11-Year Summary of Selected Financial Data

Shiseido Company, Limited and Subsidiaries
For the fiscal years ended March 31, 2008 to December 31, 2017

											Millions of yen (Except per share data)	Thousands of U.S. dollars (Except per share data)
	2008/3	2009/3	2010/3	2011/3	2012/3	2013/3	2014/3	2015/3	2015/12	2016/12	**2017/12**	**2017/12**
Operating Results:												
Net sales	723,484	690,256	644,201	670,701	682,385	677,727	762,047	777,687	763,058	850,306	**1,005,062**	**8,890,420**
Cost of sales	186,466	171,752	160,166	168,692	162,989	166,783	189,559	196,433	196,009	207,553	**231,327**	**2,046,236**
Selling, general and administrative expenses	473,553	468,589	433,684	457,550	480,260	484,898	522,843	553,640	529,388	605,972	**693,298**	**6,132,666**
Operating income	63,465	49,914	50,350	44,458	39,135	26,045	49,644	27,613	37,660	36,780	**80,437**	**711,517**
EBITDA	94,960	75,077	75,699	65,576	76,974	61,463	91,285	90,703	80,635	90,078	**154,741**	**1,368,783**
Net income (loss) attributable to owners of parent	35,459	19,373	33,671	12,790	14,515	(14,685)	26,149	33,668	23,210	32,101	**22,749**	**201,229**
Financial Position (At period-end):												
Total assets	675,864	606,568	775,445	739,120	720,707	715,593	801,346	823,636	808,547	934,590	**949,425**	**8,398,275**
Short-term liabilities	38,653	27,601	112,693	16,361	9,734	39,394	64,054	75,615	18,996	19,403	**12,203**	**107,943**
Long-term debt	24,566	34,451	101,753	181,155	175,418	145,274	91,864	31,281	67,617	156,428	**128,411**	**1,135,877**
Interest-bearing debt	63,219	62,053	214,446	197,517	185,153	184,669	155,918	106,897	86,613	120,580	**81,463**	**720,592**
Equity	382,469	337,224	348,323	307,269	290,494	287,069	338,561	386,860	391,664	392,963	**423,447**	**3,745,661**
Cash Flows:												
Cash flows from operating activities	75,307	42,767	69,431	67,586	52,599	42,040	84,320	32,134	60,529	59,129	**95,392**	**843,803**
Cash flows from investing activities	(5,802)	(28,157)	(204,884)	(30,303)	(20,668)	(25,534)	(16,799)	11,538	(23,137)	(70,640)	**(1,061)**	**(9,385)**
Cash flows from financing activities	(95,882)	(32,283)	120,359	(39,571)	(35,482)	(24,745)	(47,462)	(58,419)	(30,151)	22,378	**(53,117)**	**(469,854)**
Cash and cash equivalents at end of year	120,393	91,857	77,157	88,592	82,974	80,253	110,163	100,807	104,926	113,122	**156,834**	**1,387,297**
Per Share Data (In yen and U.S. dollars):												
Net income (loss)	86.1	48.0	84.6	32.1	36.5	(36.9)	65.7	84.4	58.2	80.4	**56.9**	**0.50**
Net assets	946.2	839.9	875.7	772.1	729.9	721.2	849.4	970.0	981.4	984.1	**1,059.8**	**9.37**
Cash dividend	34.0	50.0	50.0	50.0	50.0	50.0	20.0	20.0	20.0	20.0	**27.5**	**0.24**
Weighted average number of shares outstanding during the period (thousands)	407,696	403,240	397,886	397,864	397,974	398,007	398,300	398,704	399,026	399,227	**399,466**	
Financial Ratios:												
Operating margin (%)	8.8	7.2	7.8	6.6	5.7	3.8	6.5	3.6	4.9	4.3	**8.0**	
Return on assets (%)	5.0	3.0	4.9	1.7	2.0	(2.0)	3.4	4.1	2.8	3.7	**2.4**	
Operating ROA (%)	9.4	8.2	7.5	6.1	5.6	3.8	6.8	3.6	4.8	4.4	**8.7**	
Return on equity (%)	9.2	5.4	9.8	3.9	4.9	(5.1)	8.4	9.4	6.0	8.2	**5.6**	
Equity ratio (%)	56.6	55.6	44.9	41.6	40.3	40.1	42.2	47.0	48.4	42.0	**44.6**	
Interest-bearing debt to EBITDA ratio (times)	0.7	0.8	2.8	3.0	2.4	3.0	1.7	1.2	1.1	1.3	**0.5**	
Debt-equity ratio (times)	0.17	0.18	0.62	0.64	0.64	0.64	0.46	0.28	0.22	0.31	**0.19**	
Interest-bearing debt ratio (%)	14.2	15.5	38.1	39.1	38.9	39.1	31.5	21.6	18.1	23.5	**16.1**	
Payout ratio (consolidated) (%)	39.5	104.1	59.1	155.5	137.1	—	30.5	23.7	34.4	24.9	**48.3**	
Number of employees at year-end	28,793	28,810	28,968	31,310	32,595	33,356	33,054	33,000	33,783	36,549	**37,438**	
Net sales per employee	25.1	24.0	22.2	21.4	20.9	20.3	23.1	23.6	22.6	23.2	**26.8**	**237**

