059	**¥11,841**
Later than 1 year and not later than 5 years	10,719	**15,870**
Later than 5 years	9,217	**14,696**
Total	¥27,995	**¥42,407**

(3) Total of Minimum Lease Payments and Contingent Rents

The total of minimum lease payments and contingent rents of operating lease contracts recognized as an expense for each year is as follows:

		Millions of yen
	2017	2018
Total of minimum lease payments	¥10,220	**¥13,445**
Contingent rents	1,135	**1,188**

16. Investment Property

(1) Schedule of Investment Property

The schedule of the carrying amount of "Investment property" for each year is as follows:

		Millions of yen
	2017	2018
As of January 1	¥18,184	**¥16,700**
Expenditure after acquisition	305	**338**
Transfer from property, plant and equipment	1,732	**3,215**
Acquisition by business combination	—	**139**
Transfer to non-current assets held-for-sale	(2,777)	**(1,171)**
Depreciation	(570)	**(573)**
Impairment losses	—	**(754)**
Sale or disposal	(162)	**(303)**
Exchange differences on translation of foreign operations	6	**(6)**
Other	(17)	**(28)**
As of December 31	¥16,700	**¥17,558**
Acquisition cost as of January 1	¥51,245	**¥45,768**
Accumulated depreciation and accumulated impairment losses as of January 1	33,061	**29,068**
Acquisition cost as of December 31	45,768	**38,355**
Accumulated depreciation and accumulated impairment losses as of December 31	29,068	**20,797**

(2) Fair Value

The fair value of investment property is determined based on a valuation conducted by an external real estate appraiser. The valuation is made in accordance with the appraisal standards of the country where the investment property is located and based on market evidence of transaction prices for similar assets.

The fair value hierarchy of investment property is categorized from Level 1 to Level 3 as follows:

Level 1: Fair value measured at the quoted price in the active market
Level 2: Fair value that is calculated using the observable price other than categorized in Level 1 directly or indirectly
Level 3: Fair value that is calculated based on valuation techniques which include inputs that are not based on observable market data

The fair value of investment property based on the fair value hierarchy as of December 31 is as follows:

				Millions of yen
				As of December 31, 2017
	Level 1	Level 2	Level 3	Total
Investment property	¥ —	¥34,646	¥1,921	¥36,567

				Millions of yen
				As of December 31, 2018
	Level 1	Level 2	Level 3	Total
Investment property	**¥ —**	**¥34,678**	**¥2,485**	**¥37,164**

(3) Impairment Losses

The grouping of investment properties for impairment test is based on the smallest cash-generating unit that independently generates cash inflow. Impairment test for idle properties is carried out individually.

The Group recognized impairment losses of ¥754 million for the year ended December 31, 2018 in "Selling, general and administrative expenses" in the consolidated statement of income.

Impairment losses recognized for the year ended December 31, 2018 represent the difference between the recoverable amount and the carrying amount of land and buildings as idle properties were decided individual demolition. The recoverable amount is calculated based on value in use basis, which is "zero" for buildings due to the decision of demolition, and the recoverable amount of other properties is calculated by the fair value less costs of disposal.

17. Income Taxes

(1) Deferred Tax Assets and Deferred Tax Liabilities

The breakdown and schedule of "Deferred tax assets" and "Deferred tax liabilities" by major causes of their occurrence for each year are as follows:

Year ended December 31, 2017

					Millions of yen
Deferred Tax Assets	As of January 1, 2017	Recognized in profit or loss	Recognized in other comprehensive income	Other (Note 1)	As of December 31, 2017
Fixed assets (Note 2)	¥136,713	¥(15,864)	¥ —	¥ 3,859	¥124,709
Retirement benefits	79,940	(6,395)	(2,135)	2,211	73,621
Carryforward of unused tax losses	53,135	399	—	1,694	55,228
Other	75,971	(4,222)	(177)	2,860	74,433
Subtotal	345,760	(26,082)	(2,312)	10,625	327,991
Valuation allowance	(61,231)	(1,527)	(269)	(2,347)	(65,374)
Total	¥284,528	¥(27,609)	¥(2,581)	¥ 8,278	¥262,617

					Millions of yen
Deferred Tax Liabilities	As of January 1, 2017	Recognized in profit or loss	Recognized in other comprehensive income	Other (Note 1)	As of December 31, 2017
Fixed assets (Note 2)	¥ (73,805)	¥ 1,677	¥ —	¥(12,577)	¥ (84,705)
Retirement benefits	(4,506)	(232)	(3,971)	(534)	(9,244)
Other	(111,260)	(3,539)	(5,196)	(2,568)	(122,563)
Total	¥(189,572)	¥(2,093)	¥(9,167)	¥(15,679)	¥(216,511)

Year ended December 31, 2018

					Millions of yen
Deferred Tax Assets	As of January 1, 2018	Recognized in profit or loss	Recognized in other comprehensive income	Other (Note 1)	As of December 31, 2018
Fixed assets (Note 2)	¥124,709	¥(10,763)	¥ —	¥(1,436)	¥112,509
Retirement benefits	73,621	(1,563)	1,731	(1,543)	72,248
Carryforward of unused tax losses	55,228	(589)	—	(1,513)	53,126
Other	74,433	13,522	(2,043)	(1,697)	84,215
Subtotal	327,991	607	(312)	(6,188)	322,098
Valuation allowance	(65,374)	(1,012)	(1,248)	1,648	(65,986)
Total	¥262,617	¥ (406)	¥(1,560)	¥(4,540)	¥256,112

					Millions of yen
Deferred Tax Liabilities	As of January 1, 2018	Recognized in profit or loss	Recognized in other comprehensive income	Other (Note 1)	As of December 31, 2018
Fixed assets (Note 2)	¥ (84,705)	¥5,971	¥ —	¥(12,944)	¥ (91,678)
Retirement benefits	(9,244)	(1,530)	(254)	902	(10,125)
Other	(122,563)	(5,001)	4,337	5,529	(117,697)
Total	¥(216,511)	¥ (559)	¥4,083	¥ (6,513)	¥(219,500)

(Note 1) "Other" includes exchange differences on translation of foreign operations and acquisition through business combinations.
(Note 2) "Fixed assets" include property, plant and equipment, goodwill, intangible assets and investment property.

The deferred tax assets are recognized for the amount considered to be recoverable on deductible temporary differences, carryforward of unused tax losses and tax credits by taking taxable temporary differences and future taxable profits plan into account. The carryforward of unused tax losses, for which the deferred tax assets are not recognized, was ¥46,809 million (including ¥11,903 million, for which the carryforward expires after five years) as of December 31, 2017, and ¥44,610 million (including ¥15,696 million, for which the carryforward expires after five years) as of December 31, 2018. Tax credits, for which the deferred tax assets are not recognized, were ¥5,185 million (including ¥4,810 million, for which the carryforward expires after five years) as of December 31, 2017, and ¥5,417 million (including ¥5,183 million, for which the carryforward expires after five years) as of December 31, 2018.

(2) Income Taxes

The breakdown of "Income taxes" for each year is as follows:

		Millions of yen
	2017	2018
Current income taxes	¥112,081	¥143,090
Deferred income taxes	29,702	965
Total income taxes	¥141,783	¥144,055

Deferred income taxes decreased by ¥801 million and increased by ¥96 million for the years ended December 31, 2017 and 2018, respectively, due to the effect of changes in tax rates in Japan and other countries.

(3) Reconciliation of the Effective Tax Rate

The breakdown of major items that caused differences between the effective statutory tax rate and the average actual tax rate for each year is as follows:

The Company is subject mainly to corporate tax, inhabitant tax and enterprise tax, and the effective statutory tax rate for each year calculated based on these taxes was 30.66%. Foreign subsidiaries are subject to income taxes at their locations.

	2017	% 2018
Effective statutory tax rate	30.66	**30.66**
Different tax rates applied to foreign subsidiaries	(8.86)	**(9.57)**
Non-deductible expenses	0.95	**1.13**
Valuation allowance	1.54	**0.95**
Withholding tax in foreign countries	1.29	**1.50**
Tax contingencies	1.26	**2.32**
Other	(0.52)	**0.11**
Average actual tax rate	26.33	**27.10**

18. Trade and Other Payables

The breakdown of "Trade and other payables" as of December 31 is as follows:

	2017	Millions of yen 2018
Accounts payable	¥218,378	**¥197,426**
Other payables	66,864	**68,246**
Other	110,491	**114,844**
Total	¥395,733	**¥380,516**

Trade and other payables are classified as financial liabilities measured at amortized cost.

19. Bonds and Borrowings (Including Other Financial Liabilities)

(1) Breakdown of Financial Liabilities

The breakdown of "Bonds and borrowings" and "Other financial liabilities" as of December 31 is as follows:

	Millions of yen		
	2017	2018	Due
Derivative liabilities	¥ 5,425	**¥ 3,176**	—
Short-term borrowings	274,233	**165,985**	—
Commercial paper	66,808	**72,038**	—
Current portion of long-term borrowings	690	**12,443**	—
Current portion of bonds (Note)	56,451	**—**	—
Long-term borrowings	71,164	**116,870**	2020–2028
Bonds (Note)	275,791	**610,444**	—
Other	12,494	**11,377**	—
Total	¥763,056	**¥992,334**	
Current liabilities	¥405,088	**¥254,953**	
Non-current liabilities	357,968	**737,381**	
Total	¥763,056	**¥992,334**	

(Note) The summary of the issuing conditions of the bonds is as follows:

			Millions of yen		%		
Company	Name of bond	Date of issuance	As of December 31, 2017	As of December 31, 2018	Interest rate	Collateral	Date of maturity
Japan Tobacco Inc.	8th domestic straight bond	December 9, 2010	20,000	**20,000**	1.300	Yes	December 9, 2020
Japan Tobacco Inc.	9th domestic straight bond	July 15, 2015	60,000	**60,000**	0.217	Yes	July 15, 2020
Japan Tobacco Inc.	10th domestic straight bond	July 15, 2015	30,000	**30,000**	0.358	Yes	July 15, 2022
Japan Tobacco Inc.	11th domestic straight bond	July 15, 2015	25,000	**25,000**	0.599	Yes	July 15, 2025
Japan Tobacco Inc.	12th domestic straight bond	September 10, 2018	—	**60,000**	0.110	Yes	September 8, 2023
Japan Tobacco Inc.	13th domestic straight bond	September 10, 2018	—	**30,000**	0.355	Yes	September 8, 2028
Japan Tobacco Inc.	14th domestic straight bond	September 10, 2018	—	**10,000**	0.758	Yes	September 10, 2038
Japan Tobacco Inc.	Straight bond in USD	July 23, 2013	56,451 (56,451) [USD 500 mil.]	**—**	2.100	Yes	July 23, 2018
Japan Tobacco Inc.	Straight bond in USD	April 13, 2016	84,556 [USD 750 mil.]	**83,116 [USD 750 mil.]**	2.000	Yes	April 13, 2021
Japan Tobacco Inc.	Straight bond in USD	April 13, 2016	56,235 [USD 500 mil.]	**55,268 [USD 500 mil.]**	2.800	Yes	April 13, 2026
JT International Financial Services B.V.	Straight bond in USD	September 28, 2018	—	**57,871 [USD 525 mil.]**	3.500	No	September 28, 2023
JT International Financial Services B.V.	Straight bond in USD	September 28, 2018	—	**54,827 [USD 500 mil.]**	3.875	No	September 28, 2028
JT International Financial Services B.V.	Straight bond in EUR	September 28, 2018	—	**69,134 [EUR 550 mil.]**	1.125	No	September 28, 2025
JT International Financial Services B.V.	Straight bond in GBP	September 28, 2018	—	**55,228 [GBP 400 mil.]**	2.750	No	September 28, 2033
Total			332,242 (56,451)	**610,444 (—)**			

(Note 1) The figure in parentheses ( ) represents the amount of the current portion of the bond.
(Note 2) The figure in parentheses [ ] represents the amount of foreign currency-denominated bond.

Derivative liabilities are classified as financial liabilities measured at fair value through profit or loss excluding those to which hedge accounting is applied, and bonds and borrowings are classified as financial liabilities measured at amortized cost.

There are no financial covenants that have a significant impact on the bonds and borrowings of the Group.

(2) Assets Pledged as Collateral for Liabilities

A. Pursuant to the provisions of Article 6 of the Japan Tobacco Inc. Act, the Company's properties are pledged as general collateral for bonds issued by the Company. Bondholders are entitled to claim satisfaction in preference to unsecured creditors of the Company properties (with the exception of national and local taxes and certain other statutory obligations).

B. Assets pledged as collateral by some subsidiaries are ¥1,097 million and ¥2,138 million as of December 31, 2017 and 2018, respectively. Their corresponding debts are ¥241 million and ¥71 million as of December 31, 2017 and 2018, respectively.