Notes: 1. The fiscal year ended December 31, 2015 is the 9 months from April 1, 2015 to December 31, 2015 for Shiseido and its consolidated subsidiaries in Japan and the 12 months from January 1, 2015 to December 31, 2015 for all other subsidiaries. In this report, it is referred to as "the year ended December 2015" in the text and as "2015/12" in tables, charts, and graphs.
2. Amounts less than one million yen are omitted.
3. U.S. dollar amounts are converted from yen, for convenience only, at the rate of ¥113.05 = US$1 prevailing on December 31, 2017.
4. EBITDA (Earnings before interest, taxes, depreciation and amortization) = Net income (loss) before income taxes + Interest expense + Depreciation and amortization expense + Impairment loss on goodwill and other intangible assets
5. Short-term liabilities = Short-term debt + Current portion of long-term debt
6. Net income (loss) per share (primary) is based on the average number of shares outstanding during the fiscal year. Net assets per share is calculated using the number of shares outstanding as of the balance sheet date. Net income (loss) per share is calculated before dilution.
7. Operating ROA = (Operating income + Interest and dividend income) / Total assets (Yearly average)
8. Interest-bearing debt to EBITDA ratio = Interest-bearing debt / EBITDA
9. Debt-equity ratio = Interest-bearing debt / Equity* *Equity = Total net assets – Stock acquisition rights – Non-controlling interests in consolidated subsidiaries
10. Interest-bearing debt ratio = Interest-bearing debt / Invested capital* *Invested capital = Interest-bearing debt + Equity
11. The number of employees at year-end does not include temporary employees.
12. Shiseido Group subsidiaries in the Americas formerly recognized free samples and promotional items associated with marketing activities in stores as assets when acquired and expensed them after shipped to customers. However, effective from the fiscal year ended March 31, 2012 these subsidiaries began to expense these items when acquired in order to conform with the Group's accounting policies. As a result, the Shiseido Group retrospectively restated the consolidated financial statements for the fiscal year ended March 31, 2011, accordingly.
13. Effective from the fiscal year ended March 31, 2014, certain subsidiaries of the Shiseido Group's retrospectively adopted a new standard for Employee Benefits (IAS 19, amended June 16, 2011) and changed the method for recognizing changes in net defined benefit obligation. The Shiseido Group applied this change retrospectively and restated the consolidated financial statements for the fiscal year ended March 31, 2013, accordingly.
14. From the year ended December 2016, Shiseido has been recognizing long-term payables associated with *Dolce&Gabbana*. For the year ended December 2017, the interest-bearing debt ratio including these long-term payables was 24.9 percent, the debt-equity ratio was 0.33, and interest-bearing debt was ¥140,615 million.
15. In November 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2015-17, "Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes" ("ASU 2015-17"). The standard requires that deferred tax assets and liabilities be classified as non-current on the balance sheet rather than being separated into current and non-current. Effective from the first quarter of the current fiscal year, affiliates in the Americas have adopted ASU 2015-17 on a retrospective basis. Accordingly, the Company reclassified the current deferred taxes to non-current on the December 31, 2016 consolidated balance sheet. As a result, ¥11,845 million recorded as "Deferred tax assets" on the consolidated balance sheet for the previous fiscal year has been reclassified from the current to non-current and offset by ¥11,416 million in the non-current "Deferred tax liabilities."

Operating Results and Financial Condition

OPERATING RESULTS

For the fiscal year 2017, economic conditions in Japan continued to follow a course of moderate recovery such as positive turnaround in consumer spending reflecting the improvements in employment and income environment. Conditions in the domestic cosmetics market were also stable supported by the underlying recovery trend and the increased demand from the growing number of overseas visitors to Japan. In international cosmetics markets, overall growth in Europe was slow, as the growth conditions vary from country to country. The Americas experienced slow expansion, while China and other Asian markets continued to record steady growth.

In 2015, the Shiseido Group launched the VISION 2020 medium-to-long-term strategy, which is designed to ensure that the Group sustain growth for the next 100 years. We pursue "to be a global winner with our heritage", we are emphasizing a consumer-oriented focus in all of our activities and taking steps to enhance our brand value on a global basis. We positioned 2015 to 2017 as a three-year period for rebuilding our business foundation by increasing investment in marketing and innovation, and advancing structural reforms to support strong growth over the following three years, from 2018 to 2020.

During the fiscal year 2017, the Group increased investment in areas where the future sales growth is expected, such as the prestige category, digital communication, and e-commerce. We also expanded investment in marketing aimed at achieving higher growth for *Laura Mercier*, a prestige brand focusing on makeup we acquired in 2016, and *Dolce&Gabbana*, a brand that mainly offers fragrances, with which we concluded a licensing agreement in the same year. In addition, we approached Japan, China, and Travel Retail as a single market, and we worked to expand cross-border marketing across the entire Asia, with a principal focus on Chinese consumers. To improve profitability, we rigorously managed profits by business and brand, and we reduced products with low contributions to sales and income. Furthermore, we took steps to restructure our global business and brand portfolios, such as the sale of Zotos International, Inc. (hereinafter, "Zotos"), a North American subsidiary.

As a result of these initiatives, consolidated net sales for the fiscal year 2017 increased by 16.0 percent year on year in a local currency basis. Key factors supporting this increase included global growth in the prestige category, where we continue to expand strategic investment, and additional sales from new brands introduced by the Group since the previous fiscal year. Translated into yen, consolidated net sales rose 18.2 percent year on year to ¥1,005,062 million ($8,890,420 thousand), due to the positive effect of yen depreciation.

Operating income increased 118.7 percent year on year to ¥80,437 million ($711,517 thousand),which gain was principally due to an increase in marginal income accompanying the growth in sales, improved efficiency in marketing investment, and the effects of cost structure reforms.

A gain on the sale of Zotos shares and related assets was recorded as other income. Other expenses included expenses from the voluntary product recall-related expenses and an impairment loss on intangible and other assets related to Bare Escentuals, Inc. (hereinafter, "Bare Escentuals") in the Americas. As a result, net income attributable to owners of parent declined 29.1 percent year on year to ¥22,749 million ($201,229 thousand).

After we acquired Bare Escentuals in 2010, we implemented a range of initiatives, such as expanding consumer contact points and enhancing product development. Nonetheless, we were not able to achieve the planned level of growth for the brand. The fiscal year 2017 was the final year of the first phase of VISION 2020, in which we focused on rebuilding our business foundation. Guided by our management policy of "facing reality," we are committed to rapidly addressing issues without delay. Accordingly, we closely examined the future potential of our businesses and brands. The Board of Directors carefully considered the details of marketing and structural reforms, as well as the level of profits that would be achievable with the implementation of those reforms. As a result, in the process of evaluating intangible assets, we made the decision to recognize an impairment loss on Bare Escentuals.

For the fiscal year 2017, the consolidated operating margin was 8.0 percent, and consolidated return on equity (ROE) was 5.6 percent. The major foreign currency exchange rates applied to income and expense accounting line items in the Company's financial statements for the fiscal year 2017 are JPY112.2/USD, JPY126.7/EUR, and JPY16.6/CNY.

REVIEW BY REPORTABLE SEGMENT

Net Sales by Reportable Segment

Segments[1]

(Billions of yen)	2015/12 (Adjusted)	2016/12
Japan Business	396.0	407.6
China Business	125.7	120.5
Asia Pacific Business	52.7	49.6
Americas Business	167.5	162.6
EMEA Business	104.2	85.2
Travel Retail Business	17.2	24.8

Net Sales by Reportable Segment

Segments[2]

(Billions of yen)	2016/12	**2017/12**
Japan Business	381.2	**431.0**
China Business	118.1	**144.3**
Asia Pacific Business	45.6	**54.2**
Americas Business	127.5	**140.4**
EMEA Business	94.1	**128.4**
Travel Retail Business	24.8	**44.5**
Professional Business	44.9	**48.0**
Other[3]	14.0	**14.3**

Income by Reportable Segment

Segments[1]

(Billions of yen)	2015/12 (Adjusted)	2016/12
Japan Business	55.0	57.4
China Business	(0.5)	4.2
Asia Pacific Business	0.4	1.1
Americas Business	(5.6)	(11.8)
EMEA Business	4.6	(7.2)
Travel Retail Business	2.4	5.5