20. Provisions

The breakdown and schedule of "Provisions" for each year are as follows:

Year ended December 31, 2017

Millions of yen

	Asset retirement provisions	Restructuring provisions	Provisions for sales rebates	Other provisions	Total
As of January 1, 2017	¥3,348	¥9,124	¥3,459	¥1,021	¥16,952
Provisions	169	5,709	3,312	2,443	11,633
Interest cost associated with passage of time	40	—	—	—	40
Provisions used	(94)	(6,829)	(3,459)	(135)	(10,516)
Provisions reversed	(1)	(1,350)	—	(178)	(1,529)
Exchange differences on translation of foreign operations	—	418	—	34	453
As of December 31, 2017	¥3,463	¥7,074	¥3,312	¥3,185	¥17,033
Current liabilities	¥ —	¥6,739	¥3,312	¥2,977	¥13,028
Non-current liabilities	3,463	335	—	208	4,005
Total	¥3,463	¥7,074	¥3,312	¥3,185	¥17,033

Year ended December 31, 2018

Millions of yen

	Asset retirement provisions	Restructuring provisions	Provisions for sales rebates	Other provisions	Total
As of January 1, 2018	**¥3,463**	**¥7,074**	**¥3,312**	**¥3,185**	**¥17,033**
Provisions	**157**	**1,657**	**3,668**	**657**	**6,138**
Interest cost associated with passage of time	**29**	**—**	**—**	**—**	**29**
Provisions used	**(70)**	**(7,590)**	**(3,312)**	**(309)**	**(11,280)**
Provisions reversed	**—**	**(686)**	**—**	**(1,058)**	**(1,744)**
Exchange differences on translation of foreign operations	**—**	**(133)**	**—**	**(185)**	**(318)**
As of December 31, 2018	**¥3,579**	**¥ 322**	**¥3,668**	**¥2,289**	**¥ 9,858**
Current liabilities	**¥ —**	**¥ 309**	**¥3,668**	**¥2,101**	**¥ 6,078**
Non-current liabilities	**3,579**	**12**	**—**	**189**	**3,780**
Total	**¥3,579**	**¥ 322**	**¥3,668**	**¥2,289**	**¥ 9,858**

A. Asset Retirement Provisions

In order to settle the obligation of restoring and of removing hazardous substances from plant facilities and premises that the Group uses, the probable amount to be paid in the future is recognized based on past performances. These expenses are expected to be paid after one year or more; however, they may be affected by future business plans.

B. Restructuring Provisions

These provisions are mainly related to business integration and measures for the rationalization of the "International Tobacco Business." The timing of the payment may be affected by future business plans.

C. Provisions for Sales Rebates

These provisions are for contracts which reward the customers with discounts when the sales volume or sales amount in a given period exceeds a specified volume or amount and correspond to "Refund liabilities" in IFRS 15 "Revenue from Contracts with Customers." They are expected to be paid within one year.

21. Other Liabilities

The breakdown of "Other current liabilities" and "Other non-current liabilities" as of December 31 is as follows:

Millions of yen

	2017	2018
Tobacco excise tax payables	¥265,343	**¥297,728**
Tobacco special excise tax payables	11,989	**10,562**
Tobacco local excise tax payables	167,420	**163,704**
Consumption tax payables	103,511	**95,781**
Bonus to employees	31,412	**38,977**
Employees' unused paid vacations liabilities	18,741	**19,130**
Other	140,685	**269,582**
Total	¥739,101	**¥895,464**
Current liabilities	¥618,322	**¥716,190**
Non-current liabilities	120,779	**179,274**
Total	¥739,101	**¥895,464**

22. Employee Benefits

(1) Post-employment Benefits

The Group sponsors funded or unfunded defined benefit plans and defined contribution plans as employee retirement benefit plans. The benefits of defined benefit plans are predetermined based on conditions, such as points employees have gained in compensation for each year of service, the payment rate, years of service, and average salaries in their final years of service before retirement.

The Company is obligated to bear pension costs for a mutual assistance association incurred with respect to services in or before June 1956 (prior to enforcement of the Act on the Mutual Aid Association of Public Corporation Employees). Such obligations are recognized as liabilities at their present value using the actuarial valuation method and are included in retirement benefit liabilities.

Special termination benefits may be provided to employees on their early retirements under certain circumstances.

The Company and its subsidiary transferred a portion of their pension plans from a defined benefit plan to a defined contribution plan as of April 1, 2018.

The funded defined benefit plans are administrated by the Group or the fund that is legally separated from the Group in accordance with statutory requirements. The Group, or the board of the pension fund and the trustee of the plan, are required by law to act in the best interests of the plan participants, and are responsible for managing the plan assets in accordance with the designated investment strategy.

The Group's main defined benefit plans expose the Group to actuarial risks, such as investment risk, interest rate risk, inflation risk, and longevity risk.

(i) Investment risk

The present value of the defined benefit obligations is calculated using a discount rate set with reference to a yield on high quality corporate bonds or government bonds. If the return on the plan assets is below this yield, there is a possibility that the plan is underfunded.

(ii) Interest rate risk

A decrease in a yield on high quality corporate bonds or government bonds will increase the present value of the defined benefit obligations. However, this will be partially offset by an increase in the fair value of the debt instruments (plan assets).

(iii) Inflation risk

The level of benefit for certain defined benefit plans of the Group is linked to inflation. Accordingly, a rise in inflation will increase the present value of the defined benefit obligations.

(iv) Longevity risk

Some defined benefit plans of the Group provide a lifetime annuity, and the Group is obligated to provide pension benefits to the plan participants for the rest of their lives after their retirements. The present value of the defined benefit obligations is calculated by reference to the best estimate of the mortality of plan participants during or after employment. An increase in average life expectancy of the plan participants will increase the defined benefit obligations.

A. Schedule of Defined Benefit Obligations

The schedule of the defined benefit obligations is as follows:

	Japan (Note 3)	Overseas	Total
			Millions of yen
As of January 1, 2017 (Notes 1, 2)	¥260,122	¥516,875	¥776,997
Current service cost	10,978	9,408	20,386
Past service cost and settlement	(222)	(8,263)	(8,485)
Interest expense	1,213	11,272	12,485
Contributions by plan participants	—	1,470	1,470
Remeasurement gains and losses:			
Actuarial gains and losses arising from changes in demographic assumptions	2	(4,437)	(4,435)
Actuarial gains and losses arising from changes in financial assumptions	27	248	276
Actuarial gains and losses arising from experience adjustments	(714)	(3,608)	(4,322)
Benefits paid	(21,435)	(26,974)	(48,410)
Exchange differences on translation of foreign operations	—	32,870	32,870
Other	1	1,554	1,554
As of December 31, 2017 (Notes 1, 2)	249,972	530,415	780,386
Current service cost	**10,214**	**9,348**	**19,562**
Past service cost and settlement	**(26,868)**	**450**	**(26,418)**
Interest expense	**1,049**	**10,646**	**11,695**
Contributions by plan participants	**—**	**1,675**	**1,675**
Remeasurement gains and losses:			
Actuarial gains and losses arising from changes in demographic assumptions	**(249)**	**(1,189)**	**(1,438)**
Actuarial gains and losses arising from changes in financial assumptions	**(85)**	**(9,860)**	**(9,946)**
Actuarial gains and losses arising from experience adjustments	**3,350**	**1,255**	**4,605**
Benefits paid	**(21,159)**	**(23,942)**	**(45,101)**
Exchange differences on translation of foreign operations	**—**	**(34,097)**	**(34,097)**
Other	**—**	**263**	**263**
As of December 31, 2018 (Notes 1, 2)	**¥216,223**	**¥484,964**	**¥701,187**

(Note 1) The Group's weighted-average duration of the defined benefit obligations is 7.1 years for Japan and 15.1 years for overseas (2017: 7.7 years for Japan and 15.7 years for overseas).

(Note 2) The Group's breakdown of the defined benefit obligation by plan participant is as follows:

	As of December 31, 2017			As of December 31, 2018		
	Japan	Overseas	Total	Japan	Overseas	Total
						Millions of yen
Active members	¥163,592	¥184,639	¥348,231	**¥140,274**	**¥158,329**	**¥298,603**
Deferred members	15,102	73,182	88,284	**13,158**	**74,678**	**87,836**
Pensioners	71,278	272,594	343,872	**62,792**	**251,957**	**314,748**
Total	¥249,972	¥530,415	¥780,386	**¥216,223**	**¥484,964**	**¥701,187**

(Note 3) The schedule of mutual pension benefits obligations included in the category of Japan is as follows:

	2017	2018
		Millions of yen
As of January 1	¥48,607	**¥42,284**
Interest expense	146	**127**
Remeasurement gains and losses	(1,081)	**(875)**
Benefits paid	(5,387)	**(4,861)**
As of December 31	¥42,284	**¥36,675**

B. Schedule of Plan Assets

The schedule of the plan assets is as follows:

	Japan	Overseas	Total
			Millions of yen
As of January 1, 2017	¥93,571	¥373,696	¥467,267
Interest income	456	8,424	8,879
Remeasurement gains and losses:			
Return on plan assets (excluding amounts included in interest income)	1,223	16,430	17,653
Contributions by the employer (Notes 1, 2)	1,690	10,172	11,862
Contributions by plan participants	—	1,470	1,470
Benefits paid	(6,943)	(22,174)	(29,116)
Exchange differences on translation of foreign operations	—	22,986	22,986
As of December 31, 2017	89,998	411,004	501,002
Interest income	**322**	**8,460**	**8,782**
Decrease due to settlement	**(22,481)**	**—**	**(22,481)**
Remeasurement gains and losses:			
Return on plan assets (excluding amounts included in interest income)	**(31)**	**(11,420)**	**(11,451)**
Contributions by the employer (Notes 1, 2)	**1,159**	**10,885**	**12,044**
Contributions by plan participants	**—**	**1,675**	**1,675**
Benefits paid	**(6,180)**	**(19,163)**	**(25,343)**
Exchange differences on translation of foreign operations	**—**	**(27,738)**	**(27,738)**
As of December 31, 2018	**¥62,788**	**¥373,702**	**¥436,489**

(Note 1) Pursuant to laws and regulations, the Group and the pension fund review the financial condition of the pension plan regularly and recalculate contributions for allocating future benefit and keeping the balance of the pension financing when the plan is underfunded.

(Note 2) The Group plans to pay contributions of ¥6,300 million in the year ending December 31, 2019.

C. Reconciliation of Defined Benefit Obligations and Plan Assets

The reconciliation of the defined benefit obligations and plan assets to the net defined benefit liabilities (assets) recognized in the consolidated statement of financial position as of December 31 is as follows:

As of December 31, 2017

	Japan	Overseas	Total
			Millions of yen
Present value of the funded defined benefit obligations	¥ 87,999	¥382,679	¥470,678
Fair value of the plan assets	(89,998)	(411,004)	(501,002)
Subtotal	(1,998)	(28,325)	(30,324)
Present value of the unfunded defined benefit obligations	161,973	147,736	309,709
Net defined benefit liabilities (assets) recognized in the consolidated statement of financial position	¥159,974	¥119,411	¥279,385
Retirement benefit liabilities	¥164,793	¥165,969	¥330,762
Retirement benefit assets	(4,818)	(46,558)	(51,377)
Net defined benefit liabilities (assets) recognized in the consolidated statement of financial position	¥159,974	¥119,411	¥279,385

As of December 31, 2018

	Japan	Overseas	Total
			Millions of yen
Present value of the funded defined benefit obligations	**¥ 60,453**	**¥343,304**	**¥403,757**
Fair value of the plan assets	**(62,788)**	**(373,702)**	**(436,489)**
Subtotal	**(2,334)**	**(30,398)**	**(32,732)**
Present value of the unfunded defined benefit obligations	**155,770**	**141,660**	**297,430**
Net defined benefit liabilities (assets) recognized in the consolidated statement of financial position	**¥153,435**	**¥111,262**	**¥264,697**
Retirement benefit liabilities	**¥158,297**	**¥163,541**	**¥321,838**
Retirement benefit assets	**(4,861)**	**(52,279)**	**(57,140)**
Net defined benefit liabilities (assets) recognized in the consolidated statement of financial position	**¥153,435**	**¥111,262**	**¥264,697**

D. Major Breakdown of Plan Assets

The breakdown of plan assets by major category as of December 31 is as follows:

Japan

	As of December 31, 2017			**As of December 31, 2018**		
	Market price in an active market			Market price in an active market		**Millions of yen**
	Quoted	Unquoted	Total	Quoted	Unquoted	Total
Cash and cash equivalents	¥12,243	¥ —	¥12,243	**¥ 7,183**	**¥ —**	**¥ 7,183**
Equity instruments	3,939	—	3,939	**3,052**	**—**	**3,052**
Japan	2,065	—	2,065	**1,530**	**—**	**1,530**
Overseas	1,874	—	1,874	**1,523**	**—**	**1,523**
Debt instruments	10,512	—	10,512	**10,388**	**—**	**10,388**
Japan	9,220	—	9,220	**9,147**	**—**	**9,147**
Overseas	1,292	—	1,292	**1,242**	**—**	**1,242**
General account of life insurance companies (Note)	—	61,241	61,241	**—**	**40,309**	**40,309**
Other	1,433	629	2,062	**1,208**	**646**	**1,855**
Total	¥28,127	¥61,870	¥89,998	**¥21,832**	**¥40,956**	**¥62,788**

Overseas

	As of December 31, 2017			**As of December 31, 2018**		
	Market price in an active market			Market price in an active market		**Millions of yen**
	Quoted	Unquoted	Total	Quoted	Unquoted	Total
Cash and cash equivalents	¥ 29,815	¥ —	¥ 29,815	**¥ 15,269**	**¥ —**	**¥ 15,269**
Equity instruments	65,725	—	65,725	**47,856**	**—**	**47,856**
United Kingdom	5,093	—	5,093	**3,871**	**—**	**3,871**
North America	23,487	—	23,487	**17,539**	**—**	**17,539**
Other	37,144	—	37,144	**26,445**	**—**	**26,445**
Debt instruments	273,724	5,593	279,317	**277,109**	**5,134**	**282,242**
United Kingdom	185,607	—	185,607	**195,193**	**—**	**195,193**
North America	46,723	—	46,723	**39,583**	**0**	**39,583**
Other	41,394	5,593	46,988	**42,333**	**5,134**	**47,466**
Real estate	10,035	258	10,293	**11,581**	**65**	**11,646**
Other	17,187	8,667	25,854	**8,206**	**8,482**	**16,688**
Total	¥396,485	¥14,519	¥411,004	**¥360,021**	**¥13,681**	**¥373,702**

Total

	As of December 31, 2017			**As of December 31, 2018**		
	Market price in an active market			Market price in an active market		**Millions of yen**
	Quoted	Unquoted	Total	Quoted	Unquoted	Total
Cash and cash equivalents	¥ 42,058	¥ —	¥ 42,058	**¥ 22,452**	**¥ —**	**¥ 22,452**
Equity instruments	69,664	—	69,664	**50,908**	**—**	**50,908**
Debt instruments	284,236	5,593	289,829	**287,497**	**5,134**	**292,631**
Real estate	10,035	258	10,293	**11,581**	**65**	**11,646**
General account of life insurance companies (Note)	—	61,241	61,241	**—**	**40,309**	**40,309**
Other	18,620	9,297	27,916	**9,414**	**9,129**	**18,543**
Total	¥424,612	¥76,389	¥501,002	**¥381,852**	**¥54,637**	**¥436,489**

(Note) A certain interest rate and principal for the general account of life insurance are guaranteed by life insurance companies.