Income by Reportable Segment

Segments[2]

(Billions of yen)	2016/12	**2017/12**
Japan Business	56.4	**83.2**
China Business	3.6	**11.3**
Asia Pacific Business	1.1	**5.7**
Americas Business	(12.8)	**(10.3)**
EMEA Business	(6.7)	**(3.2)**
Travel Retail Business	5.4	**12.4**
Professional Business	1.1	**3.0**
Other[3]	(11.9)	**(12.9)**

Operating Margin by Reportable Segment[4]

Segments[1]

(%)	2015/12 (Adjusted)	2016/12
Japan Business	12.6	12.6
China Business	(0.4)	3.5
Asia Pacific Business	0.8	2.2
Americas Business	(3.1)	(6.8)
EMEA Business	4.2	(8.1)
Travel Retail Business	14.0	22.1

Operating Margin by Reportable Segment[4]

Segments[2]

(%)	2016/12	**2017/12**
Japan Business	14.1	**18.0**
China Business	3.1	**7.8**
Asia Pacific Business	2.3	**10.3**
Americas Business	(9.4)	**(6.5)**
EMEA Business	(6.8)	**(2.3)**
Travel Retail Business	21.6	**27.6**
Professional Business	2.4	**6.1**
Other[3]	(20.5)	**(13.9)**

Notes:
1. Change in Business Segment Classification
Effective from the fiscal year 2016, the Company has revised its reportable segment classification method in line with the Group's internal financial management structure. As a result, reportable segment classifications have been changed from the "Japan Business" and "Global Business" segments to the "Japan Business," "China Business," "Asia Pacific Business," "Americas Business," "EMEA Business" and "Travel Retail Business" segments.
Segment information for 2015/12 (Adjusted) (the corresponding period of the previous fiscal year) has been restated in line with changes in the method of classifying reportable segments.
2. Change in Business Segment Classification
Effective from the fiscal year 2017, the Company has revised its reportable segment classification method in line with the Group's internal financial management structure. As a result, reportable segment classifications have been changed to the "Japan Business," "China Business," "Asia Pacific Business," "Americas Business," "EMEA Business," "Travel Retail Business" and "Professional Business" segments.
Segment information for the corresponding period of the previous fiscal year has been restated in line with changes in the method of classifying reportable segments.
3. "Other" includes head office administration departments, manufacturing operations as well as the activities of the Frontier Science business (production and sale of cosmetic raw materials, medical-use drugs, medical cosmetics, precision and analytical equipment), the Restaurant business, etc.
4. "Operating margin by reportable segment" is calculated against sales for the segment, including intersegment sales.

Japan Business

In the fiscal year 2017, the Japan Business expanded at a rate substantially higher than market growth. We have increased marketing investment for brands in the mid- to high-price range, and these brands continued to perform well. Sales to domestic customers expanded, and we steadily captured demand from overseas visitors to Japan. To achieve sustainable growth, we are focusing on three skin-related segments in which we have strengths—Skincare, Base makeup, and Sun care. This focus led to significant growth in market share in each of these segments. In the personal care category, which has presented certain challenges, we worked to streamline our focused brands and categories and strengthen points of contact with customers. As a result, we achieved a recovery in sales and significant improvement in profitability.

We also launched the Shiseido Facial Expression Project in April 2017. This initiative leverages our innovative wrinkle improvement technology, which utilizes pure retinol as the active ingredient, to help women show their intrinsic rich facial expressions. The project's first product was *ELIXIR SUPERIEUR Enriched Wrinkle Cream S*, a wrinkle-reducing product that was launched in June. The second product, *SHISEIDO VITAL-PERFECTION Wrinklelift Deep Retinowhite 4*, which offers the benefits of both wrinkle reduction and skin brightening, was introduced in November. Combined sales of these two products, including China, the rest of Asia, and Travel Retail, exceeded 1.7 million units.

Consequently, the segment's sales increased 13.1 percent year on year, to ¥431,026 million ($3,812,702 thousand). Operating income rose 47.6 percent, to ¥83,154 million ($735,550 thousand), which was primarily attributable to higher marginal income accompanying the growth in sales, the effects of cost structure reforms, and improvement in the efficiency of marketing investment.