The investment strategy for the Group's major plans is as follows:

(Japan)

The Company's pension fund is managed in accordance with the internal policy for securing stable profits in the middle- and long-term in order to ensure the redemption of the plan liability. Concretely, by setting a target rate of return and composition ratio of plan assets by asset category within the risk tolerance that is annually assessed, the Company invests plan assets consistently with the composition ratio. When reviewing the composition ratio, the Company considers introducing an asset investment which has a high correlation with the liability.

In the case where an unexpected situation occurs in the market environment, it is temporarily allowed to make an adjustment on the weight of risk assets complying with the policy.

(Overseas)

The investment strategy for the foreign subsidiaries' funded pension plans is decided properly by the trustee of the plan or the management of overseas subsidiaries according to local legislation. The Company's objective for the foreign subsidiaries' funded pension plans is to manage risks arising from its defined benefit obligation, and meanwhile to achieve a return on assets in excess of the movement in the value of the defined benefit obligation.

The majority of the plan assets have been allocated to liability matching bonds and the remaining parts of the plan assets are mainly invested in equities targeting long-term return.

E. Matters Related to Actuarial Assumptions

The major items of actuarial assumptions as of December 31 are as follows:

	As of December 31, 2017		**As of December 31, 2018**	
				%
	Japan	Overseas	Japan	Overseas
Discount rate	0.5	2.1	**0.5**	**2.2**
Inflation rate	—	2.4	**—**	**2.4**

As of December 31, 2017

	Japan		Overseas	
				Years
	Males	Females	Males	Females
Average life expectancy at retirement (Note 1)				
Current pensioners	23.6 (Note 2)	29.3 (Note 2)	21.9 (Note 3)	24.2 (Note 3)
Future pensioners			23.2 (Note 4)	25.5 (Note 4)

As of December 31, 2018

	Japan		Overseas	
				Years
	Males	Females	Males	Females
Average life expectancy at retirement (Note 1)				
Current pensioners	23.6 (Note 2)	29.3 (Note 2)	**22.0** (Note 3)	**24.2** (Note 3)
Future pensioners			**23.4** (Note 4)	**25.5** (Note 4)

(Note 1) The average life expectancies underlie the values of the defined benefit obligations on major plans. Assumptions regarding future mortality rate are based on published statistics and mortality tables.
(Note 2) Life expectancy for a pensioner currently aged 60. Regardless of the plan participant's current age, the Group performs actuarial calculations based on the assumption that life expectancy remains the same.
(Note 3) Life expectancy for a pensioner currently aged 65.
(Note 4) Life expectancy at the age of 65 for an active member currently aged 50.
(Note 5) The valuation of defined benefit obligations reflects a judgment on uncertain future events. The sensitivities of defined benefit obligations due to changes in major assumptions as of December 31 are as follows. Each of these sensitivities assumes that other variables remain fixed; however, in fact, they do not always change independently. Negative figures show a decrease in pension plan obligations, while positive figures show an increase.

		As of December 31, 2017		**As of December 31, 2018**	
					Millions of yen
	Change in assumptions	Japan	Overseas	Japan	Overseas
Discount rate	Increase by 0.5%	¥(9,259)	¥(39,316)	**¥(7,192)**	**¥(34,758)**
	Decrease by 0.5%	9,971	44,188	**7,711**	**38,496**
Inflation rate	Increase by 0.5%	—	26,909	**—**	**23,889**
	Decrease by 0.5%	—	(25,490)	**—**	**(22,326)**
Mortality rate	Extended 1 year	4,956	17,777	**4,420**	**16,812**
	Shortened 1 year	(4,794)	(18,423)	**(4,267)**	**(16,915)**

F. Breakdown of Defined Benefit Cost

The breakdown of defined benefit cost for each year is as follows:

Year ended December 31, 2017

			Millions of yen
	Japan	Overseas	Total
Current service cost	¥10,978	¥ 9,408	¥ 20,386
Past service cost and gains and losses on settlement	(222)	(8,263)	(8,485)
Interest expense (income)	757	2,849	3,605
Defined benefit cost through profit or loss	11,514	3,993	15,507
Actuarial gains and losses arising from changes in demographic assumptions	2	(4,437)	(4,435)
Actuarial gains and losses arising from changes in financial assumptions	27	248	276
Actuarial gains and losses arising from experience adjustments	(714)	(3,608)	(4,322)
Return on plan assets (excluding amounts included in interest income)	(1,223)	(16,430)	(17,653)
Defined benefit cost through other comprehensive income	¥ (1,908)	¥(24,226)	¥(26,135)
Total of defined benefit cost	¥ 9,605	¥(20,233)	¥(10,628)

Year ended December 31, 2018

			Millions of yen
	Japan	Overseas	Total
Current service cost	**¥10,214**	**¥ 9,348**	**¥19,562**
Past service cost and gains and losses on settlement	**(4,388)**	**450**	**(3,937)**
Interest expense (income)	**727**	**2,186**	**2,913**
Defined benefit cost through profit or loss	**6,553**	**11,985**	**18,538**
Actuarial gains and losses arising from changes in demographic assumptions	**(249)**	**(1,189)**	**(1,438)**
Actuarial gains and losses arising from changes in financial assumptions	**(85)**	**(9,860)**	**(9,946)**
Actuarial gains and losses arising from experience adjustments	**3,350**	**1,255**	**4,605**
Return on plan assets (excluding amounts included in interest income)	**31**	**11,420**	**11,451**
Defined benefit cost through other comprehensive income	**¥ 3,047**	**¥ 1,626**	**¥ 4,673**
Total of defined benefit cost	**¥ 9,600**	**¥13,611**	**¥23,210**

(Note 1) The net amount of interest expense and interest income is included in "Financial costs." Other expenses are included in "Cost of sales" and "Selling, general and administrative expenses."
(Note 2) Contributions to the defined contribution plans were ¥7,383 million for the year ended December 31, 2017 and ¥11,517 million for the year ended December 31, 2018 and were not included in the table above.

(2) Other Employee Benefit Expenses

The employee benefit expenses other than post-employment benefits that are included in the consolidated statement of income for each year are as follows:

		Millions of yen
	2017	**2018**
Remuneration and salary	¥221,896	**¥236,971**
Bonus to employees	60,274	**67,379**
Legal welfare expenses	43,192	**44,535**
Welfare expenses	37,399	**39,086**
Termination benefits	1,577	**(304)**

23. Equity and Other Equity Items

(1) Share Capital and Capital Surplus

A. Authorized Shares

The number of authorized shares as of December 31, 2017 and 2018 is 8,000,000 thousand ordinary shares.

B. Fully Paid Issued Shares

The schedule of the number of issued shares and share capital is as follows:

	Thousands of shares		Millions of yen
	Number of ordinary issued shares	Share capital	Capital surplus
As of January 1, 2017	2,000,000	¥100,000	¥736,400
Increase (decrease)	—	—	—
As of December 31, 2017	2,000,000	100,000	736,400
Increase (decrease)	—	—	—
As of December 31, 2018	**2,000,000**	**¥100,000**	**¥736,400**

(Note) The shares issued by the Company are non-par value ordinary shares that have no restriction on any content of rights.

(2) Treasury Shares

The schedule of the number of treasury shares and its amount as of each year end is as follows:

	Thousands of shares	Millions of yen
	Number of shares	Amount
As of January 1, 2017	209,044	¥443,822
Increase (decrease) (Note 2)	(88)	(186)
As of December 31, 2017	208,957	443,636
Increase (decrease) (Note 2)	**(380)**	**(807)**
As of December 31, 2018	**208,577**	**¥442,829**

(Note 1) The Company adopts share option plans and utilizes treasury shares for delivery of shares due to its exercise. Contract conditions and amounts are described in "33. Share-based Payments."
(Note 2) Purchases of shares less than one unit are 0 thousand shares for the year ended December 31, 2017 and 0 thousand shares for the year ended December 31, 2018. The number of shares delivered upon exercise of share options is 88 thousand shares for the year ended December 31, 2017 and 380 thousand shares for the year ended December 31, 2018.

(3) Other Components of Equity

A. Subscription Rights to Shares

The Company adopts share option plans and issues subscription rights to shares based on the Companies Act. Contract conditions and amount are described in "33. Share-based Payments."

B. Exchange Differences on Translation of Foreign Operations

Exchange differences on translation of foreign operations are composed of foreign currency translation difference that occurs when consolidating financial statements of foreign subsidiaries prepared in foreign currencies, and the effective portion of net gain (loss) on the hedging instruments designated as hedge of net investment.

C. Net Gain (Loss) on Derivatives Designated as Cash Flow Hedges

The Group uses derivatives for hedging to avoid the risk of fluctuation in future cash flows. This is the effective portion of changes in the fair value of hedging instruments designated as cash flow hedges.

D. Net Gain (Loss) on Revaluation of Financial Assets Measured at Fair Value through Other Comprehensive Income

This is the valuation difference in the fair value of financial assets measured at fair value through other comprehensive income.

E. Remeasurements of Defined Benefit Plans

Remeasurements of defined benefit plans comprise actuarial gains and losses, the return on plan assets excluding amounts included in interest income, and any change in the effect of the asset ceiling excluding amounts included in interest income. In addition, actuarial gains and losses are the effects of differences between the actuarial assumptions at the beginning of the year and what has actually occurred, and the effects of changes in actuarial assumptions. Remeasurements are recognized as other comprehensive income when they occur and are transferred immediately from other components of equity to retained earnings.

24. Dividends

Dividends paid for each year are as follows:

Year ended December 31, 2017

		Millions of yen	Yen		
	Class of shares	Total dividends	Dividends per share	Basis date	Effective date
(Resolution) Annual Shareholders' Meeting (March 24, 2017)	Ordinary shares	¥118,203	¥66	December 31, 2016	March 27, 2017
Board of Directors (August 2, 2017)	Ordinary shares	125,369	70	June 30, 2017	September 1, 2017

Year ended December 31, 2018

		Millions of yen	Yen		
	Class of shares	Total dividends	Dividends per share	Basis date	Effective date
(Resolution) Annual Shareholders' Meeting (March 27, 2018)	**Ordinary shares**	**¥125,373**	**¥70**	**December 31, 2017**	**March 28, 2018**
Board of Directors (August 1, 2018)	**Ordinary shares**	**134,351**	**75**	**June 30, 2018**	**September 3, 2018**

Dividends for which the effective date falls in the following year are as follows:

Year ended December 31, 2017

		Millions of yen	Yen		
	Class of shares	Total dividends	Dividends per share	Basis date	Effective date
(Resolution) Annual Shareholders' Meeting (March 27, 2018)	Ordinary shares	¥125,373	¥70	December 31, 2017	March 28, 2018

Year ended December 31, 2018

		Millions of yen	Yen		
	Class of shares	Total dividends	Dividends per share	Basis date	Effective date
(Resolution) Annual Shareholders' Meeting (March 20, 2019)	**Ordinary shares**	**¥134,357**	**¥75**	**December 31, 2018**	**March 22, 2019**

25. Revenue

(1) Disaggregation of Revenue

The disaggregation of "Revenue" for the year ended December 31, 2018 is as follows. The amounts are presented after eliminations of intercompany transactions.

Year ended December 31, 2018

	Reportable Segments					**Millions of yen**
	Domestic Tobacco	International Tobacco	Pharmaceuticals	Processed Food	Other	Consolidated
Core revenue from tobacco business	**¥582,379**	**¥1,250,719**	**¥ —**	**¥ —**	**¥ —**	**¥1,833,098**
Other	**39,047**	**61,622**	**113,992**	**161,387**	**6,815**	**382,864**
	¥621,426	**¥1,312,342**	**¥113,992**	**¥161,387**	**¥6,815**	**¥2,215,962**

A. Domestic and International Tobacco Businesses

Domestic and international tobacco businesses engage in the sale of tobacco products.

Revenue from sales of products is recognized upon delivery of the products because the customer obtains control of the products upon delivery, by which the Group evaluates that the performance obligation is satisfied. Revenue is measured at the consideration promised in a contract with a customer, less discounts, rebates and taxes, including consumption tax. In addition, where the Group makes payments to the customer, except the case when consideration payable to the customer is a payment for a distinct product or service from the customer, revenue is measured at the amount which is consideration promised with the customer, less consideration payable to the customer.

Considerations for transactions are received mainly within one year from satisfying their performance obligations and includes no significant financing components.

The tobacco excise taxes and other transactions in which the Group is involved as an agency are excluded from revenue. The inflow of economic benefits after deducting the tobacco excise taxes and other transactions is presented as "Revenue" in the consolidated statement of income.

B. Pharmaceutical Business

Pharmaceutical business mainly engages in the sale of prescription drugs and licensing.

Revenue from sales of products is recognized upon delivery of the products because the customer obtains control of the products upon delivery, by which the Group evaluates that the performance obligation is satisfied. Revenue is measured at the consideration promised in a contract with a customer, less discounts, rebates and taxes, including consumption tax. In addition, where the Group makes payments to the customer, except the case when consideration payable to the customer is a payment for a distinct product or service from the customer, revenue is measured at the amount which is consideration promised with the customer, less consideration payable to the customer.

Revenue from licensing is generated by licensing out the rights to develop and market of each compound to licensees in the development stage, and the Group receives upfront income, milestone revenue and sales-based royalties. Upfront income is recognized at the time the customer obtains control of the license. Milestone revenue is recognized at the time the milestone agreed between the parties such as the progress of development is achieved. Sales-based royalties are measured based on the Group's licensees' sales, and recognized by taking into consideration the timing of occurrence.

Considerations for transactions are received mainly within one year from satisfying their performance obligations and includes no significant financial component.

C. Processed Foods Business

Processed foods business engages in the sale of frozen and ambient processed foods, bakery products and seasonings.

Revenue from sales of products is recognized upon delivery of the products because the customer obtains control of the products upon delivery, by which the Group evaluates that the performance obligation is satisfied. Revenue is measured at the consideration promised in a contract with a customer, less discounts, rebates and taxes, including consumption tax. In addition, where the Group makes payments to the customer, except the case when consideration payable to the customer is a payment for a distinct product or service from the customer, revenue is measured at the amount which is consideration promised with the customer, less consideration payable to the customer.

Considerations for transactions are received mainly within one year from satisfying their performance obligations and includes no significant financial component.

Transactions in which the Group is involved as an agency are excluded from revenue. The inflow of economic benefits after deducting these transactions is presented as "Revenue" in the consolidated statement of income.

(2) Transaction Price Allocated to the Remaining Performance Obligations

The Group uses the practical expedient and does not disclose information on the remaining performance obligations because it has no significant transactions with initial expected contractual terms exceeding one year. There are no significant amounts of considerations from contracts with customers that are not included in transaction prices.

(3) Gross Turnover

The reconciliation from "Gross turnover" to "Revenue" for each year is as follows:

		Millions of yen
	2017	2018
Gross turnover	¥ 7,286,883	**¥ 7,532,248**
Tobacco excise taxes and agency transaction amount	(5,147,230)	**(5,316,285)**
Revenue	¥ 2,139,653	**¥ 2,215,962**

The tobacco excise taxes and other transactions in which the Group is involved as an agency are excluded from revenue. The inflow of economic benefits after deducting the tobacco excise taxes and other transactions is presented as "Revenue" in the consolidated statement of income.

Gross turnover is an item that the Group discloses voluntarily and is not "Revenue" as defined by IFRS.

26. Other Operating Income

The breakdown of "Other operating income" for each year is as follows:

		Millions of yen
	2017	2018
Gain on sale of property, plant and equipment, intangible assets and investment properties (Notes 1, 2)	¥24,025	**¥39,402**
Reversal of impairment losses on investments in associates	8,848	**—**
Other (Note 2)	12,851	**9,129**
Total	¥45,724	**¥48,532**

(Note 1) The amount of gain on sale for the year ended December 31, 2018 mainly relates to the sale of the old plant sites.
(Note 2) The amount of restructuring incomes included in each account is as follows:

		Millions of yen
	2017	2018
Gain on sale of property, plant and equipment, intangible assets and investment properties	¥21,616	**¥38,559**
Other	29	**725**
Total	¥21,645	**¥39,284**

27. Selling, General and Administrative Expenses

The breakdown of "Selling, general and administrative expenses" for each year is as follows:

		Millions of yen
	2017	2018
Advertising expenses	¥ 24,413	**¥ 29,111**
Promotion expenses	112,212	**106,199**
Commission	54,458	**52,749**
Employee benefit expenses (Note 2)	254,045	**268,956**
Research and development expenses (Note 1)	60,600	**65,377**
Depreciation and amortization	81,298	**87,926**
Impairment losses on other than financial assets (Note 2)	3,427	**8,454**
Losses on sale and disposal of property, plant and equipment, intangible assets, and investment property (Note 2)	4,848	**8,845**
Other (Note 2)	191,610	**142,790**
Total	¥786,911	**¥770,407**

(Note 1) All research and development expenses are included in "Selling, general and administrative expenses."
(Note 2) The amount of restructuring costs included in each account is as follows:

		Millions of yen
	2017	2018
Employee benefit expenses	¥1,578	**¥ 24**
Impairment losses on other than financial assets	1,554	**3,105**
Losses on sale and disposal of property, plant and equipment, intangible assets, and investment property	1,224	**3,262**
Other	3,957	**1,530**
Total	¥8,314	**¥7,921**

28. Financial Income and Financial Costs

The breakdown of "Financial income" and "Financial costs" for each year is as follows:

		Millions of yen
Financial Income	2017	**2018**
Dividend income		
Financial assets measured at fair value through other comprehensive income	¥1,814	**¥2,056**
Interest income		
Financial assets measured at amortized cost		
Deposits and bonds	2,567	**3,695**
Other	399	**2**
Total	¥4,780	**¥5,754**

		Millions of yen
Financial Costs	2017	**2018**
Interest expenses		
Financial liabilities measured at amortized cost		
Bonds and borrowings (Note 2)	¥11,517	**¥16,267**
Other	87	**77**
Foreign exchange losses (Note 1)	11,257	**15,974**
Employee benefit expenses (Note 3)	3,605	**2,913**
Other	882	**4,022**
Total	¥27,349	**¥39,252**

(Note 1) Valuation gain (loss) of currency derivatives is included in foreign exchange losses.
(Note 2) Valuation gain (loss) of interest rate derivatives is included in interest expenses.
(Note 3) The employee benefit expenses are the net amount of interest cost and interest income related to employee benefits.

29. Other Comprehensive Income

Amount arising during the year, reclassification adjustments to profit or loss and tax effects for each component of "Other comprehensive income" for each year are as follows:

Year ended December 31, 2017

					Millions of yen
	Amount arising	Reclassification adjustments	Before tax effects	Tax effects	Net of tax effects
Items that will not be reclassified to profit or loss					
Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income	¥ 13,518	¥ —	¥ 13,518	¥ (4,116)	¥ 9,402
Remeasurements of defined benefit plans	26,135	—	26,135	(6,107)	20,028
Total of items that will not be reclassified to profit or loss	¥ 39,653	¥ —	¥ 39,653	¥(10,223)	¥ 29,430
Items that may be reclassified subsequently to profit or loss					
Exchange differences on translation of foreign operations	¥130,167	¥(341)	¥129,826	¥ (1,753)	¥128,073
Net gain (loss) on derivatives designated as cash flow hedges	(532)	455	(77)	23	(54)
Total of items that may be reclassified subsequently to profit or loss	¥129,634	¥ 115	¥129,749	¥ (1,730)	¥128,019
Total	¥169,287	¥ 115	¥169,402	¥(11,952)	¥157,449

Year ended December 31, 2018

					Millions of yen
	Amount arising	Reclassification adjustments	Before tax effects	Tax effects	Net of tax effects
Items that will not be reclassified to profit or loss					
Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income	**¥ (11,703)**	**¥ —**	**¥ (11,703)**	**¥ 3,488**	**¥ (8,215)**
Remeasurements of defined benefit plans	**(4,673)**	**—**	**(4,673)**	**1,478**	**(3,195)**
Total of items that will not be reclassified to profit or loss	**¥ (16,375)**	**¥ —**	**¥ (16,375)**	**¥ 4,965**	**¥ (11,410)**
Items that may be reclassified subsequently to profit or loss					
Exchange differences on translation of foreign operations	**¥(244,898)**	**¥(230)**	**¥(245,128)**	**¥(2,603)**	**¥(247,731)**
Net gain (loss) on derivatives designated as cash flow hedges	**1,138**	**236**	**1,374**	**(363)**	**1,012**
Total of items that may be reclassified subsequently to profit or loss	**¥(243,760)**	**¥ 6**	**¥(243,754)**	**¥(2,965)**	**¥(246,719)**
Total	**¥(260,135)**	**¥ 6**	**¥(260,129)**	**¥ 2,000**	**¥(258,129)**

30. Earnings per Share

(1) Basis of Calculating Basic Earnings per Share

A. Profit Attributable to Ordinary Shareholders of the Parent Company

		Millions of yen
	2017	**2018**
Profit for the period attributable to owners of the parent company	¥392,409	**385,677**
Profit not attributable to ordinary shareholders of the parent company	—	**—**
Profit for the period used for calculation of basic earnings per share	¥392,409	**385,677**

B. Weighted-average Number of Ordinary Shares Outstanding During the Period

		Thousands of shares
	2017	**2018**
Weighted-average number of shares during the period	1,790,995	**1,791,296**

(2) Basis of Calculating Diluted Earnings per Share

A. Profit Attributable to Diluted Ordinary Shareholders

		Millions of yen
	2017	**2018**
Profit for the period used for calculation of basic earnings per share	¥392,409	**¥385,677**
Adjustment	(0)	**—**
Profit for the period used for calculation of diluted earnings per share	¥392,409	**¥385,677**

B. Weighted-average Number of Diluted Ordinary Shares Outstanding During the Period

		Thousands of shares
	2017	**2018**
Weighted-average number of ordinary shares during the period	1,790,995	**1,791,296**
Increased number of ordinary shares under subscription rights to shares	1,042	**863**
Weighted-average number of diluted ordinary shares during the period	1,792,037	**1,792,159**

31. Non-cash Transactions

Significant Non-cash Transactions

The amount of assets acquired under finance leases was ¥3,599 million for the year ended December 31, 2017 and ¥1,041 million for the year ended December 31, 2018.

32. Reconciliation of Liabilities Arising from Financing Activities

Reconciliation of liabilities arising from financing activities for each year is as follows:

Year ended December 31, 2017

							Millions of yen
			Non-cash changes				
	As of January 1, 2017	Cash flows	Acquisition through business combinations	Foreign exchange movement	Fair value changes	Other	As of December 31, 2017
Short-term borrowings and commercial paper	¥187,949	¥116,371	¥35,349	¥ 1,373	¥ —	¥ —	¥341,041
Long-term borrowings (Note 1)	1,449	70,191	131	82	—	—	71,854
Bonds (Note 1)	358,158	(20,000)	—	(6,086)	—	169	332,242
Finance lease obligations	7,701	(1,373)	324	416	—	3,599	10,667
Derivatives (Note 2)	(3,052)	—	—	—	562	—	(2,490)
Total	¥552,205	¥165,189	¥35,804	¥(4,214)	¥562	¥3,768	¥753,314

Year ended December 31, 2018

							Millions of yen
			Non-cash changes				
	As of January 1, 2018	Cash flows	Acquisition through business combinations	Foreign exchange movement	Fair value changes	Other	**As of December 31, 2018**
Short-term borrowings and commercial paper	**¥341,041**	**¥(133,849)**	**¥49,137**	**¥(19,586)**	**¥ —**	**¥1,280**	**¥238,023**
Long-term borrowings (Note 1)	**71,854**	**56,425**	**1,795**	**(764)**	**—**	**2**	**129,313**
Bonds (Note 1)	**332,242**	**285,136**	**—**	**(7,346)**	**—**	**413**	**610,444**
Finance lease obligations	**10,667**	**(1,637)**	**—**	**(264)**	**—**	**1,041**	**9,807**
Derivatives (Note 2)	**(2,490)**	**2,294**	**—**	**—**	**196**	**—**	**—**
Total	**¥753,314**	**¥ 208,370**	**¥50,932**	**¥(27,960)**	**¥196**	**¥2,736**	**¥987,588**

(Note 1) Current portion is included.
(Note 2) Derivatives are held for the purpose of hedging bonds.

33. Share-based Payments

The Company and Torii Pharmaceutical adopt share option plans. Share options are granted by the resolutions of the Board of Directors based on the approvals at the Annual Shareholders' Meeting.

The outline of the share option plan of the Company is as follows:

(1) Share Option Contract Conditions of the Company

Positions of persons granted : Directors and Executive Officers
Settlement : Issuance of shares
Effective period of granted share option : 30 years after the date of grant
Vesting conditions : None

Conditions related to the exercise of share options are as follows:

A. The subscription rights to shares become exercisable when a holder of a subscription right to shares no longer holds a position as a director, an audit & supervisory board member or an executive officer. In the subscription rights to shares allocation contract with holders of such rights, it is provided for that the rights become exercisable from the date following the date on which they no longer hold their positions.
B. In the case where any holders of subscription rights to shares waive such rights, they cannot exercise them.