China Business

In the China Business, prestige brands such as *SHISEIDO, Clé de Peau Beauté* and *IPSA* continued to record strong growth by leveraging their appeal as products "Made in Japan." In addition, e-commerce sales drove strong sales growth in the personal care category. In the past, personal care products have contributed the majority of sales in the e-commerce segment. However, in line with changes in consumer purchasing behavior, we actively launched products in the prestige and cosmetics categories, and rolled out digital marketing activities and stepped up marketing collaboration with a major e-commerce retailer. As a result of these types of initiatives, the China Business recorded substantial growth in e-commerce sales. An increasing number of customers in China have high regard for the value of products that are "Made in Japan." In consideration of this trend, we positioned the *ELIXIR* brand, which originated in Japan, as a strategic brand, and we stepped up initiatives aligned with the lifestyles and preferences of local customers. We also took steps to improve profitability in the cosmetics category. These initiatives included renewing the *AUPRES* brand, which recorded year-on-year growth in sales, and reinforcing self-service sales of *Za* and *PURE&MILD*.

As a result, the segment's sales were up 20.1 percent year on year on a local currency basis. Translated into yen, sales rose 22.2 percent, to ¥144,266 million ($1,276,125 thousand). Operating income increased 212.2 percent year on year, to ¥11,329 million ($100,212 thousand), which was due not only to higher marginal income accompanying the increase in sales but also to such factors as improved efficiency in marketing investment.

Asia Pacific Business

In the Asia Pacific Business, we recorded strong growth in sales of *Clé de Peau Beauté, NARS*, and other prestige brands, mainly in South Korea, Thailand, and Taiwan. Sales of *Clé de Peau Beauté* products were especially strong in the Company-owned retail store opened in Singapore. In the cosmetics and personal care categories, sales growth was driven by *SENKA*, which benefited from enhanced marketing tailored to the differing consumer preferences and lifestyles in each country, and by the sunscreen brand *ANESSA*, which we expanded the marketing channels.

Consequently, the segment's sales increased 11.2 percent year on year on a local currency basis. Translated into yen, sales were up 18.8 percent to ¥54,169 million ($479,159 thousand). Operating income rose 439.5 percent year on year, to ¥5,745 million ($50,818 thousand), largely due to improvement in the product mix and higher marginal income accompanying the growth in sales.

Americas Business

In the Americas Business, *NARS, SHISEIDO*, and other prestige brands continued to record growth in sales. We also increased marketing investment in the *Laura Mercier* brand, which we acquired in 2016. Sales of the *bareMinerals* brand, which we are working to restructure, decreased year on year due to the impact of department store closures and intensified competition in specialty stores. The Group is implementing a strategy of selection and concentration to further strengthen its business and brand portfolios. As part of this strategy, we acquired MATCHCo., whose latest technology can determine a customer's unique skin tone through a mobile app and use the data to blend a perfectly matching personalized foundation for each consumer. We also acquired Giaran, Inc., which possesses AI-based personalization technology.

As a result, the segment's sales were up 6.6 percent year on year on a local currency basis. Translated into yen, sales rose 10.1 percent ¥140,413 million ($1,242,043 thousand). In addition to the decline in *bareMinerals* sales, we also recorded increased costs associated with the Center of Excellence and implemented advance investment in *Laura Mercier* and in digital marketing. Nonetheless, due principally to the higher sales of *NARS* and *SHISEIDO* products and to the efficient utilization of expenditures, the operating loss in the Americas Business segment was reduced by ¥2,501 million ($22,122 thousand) from the previous fiscal year, to ¥10,288 million ($91,003 thousand).

EMEA Business

In the EMEA Business, we increased marketing investment in *Dolce&Gabbana*, for which we concluded a licensing agreement in 2016, in order to further enhance brand value. We also took steps to establish a more profitable business foundation by combining the cosmetics and fragrance businesses which previously operated separately into a single organization and implementing other structural reforms such as integrating back office and logistics systems.

The segment's sales increased 30.0 percent year on year on a local currency basis. Translated into yen, sales rose 36.4 percent to ¥128,418 million ($1,135,939 thousand), which increase resulted primarily from steady growth in existing brands led by *NARS* and the *narciso rodriguez* fragrance brand, and the additional contribution from sales of *Dolce&Gabbana* products. Although we increased marketing investment, we recorded higher marginal income accompanying the increase in sales, and the segment's operating loss was reduced by ¥3,531 million ($31,233 thousand) from the previous fiscal year, to ¥3,181 million ($28,137 thousand).