(2) Changes in the Number of Share Options of the Company

						Shares
			2017			2018
	Directors	Executive Officers	Total	Directors	Executive Officers	Total
Balance as of January 1	275,800	701,000	976,800	**328,800**	**702,400**	**1,031,200**
Granted	53,000	89,400	142,400	**68,800**	**109,400**	**178,200**
Exercised	—	(88,000)	(88,000)	**—**	**(380,000)**	**(380,000)**
Transferred	—	—	—	**(202,200)**	**202,200**	**—**
Balance as of December 31	328,800	702,400	1,031,200	**195,400**	**634,000**	**829,400**
Exercisable balance as of December 31	—	378,800	378,800	**—**	**239,600**	**239,600**

(Note 1) The number of share options is presented as the number of underlying shares.
(Note 2) All share options are granted with an exercise price of ¥1 per share.
(Note 3) Share options are granted to 5 directors and 19 executive officers for the year ended December 31, 2017, and 5 directors and 18 executive officers for the year ended December 31, 2018.
"Transferred" included in the "Changes in the Number of Share Options" represents the number of share options for persons granted whose management position changed during the period.
(Note 4) The weighted-average fair values per share of share options granted during the period were ¥2,411 and ¥1,500 for the years ended December 31, 2017 and 2018, respectively.
(Note 5) The weighted-average share prices of share options at the time of exercise during the period were ¥3,810 and ¥3,086 for the years ended December 31, 2017 and 2018, respectively.
(Note 6) The weighted-average remaining contract years of unexercised share options at the end of each period were 25.0 years and 25.4 years for the years ended December 31, 2017 and 2018, respectively.

(3) Method of Measuring Fair Value of Share Options Granted During the Period of the Company

A. Valuation Model

Black-Scholes Model

B. Main Assumptions and Estimation

	2017	2018
Share price	¥3,950	**¥3,013**
Volatility of share price (Note 1)	31.9%	**31.7%**
Estimated remaining period (Note 2)	15 years	**15 years**
Estimated dividends (Note 3)	¥130/share	**¥140/share**
Risk free interest rate (Note 4)	0.32%	**0.26%**

(Note 1) Calculated based on daily share prices quoted for the past 15 years.
(Note 2) Because of the difficulty of a reasonable estimation due to insufficient data, the remaining period is estimated based on the assumption that share option rights would be exercised at a midpoint of the exercise period.
(Note 3) Based on the latest dividends paid.
(Note 4) The yield on government bonds for a period of the expected remaining period.

(4) Share-based Payment Expenses

The costs for share options included in "Selling, general and administrative expenses" in the consolidated statement of income were ¥341 million and ¥275 million for the years ended December 31, 2017 and 2018, respectively.

34. Financial Instruments

(1) Capital Management

The Group's management principle is pursuit of the "4S" model: balancing the interests of consumers, shareholders, employees and wider society, and fulfilling our responsibilities towards them, aiming to exceed their expectations.

The Group believes that sustainable profit growth in the mid- to long-term based on this principle will increase the Group's value in the mid- to long-term, and is consequently in the best interest of all stakeholders, including our shareholders.

For that reason, as its financial policy, the Group maintains a strong financial base that secures stability in the case of changes in business environment such as economic crises, and flexibility enabling expeditious responses to business investment opportunities.

The Group manages net interest-bearing debt, where cash and cash equivalents are deducted from interest-bearing debt, and capital (the part attributable to the owners of the parent company). The amounts as of December 31 are as follows:

		Millions of yen
	2017	2018
Interest-bearing debt	¥ 755,804	**¥ 987,588**
Cash and cash equivalents	(285,486)	**(282,063)**
Net interest-bearing debt	470,318	**705,526**
Capital (equity attributable to owners of the parent company)	2,761,687	**2,630,594**

There are specific rules for shares of the Company under the Japan Tobacco Inc. Act, as follows:

The Japanese government shall hold more than one-third of all of the shares issued by the Company (excluding the type of shares, for which it is stipulated that voting rights may not be exercised on any matters that can be resolved by the Annual Shareholders' Meeting) (Article 2 (1)).

In cases where the Company intends to solicit persons to subscribe for shares to be issued or subscription rights to shares or where the Company intends to deliver shares (excluding treasury shares), subscription rights to shares (excluding subscription right to own shares) or bonds with subscription rights to shares (excluding bonds with subscription rights to shares) when exchanging with shares, the Company shall obtain the approval of the Minister of Finance (Article 2 (2)).

Disposal of shares owned by the Japanese government shall be within the limits on the number of shares decided by the Diet in the relevant annual budget (Article 3).

The Group monitors financial indicators in order to maintain a well-balanced capital structure that ensures an appropriate return on equity and a stable and flexible financial condition for future investment. We monitor credit ratings for financial stability and flexibility, and ROE (return on equity) for profitability, while focusing on changes in the domestic and overseas environment.

(2) Financial Risk Management

The Group is exposed to financial risks (credit risk, liquidity risk, foreign exchange risk, interest rate risk, and market price fluctuation risk) in the process of its management activities and it manages risks based on a specific policy in order to avoid or reduce said risks. The results of risk management are regularly reported by the Treasury Division to the president and the Board of Directors of the Company.

The Group policy limits derivatives to transactions for the purpose of mitigating risks from transactions based on actual demand. Therefore, we do not transact derivatives for speculation purposes or trading purposes.

(3) Credit Risk

Receivables, such as note and account receivables, acquired from the operating activities of the Group are exposed to customer credit risk.

The Group holds mainly debt securities for surplus investment and equity securities of customers and suppliers to strengthen relationships with them; those securities are exposed to the issuer's credit risk. In addition, through derivative transactions that the Group conducts in order to hedge foreign exchange fluctuation risks and interest rate fluctuation risks, we are exposed to the credit risk of the financial institutions which are counterparties to these transactions.

In principle, the Group sets credit lines or transaction conditions with respect to trade receivables for counterparties based on the Credit Management Guidelines in order to control the credit risk relating to counterparties. In addition, the receivable balances of counterparties with high credit risk are monitored. The Treasury Division of the Company regularly monitors the status of the occurrence and collection of bad debts, and reports them to the president and the Board of Directors of the Company.

With regard to the investment of cash surpluses and derivatives, the Group invests in debt securities and other financial instruments with a certain credit rating and transacts with financial institutions with a high credit rating in principle in order to prevent credit risks from occurring and based on the Group Financial Operation Basic Policy. In addition, the Treasury Division of the Company regularly monitors the performance of these transactions and reports the results to the president and the Board of Directors of the Company.

The maximum exposure pertaining to credit risks for financial assets is the carrying amount after considering impairment in the consolidated financial statements.

There is no excessive concentration of the credit risks to certain counterparties.

The analysis of the aging of financial assets that are past due but not impaired as of December 31, 2017 is as follows:

The financial assets include amounts considered recoverable by credit insurance and collateral.

As of December 31, 2017

					Millions of yen
	Total	Amount past due			
		Within 30 days	Over 30 days, within 60 days	Over 60 days, within 90 days	Over 90 days
Trade and other receivables	**¥6,347**	**¥4,724**	**¥814**	**¥214**	**¥595**

The Group reviews collectability of trade receivables depending on the credit conditions of counterparties and recognizes allowance for doubtful accounts. The schedule of the allowance for doubtful accounts is as follows.

The amounts of the allowance for doubtful accounts for the year ended December 31, 2017 are recognized based on IAS 39.

	Millions of yen
	2017
As of January 1, 2017	¥ 8,436
Addition	22,090
Decrease (intended use)	(780)
Decrease (reversal)	(127)
Other	539
As of December 31, 2017	¥30,158

					Millions of yen
	Trade receivables	Other financial assets			
		Measured at an amount equal to the 12-month expected credit losses	Measured at an amount equal to the full lifetime expected credit losses		
			Non-credit-impaired financial assets	Credit-impaired financial assets	Total
As of January 1, 2018	**¥23,589**	**¥—**	**¥317**	**¥6,252**	**¥30,158**
Addition	**228**	**—**	**13**	**906**	**1,147**
Decrease (intended use)	**(19,537)**	**—**	**(3)**	**(117)**	**(19,656)**
Decrease (reversal)	**(591)**	**—**	**(58)**	**(979)**	**(1,628)**
Other	**(2,040)**	**—**	**—**	**(223)**	**(2,263)**
As of December 31, 2018	**¥ 1,650**	**¥—**	**¥269**	**¥5,839**	**¥ 7,758**

(Note) There is no significant change in the carrying amounts of financial assets which affects the change in the allowance for doubtful accounts for the year ended December 31, 2018.

(4) Liquidity Risk

The Group raises funds by borrowings, commercial paper and bonds; however, these liabilities are exposed to the liquidity risk that we would not be able to repay liabilities on the due date due to the deterioration of the financing environment.

In accordance with the Group Financial Operation Basic Policy, the Group establishes a finance plan based on the annual business plan and the Treasury Division of the Company regularly monitors and collects information on the balance of liquidity-in-hand and interest-bearing debt and reports it to the president and the Board of Directors of the Company. In addition, the Group keeps necessary credit facilities to manage liquidity risk by having commitment lines with several financial institutions.

The financial liability balance (including derivative financial instruments) by maturity as of December 31 is as follows:

As of December 31, 2017

								Millions of yen
	Carrying amount	Contractual cash flow	Due within one year	Due after one year through two years	Due after two years through three years	Due after three years through four years	Due after four years through five years	Due after five years
Non-derivative financial liabilities								
Trade and other payables	¥ 395,733	¥ 395,733	¥395,733	¥ —	¥ —	¥ —	¥ —	¥ —
Short-term borrowings	274,233	274,233	274,233	—	—	—	—	—
Commercial paper	66,808	66,808	66,808	—	—	—	—	—
Current portion of long-term borrowings	690	690	690	—	—	—	—	—
Long-term borrowings	71,164	71,164	—	386	201	117	30,119	40,341
Current portion of bonds	56,451	56,500	56,500	—	—	—	—	—
Bonds	275,791	276,250	—	—	80,000	84,750	30,000	81,500
Subtotal	1,140,870	1,141,378	793,964	386	80,201	84,867	60,119	121,841
Derivative financial liabilities								
Foreign exchange forward contract	5,425	5,425	5,425	—	—	—	—	—
Subtotal	5,425	5,425	5,425	—	—	—	—	—
Total	¥1,146,295	¥1,146,803	¥799,389	¥386	¥80,201	¥84,867	¥60,119	¥121,841

As of December 31, 2018

								Millions of yen
	Carrying amount	Contractual cash flow	Due within one year	Due after one year through two years	Due after two years through three years	Due after three years through four years	Due after four years through five years	Due after five years
Non-derivative financial liabilities								
Trade and other payables	**¥ 380,516**	**¥ 380,516**	**¥380,516**	**¥ —**	**¥ —**	**¥ —**	**¥ —**	**¥ —**
Short-term borrowings	**165,985**	**165,985**	**165,985**	**—**	**—**	**—**	**—**	**—**
Commercial paper	**72,038**	**72,150**	**72,150**	**—**	**—**	**—**	**—**	**—**
Current portion of long-term borrowings	**12,443**	**12,443**	**12,443**	**—**	**—**	**—**	**—**	**—**
Long-term borrowings	**116,870**	**117,006**	**—**	**11,956**	**11,608**	**41,610**	**11,576**	**40,257**
Bonds	**610,444**	**613,773**	**—**	**80,000**	**83,250**	**30,000**	**118,275**	**302,248**
Subtotal	**1,358,297**	**1,361,873**	**631,094**	**91,956**	**94,858**	**71,610**	**129,851**	**342,505**
Derivative financial liabilities								
Foreign exchange forward contract	**3,176**	**3,176**	**3,176**	**—**	**—**	**—**	**—**	**—**
Subtotal	**3,176**	**3,176**	**3,176**	**—**	**—**	**—**	**—**	**—**
Total	**¥1,361,472**	**¥1,365,049**	**¥634,270**	**¥91,956**	**¥94,858**	**¥71,610**	**¥129,851**	**¥342,505**

The total of commitment lines and withdrawal as of December 31 are as follows:

		Millions of yen
	2017	**2018**
Total committed line of credit	¥601,580	**¥478,531**
Withdrawing	114,130	**—**
Unused balance	¥487,450	**¥478,531**

(5) Foreign Exchange Risk

The Group operates businesses globally and, therefore, is exposed to the following risks due to foreign exchange fluctuation:

(i) The risk where the profit or loss and cash flow in each functional currency of the Group is influenced by foreign exchange fluctuation as a result of external transactions and intergroup transactions, including the payment and receipt of dividends, in currencies that are different from each functional currency of the Group.

(ii) The risk that the equity of the Group is influenced by foreign exchange fluctuation when equity denominated in each functional currency of the Group is translated into Japanese yen and consolidated.

(iii) The risk that the profit or loss of the Group is influenced by foreign exchange fluctuation when profit or loss denominated in each functional currency of the Group is translated into Japanese yen and consolidated.

The Group hedges against risk (i) using derivatives or foreign currency-denominated interest-bearing debts for example, when future cash flow is projected or when receivables and payables are fixed, and some of them are designated as cash flow hedges.

The Group hedges against risk (ii) using foreign currency-denominated interest-bearing debts for example, and part of these are designated as net investment hedges. The Group does not hedge against risk (iii) in principle.

In order to mitigate risks mentioned above resulting from the foreign exchange fluctuation, in accordance with the Group Financial Operation Basic Policy, and under the supervision of the Financial Risk Management Committee of the Company, the Group establishes and implements a foreign currency hedge policy, taking into consideration the impact on the Group's performance and the current conditions of the foreign exchange market in a comprehensive manner. The Treasury Division of the Company regularly reports the performances to the president and the Board of Directors of the Company.

Foreign Exchange Sensitivity Analysis

In cases where each currency other than the functional currency that denominates the financial instruments held by the Group as of each year end increases by 10% in value against the functional currency, the impact on profit before income taxes in the consolidated statement of income is as follows:

The impact from the translation of functional currency-denominated financial instruments, and assets, liabilities, income and expenses of foreign operations into Japanese yen is not included. Also, it is based on the assumption that currencies other than the currencies used for the calculation do not fluctuate.

		Millions of yen
	2017	**2018**
Profit before income taxes	¥(9,473)	**¥(2,725)**

(6) Interest Rate Risk

Interest rate risk within the Group arises from interest-bearing debts after deducting cash equivalents. Borrowings and bonds with floating rates are exposed to interest rate fluctuation risk.

In order to reduce the interest rate fluctuation risk related to borrowings and bonds, in accordance with the Group Financial Operation Basic Policy, and under the supervision of the Financial Risk Management Committee of the Company, the Group establishes and implements an interest rate hedging policy, taking into consideration the impact on the Group's performance and the current condition of the interest rates in a comprehensive manner. The Treasury Division of the Company reports the performances to the president and the Board of Directors of the Company.

Interest Rate Sensitivity Analysis

In cases where the interest rate of financial instruments held by the Group as of each year end increases by 100bp, the impact on profit before income taxes in the consolidated statement of income is as follows:

The analysis is subject to financial instruments affected by interest rate fluctuation and based on the assumption that other factors, including the impacts of foreign exchange fluctuation, are constant.

		Millions of yen
	2017	**2018**
Profit before income taxes	¥(2,593)	**¥(955)**

(7) Hedging Transactions

The Group's policy for hedging transactions is stated in "3. Significant Accounting Policies."

A. Cash Flow Hedges

The details of hedging instruments designated as cash flow hedges are as follows:

As of December 31, 2017

	Contract amount	Over one year	Carrying amount (Note) (Millions of yen) Assets	Liabilities	Average rate, etc.
Foreign exchange risk					
Foreign exchange forward contract					
JPY/USD	USD 338 mil.	USD —	¥ 176	¥414	¥109.75
Interest rate risk					
Cross currency swap					
Fixed rate receipt and fixed rate payment	USD 175 mil.	USD —	2,490	—	0.24%

As of December 31, 2018

	Contract amount	Over one year		Carrying amount (Note) (Millions of yen) Assets	Liabilities	Average rate, etc.
Foreign exchange risk						
Foreign exchange forward contract						
JPY/USD	**USD 638 mil.**	**USD**	**—**	**¥1,329**	**¥613**	**¥109.21**
JPY/CNY	**CNY 49 mil.**	**CNY**	**—**	**—**	**8**	**¥15.92**

(Note) Carrying amounts of derivatives are presented as "Other financial assets" or "Other financial liabilities" in the consolidated statement of financial position, and the portion with over one year maturity is classified as "Non-current assets" or "Non-current liabilities."

The schedule of net gains (losses) on hedging instrument designated as cash flow hedges is as follows:

	Millions of yen Effective portion of changes in the fair value of cash flow hedges Foreign exchange risk	Interest rate risk	Total
As of January 1, 2017	¥ 367	¥ 73	¥ 440
Other comprehensive income			
Amount arising (Note 1)	30	(562)	(532)
Reclassification adjustments (Note 2)	(155)	611	455
Tax effects	39	(15)	23
Other	(475)	—	(475)
As of December 31, 2017	(195)	106	(88)
Other comprehensive income			
Amount arising (Note 1)	**1,334**	**(196)**	**1,138**
Reclassification adjustments (Note 2)	**194**	**42**	**236**
Tax effects	**(410)**	**47**	**(363)**
Other	**(480)**	**—**	**(480)**
As of December 31, 2018	**¥ 443**	**¥ —**	**¥ 443**

(Note 1) The change in value of the hedged item used as the basis for recognizing hedge ineffectiveness approximates the change in fair value of the hedging instrument.
(Note 2) The amount, which is reclassified when the hedged item affects profit or loss, is recognized in "Revenue," "Financial income" or "Financial costs" in the consolidated statement of income. The amount of hedge ineffectiveness is immaterial.

B. Hedge of Net Investment in Foreign Operations

The details of hedging instruments designated as hedge of net investment are mainly as follows:

As of December 31, 2017

	Contract amount	Over one year	Carrying amount (Note) (Millions of yen) Assets	Liabilities	Average rate, etc.
Bonds in USD	USD 1,575 mil.	USD 1,250 mil.	¥ —	¥177,467	¥107.36

As of December 31, 2018

	Contract amount	Over one year		Carrying amount (Note) (Millions of yen) Assets	Liabilities	Average rate, etc.
Bonds in USD	**USD 1,250 mil.**	**USD 1,250 mil.**		**¥ —**	**¥138,384**	**¥109.41**
Bonds in GBP	**GBP 400 mil.**	**GBP 400 mil.**		**—**	**55,216**	**$0.76**
Foreign exchange forward contract						
EUR / RUB	**RUB 19,973 mil.**	**RUB**	**—**	**516**	**338**	**€0.012**
USD / TWD	**TWD 6,113 mil.**	**TWD**	**—**	**67**	**—**	**$0.033**

(Note) Carrying amounts of bonds are presented as "Bonds and borrowings" in the consolidated statement of financial position, and the portion with over one year maturity is classified as "Non-current liabilities." Carrying amounts of derivatives are presented as "Other financial assets" or "Other financial liabilities" in the consolidated statement of financial position, and the portion with over one year maturity is classified as "Non-current assets" or "Non-current liabilities."

The schedule of net gains (losses) on hedging instrument designated as hedge of net investment in foreign operations is as follows:

	Millions of yen 2017	2018
As of January 1	¥ 8,784	**¥10,793**
Other comprehensive income		
Amount arising (Note 1)	3,763	**9,652**
Tax effects	(1,753)	**(2,603)**
As of December 31	¥10,793	**¥17,842**

(Note 1) The change in value of the hedged item used as the basis for recognizing hedge ineffectiveness approximates the change in fair value of the hedging instrument.
(Note 2) Net gain arising from the hedging instruments for which hedge accounting is discontinued were ¥16,936 million and ¥17,505 million as of December 31, 2017 and 2018 respectively those which are included in the exchange differences on translation of foreign operations.

(8) Market Price Fluctuation Risk

With respect to securities, the Group regularly assesses the fair value and financial conditions of the issuers, and each relevant department reviews the portfolio held by taking into account the relationship with counterparty entities as necessary.

(9) Fair Value of Financial Instruments

The fair value hierarchy of financial instruments is categorized from Level 1 to Level 3 as follows:

Level 1: Fair value measured at the quoted price in the active market
Level 2: Fair value that is calculated using the observable price other than categorized in Level 1 directly or indirectly
Level 3: Fair value that is calculated based on valuation techniques which include inputs that are not based on observable market data

A. Financial Instruments Measured at Amortized Cost

The carrying amount and fair value hierarchy of financial instruments measured at amortized cost as of December 31 are as follows:

As of December 31, 2017

	Millions of yen Carrying amount	Fair value Level 1	Level 2	Level 3	Total
Long-term borrowings (Note)	¥ 71,854	¥ —	¥ —	¥71,829	¥ 71,829
Bonds (Note)	332,242	331,998	—	—	331,998

As of December 31, 2018

	Millions of yen Carrying amount	Fair value Level 1	Level 2	Level 3	Total
Long-term borrowings (Note)	**¥129,313**	**¥ —**	**¥ —**	**¥129,978**	**¥129,978**
Bonds	**610,444**	**606,495**	**—**	**—**	**606,495**

(Note) Current portion is included.

With regard to short-term financial assets and short-term financial liabilities measured at amortized cost, their fair value approximates the carrying amount.

The fair value of long-term borrowings is calculated based on the present value which is obtained by discounting the total of the principal and interest by the interest rate assumed in a case where the same loan is newly made.

B. Financial Instruments Measured at Fair Value

The fair value hierarchy of financial instruments measured at fair value as of December 31 is as follows:

As of December 31, 2017

				Millions of yen
	Level 1	Level 2	Level 3 (Note)	Total
Derivative assets	¥ —	¥5,978	¥ —	¥ 5,978
Equity securities	71,859	—	5,783	77,642
Other	408	—	3,559	3,967
Total	¥72,267	¥5,978	¥9,342	¥87,587
Derivative liabilities	¥ —	¥5,425	¥ —	¥ 5,425
Total	¥ —	¥5,425	¥ —	¥ 5,425

As of December 31, 2018

				Millions of yen
	Level 1	Level 2	Level 3 (Note)	Total
Derivative assets	**¥ —**	**¥ 8,653**	**¥ —**	**¥ 8,653**
Equity securities	**58,847**	**—**	**5,837**	**64,684**
Other	**401**	**11,025**	**4,514**	**15,940**
Total	**¥59,248**	**¥19,677**	**¥10,351**	**¥89,277**
Derivative liabilities	**¥ —**	**¥ 3,176**	**¥ —**	**¥ 3,176**
Total	**¥ —**	**¥ 3,176**	**¥ —**	**¥ 3,176**

(Note) The schedule of financial instruments that are classified in Level 3 is as follows:

		Millions of yen
	2017	2018
As of January 1	¥7,202	**¥ 9,342**
Total gain (loss)		
Profit or loss (Note 1)	391	**(341)**
Other comprehensive income (Note 2)	914	**(1003)**
Purchases	995	**2,270**
Sales	(159)	**(81)**
Other	—	**164**
As of December 31	¥9,342	**¥10,351**

(Note 1) Gains and losses included in profit or loss for the years ended December 31, 2017 and 2018 are related to financial assets measured at fair value through profit or loss as of the year end. These gains and losses are included in "Financial income" and "Financial costs."
(Note 2) Gains and losses included in other comprehensive income for the years ended December 31, 2017 and 2018 are related to financial assets measured at fair value through other comprehensive income as of the year end. These gains and losses are included in "Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income."

35. Related Parties

Based on the Japan Tobacco Inc. Act, the Japanese government shall hold more than one-third of all of the shares issued by the Company (excluding the type of shares, for which it is stipulated that voting rights may not be exercised on any matters that can be resolved by Annual Shareholders' Meeting). As of December 31, 2018, the Japanese government held 33.35% of all outstanding shares of the Company.

(1) Related-party Transactions

Related-party transactions are conducted under the same conditions as regular business transactions.

The Group's revenue from CJSC TK Megapolis, the local Russian distribution affiliate, was ¥216,852 million and ¥216,913 million for the years ended December 31, 2017 and 2018, respectively. The Group held trade receivables of ¥49,097 million and ¥44,436 million from CJSC TK Megapolis as of December 31, 2017 and 2018, respectively.

(2) Remuneration for Directors and Audit and Supervisory Board Members

Remuneration for directors and audit and supervisory board members for each year is as follows:

		Millions of yen
	2017	2018
Remuneration and bonuses	¥540	**¥795**
Share-based payments	120	**109**
Total	¥660	**¥904**

36. Subsidiaries, Associates and Others

(The composition of the Group)

The composition of the Group by reportable segment as of December 31 is as follows:

	2017		2018	
Reportable Segments	Number of subsidiaries	Number of entities accounted for using the equity method (Note)	Number of subsidiaries	Number of entities accounted for using the equity method (Note)
Domestic Tobacco	13	2	**13**	**1**
International Tobacco	156	5	**166**	**5**
Pharmaceuticals	2	—	**2**	**—**
Processed Food	28	3	**29**	**3**
Other	11	3	**14**	**2**
Total	210	13	**224**	**11**

(Note) No associates or joint ventures are considered to be material to the Group.

There is no significant change in the composition of the Group for the year ended December 31, 2018.

Regarding the restrictions on the ability to use the assets of the Group, please refer to "7. Cash and Cash Equivalents."

37. Commitments

(1) Commitments for the Acquisition of Assets

Commitments for the acquisition of assets as of December 31 are as follows:

		Millions of yen
	2017	2018
Acquisition of property, plant and equipment	¥74,732	**¥54,030**
Acquisition of intangible assets	3,103	**3,127**
Total	¥77,835	**¥57,157**

(2) Procurement of Domestic Leaf Tobacco

With regard to the procurement of domestic leaf tobacco by the Company, based on the Tobacco Business Act, the Company enters into purchase contracts with domestic leaf tobacco growers every year, and the contracts determine the area under cultivation by type of tobacco and the prices by type and quality of tobacco leaf. Under the contracts, the Company is obligated to purchase all domestic leaf tobacco produced pursuant to such contracts, except for any domestic leaf tobacco not suited for the manufacture of tobacco products.

38. Business Combinations

(1) Acquisition of the Tobacco Company in Russia

A. Summary of the Business Combination

On July 31, 2018, the Group acquired 100% of the outstanding shares of JSC Donskoy Tabak ("DT"), a company operating tobacco business in Russia (Note).

DT has well-established brands such as "Donskoy Tabak", "Kiss" and "Play" in the value segment, the largest and growing price segment in Russia.

The purpose of this acquisition is to expand brand portfolio in the value segment and strengthen a distribution and sales network in the Russian tobacco market, a cornerstone of the Group's earnings growth.

(Note) The acquisition also includes purchases of 100% of the outstanding shares of JSC Pereslavl-Tabak and 94.97% of the outstanding shares of Syneteristiki Kapnoviomihania Ellados Sekap S.A.