Travel Retail Business

The Travel Retail Business involves the sale of cosmetics through channels such as airport duty-free stores. The travel retail market is expanding due to an increase in travelers, especially in Asia. We believe that the Shiseido Group has potential for further growth in the travel retail business, which we have positioned as one of our most important businesses. Accordingly, we are working actively to further strengthen our position in the global prestige market segment. During the fiscal year 2017, we actively engaged in promotions and advertising in airports around the world, introduced products exclusively available through travel retail channels, and took steps to strengthen our relationships with major retailers.

These initiatives resulted in higher sales per airport duty-free store as well as substantial sales growth in South Korea, China, Thailand, and other countries in Asia. As a result, the segment's sales grew 73.8 percent year on year on a local currency basis. Translated into yen, sales increased 79.3 percent to ¥44,495 million ($393,586 thousand). Operating income increased 130.3 percent year on year to ¥12,361 million ($109,340 thousand), due to higher marginal income accompanying the growth in sales as well as the improvement in productivity per store and other factors.

Professional Business

In the Professional Business, we provide professional products to hair salons, including hair care, hair styling products, hair color, and hair perming products. It also has directly operated beauty salons in Japan and Thailand. During the fiscal year 2017, we worked to strengthen products and marketing in order to accelerate growth in China and the rest of Asia.

As a result, the segment's sales grew 4.3 percent year on year on a local currency basis. Translated into yen, sales rose 6.7 percent to ¥47,959 million ($424,228 thousand). Operating income increased 168.1 percent year on year, to ¥2,958 million ($26,165 thousand), principally due to higher marginal income accompanying the growth in sales.

In December 2017, we transferred the shares and assets associated with the business of our subsidiary Zotos to Henkel AG & Co. KGaA of Germany. The transfer of Zotos, which operates a hair care business centered in the Americas, was part of the global restructuring of our business and brand portfolios.

[Reference]
Period-on-Period Growth in Sales (Local Currency Basis)

(%)	2014/3	2015/3	2015/12 (Adjusted)	2016/12	**2017/12**
Net Sales	1.3	(2.0)	7.8	5.2	**16.0**

Note: The above period-on-period growth in sales on a local currency basis is a period-on-period comparison before translation into yen. Exchange rates for each fiscal period are presented below.

(Yen)	2014/3	2015/3	2015/12	2016/12	**2017/12**
USD	97.7	105.9	121.2	108.9	**112.2**
EUR	129.7	140.4	134.3	120.4	**126.7**
CNY	15.9	17.2	19.2	16.4	**16.6**

Sales by Region

(Billions of yen)	2014/3	2015/3	2015/12	2016/12	**2017/12**
Japan	377.3	365.6	296.9	407.7	**456.9**
China	111.5	114.8	132.4	129.8	**161.0**
Asia (excl. China)	52.5	55.3	66.6	69.1	**94.9**
Americas	118.7	133.1	155.3	148.4	**163.9**
Europe	102.1	108.9	111.8	95.3	**128.3**
Total	762.0	777.7	763.1	850.3	**1,005.1**

Note: Sales are categorized by country or region based on customer location.

CASH FLOWS

Cash and cash equivalents (net cash) as of December 31, 2017, totaled ¥156,834 million ($1,387,297 thousand), an increase of ¥43,711 million ($386,651 thousand) compared with previous year.

Cash Flows Summary

(Billions of yen)	2015/12	2016/12	**2017/12**
Cash Flows from Operating Activities	60.5	59.1	**95.4**
Cash Flows from Investing Activities	(23.1)	(70.6)	**(1.1)**
Cash Flows from Financing Activities	(30.2)	22.4	**(53.1)**
Cash and Cash Equivalents at End of Year	104.9	113.1	**156.8**

Cash Flows from Operating Activities

Net cash provided by operating activities was ¥95,392 million ($843,803 thousand). Income before income taxes was ¥38,555 million ($341,043 thousand), depreciation was ¥39,614 million ($350,411 thousand), amortization of goodwill was ¥4,235 million ($37,461 thousand), impairment loss was ¥70,922 million ($627,350 thousand), and increase in notes and accounts payable was ¥22,082 million ($195,329 thousand). On the other hand, increase in notes and accounts receivable was ¥25,447 million ($225,095 thousand), increase in inventories was ¥13,287 million ($117,532 thousand), and gain on transfer of business was ¥36,787 million ($325,404 thousand).

Cash Flows from Investing Activities

Net cash used in investing activities was ¥1,061 million ($9,385 thousand). Proceeds from transfer of business provided ¥53,549 million ($473,675 thousand). On the other hand, acquisition of property, plant and equipment used ¥36,015 million ($318,575 thousand), acquisition of intangible assets used ¥8,618 million ($76,231 thousand), payments of long-term prepaid expenses used ¥6,581 million ($58,213 thousand), and acquisition of shares in subsidiaries resulting in change in scope of consolidation used ¥5,226 million ($46,227 thousand).