B. Financial Impact on the Group

Since the acquisition date, the acquired business has contributed to consolidated revenue of ¥12,682 million and consolidated operating profit of ¥304 million.

It is assumed that had the business been acquired on January 1, 2018, total consolidated revenue would have increased by ¥22,253 million to ¥2,238,215 million, and total consolidated operating profit would have decreased by ¥1,893 million to ¥563,091 million (Unaudited).

The above operating profit includes the amortization of trademarks acquired from the business combinations, etc.

C. Consideration and Details (Total of the Acquisition)

The consideration is ¥163,127 million and paid fully in cash.

Out of the total consideration, ¥134,644 million has been paid as of the year end and ¥28,484 million will be paid after the year end.

D. Net Cash Outflow for the Business Combination (Total of the Acquisition)

	Millions of yen
	Net cash outflow for the business combination
Cash consideration	¥163,127
Cash and cash equivalents in subsidiaries acquired	(293)
Net cash outflow for the business combination	¥162,834

E. Fair Values of the Assets Acquired and Liabilities Assumed

	Millions of yen
	Fair value
Current assets	¥ 44,762
Trademarks	60,353
Non-current assets	9,707
Total assets	¥114,822
Current liabilities	¥ 75,909
Non-current liabilities	44,494
Total liabilities	¥120,403
Non-controlling interests	(13)
Goodwill	¥168,696

Goodwill represents future economic benefits for integration synergies including enhanced business scale.

Fair value of assets acquired and liabilities assumed are provisional amounts recognized at the acquisition date and may change during the measurement period (one year from the acquisition date).

Transaction costs of ¥369 million are expensed as incurred and recognized in "Selling, general and administrative expense."

(2) Acquisition of the Tobacco Business in Bangladesh

A. Summary of the Business Combination

On November 29, 2018, the Group acquired the tobacco business of Akij Group ("Akij"), a tobacco business in Bangladesh.

Akij has well-established brands such as "Navy" and "Sheikh" in the value and base segments, together covering majority of the Bangladeshi tobacco market.

The purpose of this acquisition is to expand the presence in Bangladesh which is large and growing market.

(Note) The Group acquired 100% of the outstanding shares of United Dhaka Tobacco Company Limited, the entity taking over the tobacco business assets of Akij, as well as all tobacco related trademarks and design rights from Akij.

B. Financial Impact on the Group

Since the acquisition date, the acquired business has contributed to consolidated revenue of ¥1,345 million and consolidated operating loss of ¥454 million.

It is assumed that had the business been acquired on January 1, 2018, total consolidated revenue would have increased by ¥23,802 million to ¥2,239,765 million, and total consolidated operating profit would have decreased by ¥727 million to ¥564,257 million (Unaudited).

The above operating profit includes the amortization of trademarks acquired from the business combination, etc.

C. Consideration and Details (Total of the Acquisition)

The consideration is ¥174,019 million and paid fully in cash.

Out of the total consideration, ¥111,066 million has been paid as of the year end and ¥62,953 million will be paid after the year end.

D. Net Cash Outflow for the Business Combination (Total of the Acquisition)

	Millions of yen
	Net cash outflow for the business combination
Cash consideration	¥174,019
Cash and cash equivalents in subsidiaries acquired	(388)
Net cash outflow for the business combination	¥173,632

E. Fair Values of the Assets Acquired and Liabilities Assumed

	Millions of yen
	Fair value
Current assets	¥ 15,725
Trademarks	43,498
Non-current assets	16,468
Total assets	¥ 75,691
Current liabilities	¥ 5,149
Non-current liabilities	4,665
Total liabilities	¥ 9,814
Goodwill	¥108,142

Goodwill represents future economic benefits for integration synergies including enhanced business scale.

Fair value of assets acquired and liabilities assumed are provisional amounts recognized at the acquisition date and may change during the measurement period (one year from the acquisition date).

Transaction costs of ¥516 million are expensed as incurred and recognized in "Selling, general and administrative expense."

(3) Other Acquisitions

The information on the business combinations other than the above for the year ended December 31, 2018, is omitted as it is immaterial both individually and in the aggregate.

39. Contingencies

Contingent Liabilities

The Company and some of its subsidiaries are defendants in legal proceedings. Provisions are not accounted for in matters where it is not practicable to reasonably estimate the final outcomes.

The Company and some of its subsidiaries, who are defendants in such legal proceedings, believe that our defenses asserted in these proceedings are based on substantial evidence and implement the system for the response to action with the assistance of external lawyers.

(1) Smoking and Health Related Litigation

The Company and some of its subsidiaries are defendants in lawsuits filed by plaintiffs seeking damages for harm allegedly caused by smoking, the marketing of tobacco products, or exposure to tobacco smoke. As of December 31, 2018, there were a total of 21 smoking and health related cases pending in which one or more members of the Group were named as a defendant or for which the Company may have certain indemnity obligations pursuant to the agreement such as for the Company's acquisition of RJR Nabisco Inc.'s overseas (non-U.S.) tobacco operations.

The major ongoing smoking and health related cases are as follows:

On March 8, 2019, JTI-Macdonald Corp. (hereinafter referred to as "JTI-Mac"), the Company's Canadian subsidiary, filed for protection from its creditors under the Companies' Creditors Arrangement Act (CCAA). The Ontario Superior Court has granted the CCAA application and extended protection in favor of JTI-Mac. All of the below Canadian matters against JTI-Mac have been stayed by the court order. JTI-Mac carries on business in the ordinary course under the CCAA.

A. Individual Claim

There is one individual case brought against the Company's indemnitee in South Africa.

South Africa Individual Claim (Joselowitz):

The individual claim was brought against the Company's indemnitee in South Africa in October 2000. Plaintiff seeks compensatory and punitive damages, alleging that the Company's indemnitee marketed products which it knew to be dangerous to health, manipulated nicotine content to foster addiction, failed to comply with South African labeling requirements and participated in a clandestine worldwide operation to encourage children to smoke. This case has been dormant since February 2001.

In addition, there is one individual case (which is currently dormant) brought against the Company's subsidiary in Ireland.

B. Class Actions

There are eight ongoing class actions in Canada against the Company's subsidiary and/or indemnitees.

Canada Quebec Class Action (Cecilia Letourneau):

This class action was brought in September 1998 against three Canadian tobacco manufacturers including JTI-Mac. Plaintiffs were seeking a total of approximately ¥374.3 billion (approximately CAD 4.6 billion) in compensatory damages, an amount for which all the defendants are jointly and severally liable, and a total amount of approximately ¥374.3 billion (approximately CAD 4.6 billion) in punitive damages, to be divided among all the defendants based on their respective market shares.

The Quebec Superior Court published the first instance judgment in favor of the plaintiffs in June 2015. In June 2015, JTI-Mac and other tobacco manufacturers appealed the judgment to the Quebec Court of Appeal, and the appeal on the merits was heard and concluded in November 2016.

In March 2019, the Quebec Court of Appeal dismissed the appeal of defendants by substantively upholding the first instance judgment and ordering a punitive damage award against the appellants of approximately ¥13.1 billion (approximately CAD 161 million), in which the share of the total damage award against JTI-Mac is approximately ¥1.3 billion (approximately CAD 15 million).

Canada Quebec Class Action (Conseil Québécois sur le tabac et la santé):

This class action was brought in November 1998 against three Canadian tobacco manufacturers including JTI-Mac. Plaintiffs were seeking a total of approximately ¥1,013.9 billion (approximately CAD 12.4 billion) in compensatory damages, an amount for which all the defendants are jointly and severally liable, and a total amount of approximately ¥66.1 billion (approximately CAD 0.8 billion) in punitive damages, to be divided among all the defendants based on their respective market shares.

The Quebec Superior Court published the first instance judgment in favor of the plaintiffs in June 2015. In June 2015, JTI-Mac and other tobacco manufacturers appealed the judgment to the Quebec Court of Appeal, and the appeal on the merits was heard and concluded in November 2016.

In March 2019, the Quebec Court of Appeal dismissed the appeal of the defendants by substantively upholding the first instance judgment and ordering a compensatory damage award jointly and severally against the defendants of approximately ¥1,102.9 billion (approximately CAD 13.5 billion), in which the share of the total damage award against JTI-Mac is approximately ¥143.4 billion (approximately CAD 1.8 billion), and a punitive damage award of approximately ¥3 million (approximately CAD 0.04 million) per defendants.

The Quebec Court of Appeal rendered one judgment for both class actions against the defendants and ordered them to make an initial deposit of approximately ¥94.7 billion (approximately CAD 1.2 billion), in which the share of JTI-Mac is approximately ¥11.9 billion (approximately CAD 145 million).

Canada Saskatchewan Class Action (Adams):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2009. Plaintiffs are seeking unspecified compensatory and punitive damages on behalf of class members who allege to be or have been addicted to nicotine contained in cigarettes manufactured by the defendants. The preliminary motions are pending. The case is currently dormant.

Canada Manitoba Class Action (Kunta):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2009. Plaintiffs are seeking unspecified compensatory and punitive damages on behalf of class members who allege to be or have been addicted to nicotine contained in cigarettes manufactured by the defendants. The statement of claim was served on the Company's indemnitees but not on JTI-Mac. The case is currently dormant.

Canada Nova Scotia Class Action (Semple):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2009. Plaintiffs are seeking unspecified compensatory and punitive damages on behalf of class members who allege to be or have been addicted to nicotine contained in cigarettes manufactured by the defendants. The statement of claim was served on the Company's indemnitees but not on JTI-Mac. The case is currently dormant.

Canada British Columbia Class Action (Bourassa):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2010. Plaintiffs are seeking unspecified compensatory and punitive damages for class members. The preliminary motions are pending. The case is currently dormant.

Canada British Columbia Class Action (McDermid):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2010. Plaintiffs are seeking unspecified compensatory and punitive damages for class members. The preliminary motions are pending. The case is currently dormant.

Canada Ontario Class Action (Jacklin):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2012. Plaintiffs are seeking unspecified compensatory and punitive damages for class members. The preliminary motions are pending. The case is currently dormant.

In addition, there is one class action brought in Israel against an indemnitee of the Company's subsidiary.

C. Health-Care Cost Recovery Litigation

There are 10 ongoing health-care cost recovery cases in Canada pending against the Company's subsidiary and indemnitees brought by all the Canadian provinces (except three Canadian territories). These provinces filed lawsuits under their own provincial legislation which was enacted exclusively for the purpose of authorizing the provincial government to file a direct action against tobacco manufacturers to recoup the health-care costs the government has allegedly incurred and will incur, resulting from "tobacco related wrongs."

Canada British Columbia Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of British Columbia in January 2001 against tobacco industry members including JTI-Mac and the Company's indemnitees based on its provincial legislation, the "Tobacco Damages and Health-Care Costs Recovery Act." The claim amount is unspecified. In 2001, several defendants challenged the legislation's constitutionality, which was ultimately rejected by the Supreme Court of Canada in September 2005. The action remains pending in the first instance. The pre-trial process is ongoing. A trial date is not yet scheduled.

Canada New Brunswick Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of New Brunswick in March 2008 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The trial is set to begin in November 2019.

Canada Ontario Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of Ontario in September 2009 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The statement of claim contains allegations of joint and several liabilities among all the defendants but does not specify any individual amount or percentages within the total claimed amount of ¥4,076.0 billion (CAD 50.0 billion). The pre-trial process is ongoing. A trial date is not yet scheduled.

Canada Newfoundland and Labrador Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of Newfoundland and Labrador in February 2011 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The pre-trial process is ongoing. A trial date is not yet scheduled.

Canada Manitoba Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of Manitoba in May 2012 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The pre-trial process is ongoing. A trial date is not yet scheduled.

Canada Quebec Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of Quebec in June 2012 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The statement of claim contains allegations of joint and several liabilities among all the defendants but does not specify any individual amount or percentages within the total amount of the claim approximately ¥4,944.8 billion (approximately CAD 60.7 billion). The pre-trial process is ongoing. A trial date is not yet scheduled.

Canada Alberta Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of Alberta in June 2012 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The statement of claim contains allegations of joint and several liabilities among all the defendants but does not specify any individual amount or percentages within the total claimed amount of at least ¥815.2 billion (CAD 10.0 billion). The pre-trial process is ongoing. A trial date is not yet scheduled.

Canada Saskatchewan Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of Saskatchewan in June 2012 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The pre-trial process is ongoing. A trial date is not yet scheduled.

Canada Prince Edward Island Health-Care Cost Recovery Litigation:
This health-care cost recovery litigation was filed by the Province of Prince Edward Island in September 2012 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The pre-trial process is ongoing. A trial date is not yet scheduled.

Canada Nova Scotia Health-Care Cost Recovery Litigation:
This health-care cost recovery litigation was filed by the Province of Nova Scotia in January 2015 against tobacco industry members

including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The pre-trial process is ongoing. A trial date is not yet scheduled.

(2) Other Legal Proceedings

The Company and some of its subsidiaries are also engaged in other legal proceedings such as commercial and tax disputes.

(Note) The amount of damages sought denominated in foreign currencies is translated into Japanese yen at the rates as of December 31, 2018.

40. Subsequent Events

As part of the shareholder return based on our shareholder return policy, the Company's Board of Directors made a resolution on February 7, 2019 for the Company to acquire its own shares according to the particulars stated below pursuant to the provision of Article 156 of the Companies Act, as applied by replacing the relevant terms pursuant to the Act's provision of Article 165, paragraph 3.

a. Class of shares to be acquired
   Common stock
b. Number of shares to be acquired
   Up to 23,000,000 shares
c. Total payment amount to acquire shares
   Up to ¥50,000 million
d. Period of share acquisition
   From February 8, 2019 to April 22, 2019
e. Method of acquisition
   Purchase on the stock exchange via a trust bank

Consolidated Supplementary Information

A. Quarterly Information for the Year ended December 31, 2018

Millions of yen

	Q1 January 1, 2018 to March 31, 2018	Q2 January 1, 2018 to June 30, 2018	Q3 January 1, 2018 to September 30, 2018	2018 January 1, 2018 to December 31, 2018
Revenue	¥515,050	¥1,075,271	¥1,675,819	¥2,215,962
Profit before income taxes for the period (year)	139,891	290,367	449,402	531,486
Profit attributable to owners of the parent company for the period (year)	104,011	216,093	332,686	385,677
Basic earnings per share for the period (year) (yen)	58.07	120.64	185.73	215.31

	Q1 January 1, 2018 to March 31, 2018	Q2 April 1, 2018 to June 30, 2018	Q3 July 1, 2018 to September 30, 2018	Q4 October 1, 2018 to December 31, 2018
Basic earnings per share for the quarter (yen)	¥58.07	¥62.57	¥65.09	¥29.58

B. Significant Lawsuits

The significant lawsuits of the Group are as stated in "39. Contingencies" in the notes to consolidated financial statements.

Deloitte.

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of Japan Tobacco Inc.:

We have audited the accompanying consolidated statement of financial position of Japan Tobacco Inc. and its consolidated subsidiaries as of December 31, 2018, and the related consolidated statements of income, comprehensive income, changes in equity, and cash flows for the fiscal year from January 1, 2018 to December 31, 2018, and notes to consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in Japan. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Japan Tobacco Inc. and its consolidated subsidiaries as of December 31, 2018, and the consolidated results of their operations and their cash flows for the fiscal year then ended in accordance with International Financial Reporting Standards.

Emphasis of Matter

As discussed in Note 39, "Contingencies" to the consolidated financial statements, the Quebec Court of Appeal ordered JTI-Macdonald Corp. ("JTI-Mac"), the Company's Canadian subsidiary, a punitive damage award of approximately ¥1.3 billion for the Canada Quebec Class Action (Cecilia Letourneau), and a compensatory damage award of approximately ¥143.4 billion and a punitive damage award of approximately ¥3 million for the Canada Quebec Class Action (Conseil Québécois sur le tabac et la santé) in March 2019. JTI-Mac filed an application for protection from its creditors under the Companies' Creditors Arrangement Act ("CCAA") on March 8, 2019. The Ontario Superior Court has granted the CCAA application and extended protection in favor of JTI-Mac. All of the Canadian matters against JTI-Mac have been stayed by the court order. JTI-Mac carries on business in the ordinary course under the CCAA. Our opinion is not qualified in respect of this matter.

Deloitte Touche Tohmatsu LLC

March 20, 2019

Member of
Deloitte Touche Tohmatsu Limited

Unless otherwise stated, terms and numbers reported in this glossary are in accordance with IFRS.

Adjusted Operating Profit: Operating profit + Amortization cost of acquired intangibles arising from business acquisitions + Adjusted items (income and costs).*

* Adjusted items (income and costs) = Impairment losses on goodwill ± restructuring income and costs ± others

BnU: Billion Units.

Constant Exchange Rates: Constant exchange rates are computed by restating current year results at the previous year's foreign currency exchange rate. Results at constant rates of exchange should be considered in addition to, not as a substitute for, results reported in accordance with IFRS.

Contraband: Genuine products smuggled from abroad that are diverted from the legitimate supply chain and sold in a country other than the intended retail market without payment of domestic duty in that country.

Core Revenue (International Tobacco Business): Includes revenues from waterpipe tobacco and Reduced-Risk Products, but excludes revenues from distribution, contract manufacturing and other peripheral businesses.

Core Revenue (Japanese Domestic Tobacco Business): Excludes revenue from distribution of imported tobacco in the Japanese domestic tobacco business, among others, but includes revenue from domestic duty free, the China business and Reduced-Risk Products such as Ploom TECH devices and capsules.

Counterfeit: Fake products appearing to be genuine brand products protected by intellectual property rights. Counterfeit products are manufactured without authorization from the rights' owners and with the intent to copy the genuine brand to deceive the consumer. They are also sold without duties being paid.

FCF (Free Cash Flow): The sum of cash flows from operating activities and investing activities but excluding the following items:

- Cash flows from operating activities: interest received, dividends received, interest paid and the tax effect related to these items.
- Cash flows from investing activities: purchase of investment securities (both short-term and long-term), payments into time deposits, proceeds from sale or redemption of investment securities (both short-term and long-term), proceeds from withdrawal of time deposits and other investing activities not for business operation purposes.

FY2014: Results for the fiscal year ended December 31, 2014.

In FY2014, the Company and its subsidiaries with fiscal year-ends other than December 31 changed their fiscal year-ends to December 31.

The fiscal year-end for international business continued to be December 31 as before, hence the Group consolidated financial results of international business for the twelve-month period from January 1, 2014 to December 31, 2014 into the Group's consolidated financial results for the nine months ended December 31, 2014 (Reported basis).

For the purpose of fair comparison of business performance, we are providing figures for the twelve-month period from January 1, 2014 to December 31, 2014 (Like-for-Like basis) with regard to all business segments in continuing operations.

GFB: Global Flagship Brands (Winston, Camel, MEVIUS, LD).

IFRS: International Financial Reporting Standards.

Illicit Whites: Tobacco products manufactured legitimately but without any product flow control measures afterwards and, smuggled and sold in another market.

JPY BN: Billion Japanese Yen.

JT Cigarette Sales Volume (Japanese Domestic Tobacco Business): Excludes sales volume of domestic duty free, the China business and Reduced-Risk Products.

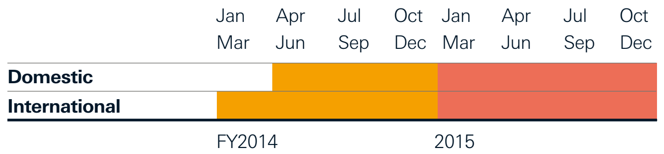
Profit: Profit attributable to owners of the parent.

Reduced-Risk Products (RRP): Products with the potential to reduce the risks associated with smoking.

Restated: See 'Constant Exchange Rates'.

Results for Nine Months ended December 31, 2014 (Reported Basis): For domestic businesses: consolidated nine-month results from April 1 to December 31, 2014.

For international business: consolidated twelve-month results from January 1 to December 31, 2014.



Results of Jan-Dec 2014 (Like-for-Like Basis): For the purpose of fair comparison of business performance, we are providing figures with regard to all business segments in continuing operations for January to December, 2014.

- Revenue, operating profit, adjusted operating profit from continuing operations and profit attributed to owners of the parent company from continuing and discontinued operations combined for January to December 2014 were disclosed in the 2015 Annual Securities Report, which was audited.

Revenue: Excluding tobacco excise taxes and revenue from agent transactions.

RMC: Ready-Made Cigarettes

TableMark: References to 'TableMark' are to TableMark Co., Ltd.

Total Shipment Volume (International Tobacco Business): Includes fine cut, cigars, pipe tobacco, snus and kretek, but excluding contract manufactured products, waterpipe tobacco and Reduced-Risk Products.

USD MM: Million US dollars.

As of December 31, 2018

Common Stock

Authorized:	8,000,000,000
Issued:	2,000,000,000
Number of shareholders:	394,994

Share Registrar
Mitsubishi UFJ Trust and Banking Corporation
4-5, Marunouchi 1-chome, Chiyoda-ku, Tokyo

Listing
Tokyo Stock Exchange: First Section

Composition of Shareholders (excluding treasury stock)

Minister of Finance	37.2%
Financial institutions	22.3%
Individuals and others	13.3%
Securities companies	3.6%
Other Japanese companies	1.3%
Foreign institutions, etc.	22.3%

Principal Shareholders	
Name	Shares held
Minister of Finance	666,926,200
Master Trust Bank of Japan, Ltd. (Trust Account)	91,137,400
Japan Trustee Services Bank, Ltd. (Trust Account)	68,848,700
Trust & Custody Services Bank, Ltd. as trustee for Mizuho Bank, Ltd. Retirement Benefit Trust Account re-entrusted by Mizuho Trust and Banking Co., Ltd.	23,660,000
State Street Bank and Trust Company 505223 (Standing proxy: Mizuho Bank, Ltd., Settlement Sales Department)	23,351,971
Japan Trustee Services Bank, Ltd. (Trust Account 5)	22,744,400
SSBTC Client Omnibus Account (Standing proxy: Hongkong and Shanghai Banking Corporation Limited, Tokyo Branch)	22,178,610
Japan Trustee Services Bank, Ltd. (Trust Account 9)	21,978,900
State Street Bank West Client-Treaty 505234 (Standing proxy: Mizuho Bank, Ltd., Settlement Sales Department)	20,542,232
JP Morgan Chase Bank 385151 (Standing proxy: Mizuho Bank, Ltd., Settlement Sales Department)	20,367,542

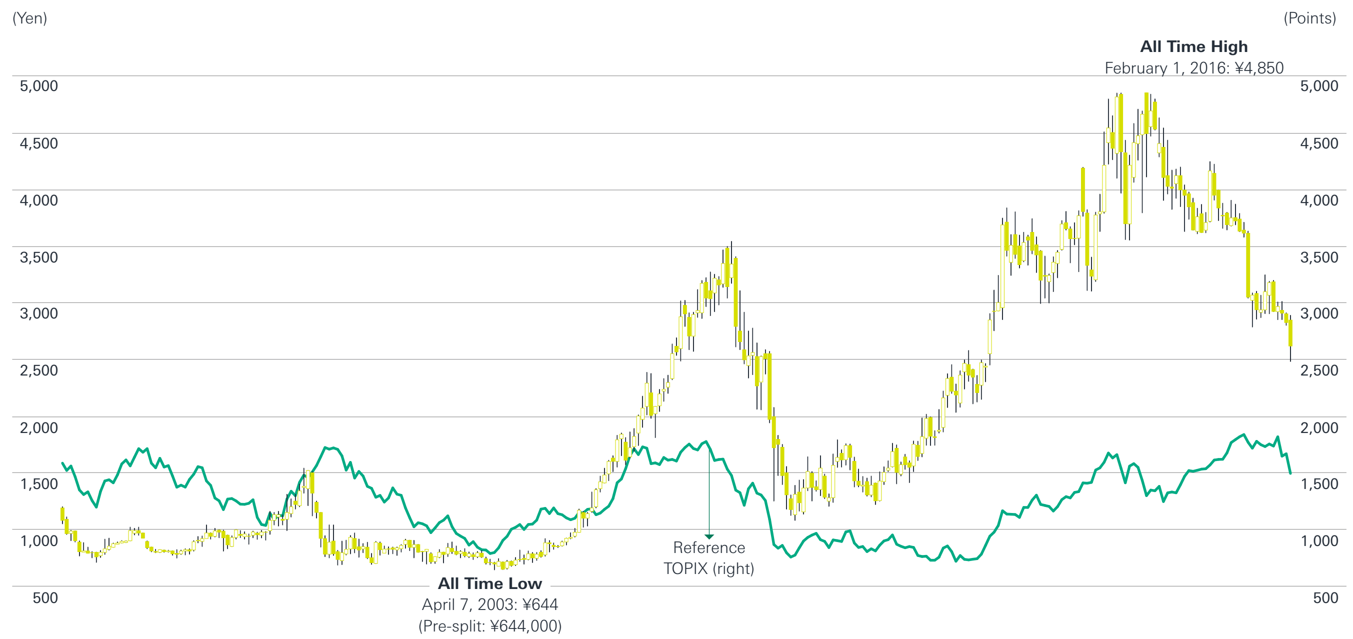
Government Offerings of JT Shares

1st Offering		
Method	Offering by Bids	Offering by non-Bids
Offer price (Pricing date)	Bid price: From ¥1,362,000 to ¥2,110,000 Weighted average price: ¥1,438,000 (August 29, 1994)	¥1,438,000 (August 31, 1994)
Number of shares offered	229,920 shares	164,356 shares
Offer term	From August 15 to 18, 1994	From September 2 to 8, 1994

Note:
Listing date: October 27, 1994
Exchange: First Section of Tokyo Stock Exchange

2nd and 3rd, 4th Offering			
	2nd Offering	3rd Offering	4th Offering
Method	Offering by Book-Building formula	Offering by Book-Building formula	Offering by Book-Building formula
Offer price (Pricing date)	¥815,000 (June 17, 1996)	¥843,000 (June 7, 2004)	¥2,949 (March 11, 2013)
Number of shares offered	Japan: 237,390 shares, International: 35,000 shares (Total: 272,390 shares)	Japan: 198,334 shares, International: 91,000 shares (Total: 289,334 shares)	Japan: 145,625,500 shares, International: 107,636,300 shares (Total: 253,261,800 shares)
Offer term	From June 18 to 19, 1996	From June 8 to 10, 2004	From March 12 to 13, 2013

Stock Price Chart



Note: Due to a 5 for 1 stock split on April 1, 2006, and a 200 for 1 stock split on July 1, 2012, stock prices reflect post-split levels.

Corporate Data

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Date of Establishment
April 1, 1985

Paid-in Capital
¥100 billion

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