Cash Flows from Financing Activities

Net cash used in financing activities was ¥53,117 million ($469,854 thousand). Proceeds from long-term debt provided ¥10,000 million ($88,456 thousand). On the other hand, repayment of long-term debt used ¥45,762 million ($404,794 thousand) and cash dividend paid used ¥8,977 million ($79,407 thousand).

BUSINESS AND OTHER RISKS

The various risks that could potentially affect the business performance and financial position of the Shiseido Group are summarized below. We feel that these risks could have a major impact on investors' decisions. Items that deal with future events are based on our judgment as of March 27, 2018. Please note that the potential risks are not limited to those listed below.

1. Consumer Services

The Shiseido Group places high priority on its relationships with consumers. The Group corporate philosophy Our Mission, Values and Way and the Shiseido Group Standards of Business Conduct and Ethics clearly state that we shall act in a manner that earns the satisfaction and trust of consumers, and we will continue working to ensure that all employees are aware of these standards. However, an unforeseen event could cause loss of such satisfaction and trust, leading to a decline in the value of the Group's brands. The Group's business performance and financial position could be negatively affected as a result.

2. Quality Control

The Shiseido Group acts in accordance with its belief that achieving customer satisfaction through the provision of high-quality, safe products is top priority. In addition to strict compliance with laws and regulations, the Group has formulated Quality Management Basic Guidelines and Global Quality Policy Guidance, which are applied throughout the Group. On this basis, the Group is working to maintain and control quality. At the development stage of new products, the Group has established in-house, rigorous safety assurance standards, with reference to domestic and overseas safety assurance guidelines. At the manufacturing stage, the Group observes ISO22716 cosmetics good manufacturing practices (GMP) and manufactures cosmetics products in accordance with rigorous quality control. However, in the event of an unexpected incident regarding quality, such as a major problem with quality below the expectation, concerns about safety based on newly obtained scientific knowledge or other factors, and social trust in the Shiseido Group could decline and the Group's financial position and business performance could be negatively affected.

3. Strategic Investment Activities
When making decisions about investments in strategic markets, mergers and acquisitions, and expansion in new businesses and new markets, the Shiseido Group endeavors to collect sufficient information and undertake due diligence prior to making rational judgments. Due to various unforeseeable factors that may cause the operating environment to deteriorate, however, we may not achieve the results originally anticipated. This could negatively affect the Group's business performance and financial position.

4. Information Security Risks
The Shiseido Group takes various measures aimed at protecting its information assets, which include consumers' personal information and confidential information. Specifically, in Japan we have formulated and rigorously comply with our Personal Information Protection Rules for the handling of individual number and specific personal information, Confidential Information Controlling Regulations and Information System Controlling Regulations to carefully handle personal consumer information and protect all information assets. Overseas, we have also established rules based on the laws of the countries in which we operate. However, unforeseeable events, such as leakage of information due to unauthorized access, could negatively affect the Group's business performance and financial position.

5. Competitive Environment of the Cosmetics Industry
The Shiseido Group operates in the cosmetics industry, in which competition is intensifying on a global scale. Competition in the mature domestic market is intensifying because of factors including the increased level of competition with companies in the same industry and the entry of new competitors from other industries. In addition, in overseas markets such as China and other Asian countries, which the Group has positioned as central to its growth strategy, the competitive environment is becoming increasingly challenging as global competitors are aggressively conducting mergers and acquisitions and expanding market share by executing marketing activities to raise consumer awareness of their brands. Consequently, the inability to respond to this competitive environment effectively could negatively affect the Group's business performance and financial position.

6. Responding Appropriately to Market Needs
The Shiseido Group's ability to develop and cultivate products and brands and to conduct marketing activities that respond appropriately to market needs exerts a significant impact on its sales and earnings. To respond to market needs, we continuously develop appealing new products and brands; reinforce and cultivate new and existing products and brands through marketing activities; and withdraw existing products and brands that no longer meet market needs. However, by nature these activities entail uncertainties that may prevent the Group from achieving its intended results, which could negatively affect the Group's business performance and financial position.

7. Specific Business Partners
Failure to respond effectively to changes in retail and whole sale distribution channels could negatively affect the Shiseido Group's business performance and financial position.

8. Operational Risks
In the event of an incident of fraud or other wrongdoing by someone associated with the business operations of the Shiseido Group, such as an employee or business partner, or by a third party, society's evaluation of the Group could decline, directly or indirectly, and the Group's business performance and financial position could be negatively affected.

9. Hiring and Developing Talented Human Resources
The Shiseido Group is working to strengthen the employment of diverse human resources; develop training programs that draw out the capabilities of employees; and hire and develop talented human resources. In addition, the Group is working to maintain workplace environments that enable employees to work in a comfortable manner. However, in the event that the hiring and development of necessary employees does not proceed according to plan, or that there is an outflow of human resources that substantially exceeds expectations, competitiveness could decline and business expansion could be hindered. The Group's business performance and financial position could be negatively affected as a result.

10. Consideration for the Environment and Human Rights
The Shiseido Group conducts business activities with consideration for the environment and strictly observes various related environmental laws and regulations. In addition, stakeholders are increasingly concerned with possible violations of the human rights of workers in the raw material procurement process. In response, the Group is working to identify any potential issues related to consideration for the environment, human rights, working environments, and health and safety in the procurement process, and to resolve issues through cooperation with suppliers. These efforts extend over the entire value chain, reaching back to the location that produces the raw materials. However, in the event of an inability to respond appropriately to these issues at worksites or in the supply chain, social trust in the Group could decline and its business performance and financial position could be negatively affected.

11. Material Litigation
In the fiscal year 2017, the Shiseido Group was not involved in any material litigation. In the future, unfavorable judgments resulting from material litigation could negatively affect the Group's business performance and financial position.

12. Regulatory Risks
The Shiseido Group is subject to a range of domestic and overseas legal and regulatory provisions in the course of conducting business. These include Japanese laws pertaining to ensuring the quality, efficacy, and safety of pharmaceutical products and medical devices, as well as quality-related standards, environmental standards, accounting standards, and tax regulations. The Group aspires to be completely ethical based on legal compliance and corporate social responsibility. However, future regulatory changes or the establishment of unanticipated new regulations may limit the Group's activities, which could negatively affect the Group's business performance and financial position.

13. Raw Material Price Fluctuations
International market conditions affect the price of raw materials used in Shiseido Group products. Factors affecting market conditions include geopolitical risk, the impact on supply and demand from increasing demand in developing countries and speculative capital flows, weather abnormalities, and fluctuations in exchange rates. The Shiseido Group constantly works to limit the impact of rising raw material prices by reducing the cost of sales and other means. However, changes in market conditions and prices that exceed projections could negatively affect the Group's business performance and financial position.

14. Exchange Rate Fluctuations
Export, import, and other transactions denominated in foreign currencies expose the Shiseido Group to foreign exchange rate risk. Although the Group hedges foreign exchange rate risk through means such as limiting export and import transactions by establishing production bases to serve local markets, we are unable to completely eliminate risk. Moreover, the financial statements of overseas consolidated subsidiaries and equity affiliates are denominated in local currencies that are translated into yen upon inclusion in the consolidated financial statements. This has the potential to exert a negative impact on operating performance if the yen appreciates versus foreign currencies when revenues exceed expenses. Moreover, the Group's investments in overseas subsidiaries and equity affiliates are subject to foreign currency translation adjustments that reduce shareholders' equity if the yen appreciates. Foreign exchange fluctuations that exceed assumptions could negatively affect the Group's business performance and financial position.

15. Share Price Fluctuations
As of December 31, 2017, the Shiseido Group held investments in securities and is therefore exposed to the risk of changes in share price, which can increase or decrease unrealized gains or losses and expose the Group to the risk of loss on revaluation. In addition, a portion of the pension plan assets of the Group's retirement benefit plan is invested in listed shares. Lower share prices could therefore reduce pension plan assets and negatively affect operating performance by increasing retirement benefit expenses. Unforeseen situations could negatively affect the Group's business performance and financial position.

16. Geopolitical Risks
In the course of conducting business, the Shiseido Group's business performance and financial position could be negatively affected by various geopolitical factors. These include the occurrence of sudden and unpredictable economic, political, and social crises; terrorism, war, and civil war; economic and civil upheaval resulting from the spread of contagious diseases; natural disasters; and severe or abnormal weather.

17. Natural Disasters and Accidents
The Shiseido Group has developed a business continuity plan covering issues critical to the continued operation of production bases, distribution bases, information systems, and the head office to minimize loss due to interruption of production, distribution, or sales resulting from the occurrence of a natural disaster or accident, such as a major earthquake. However, a natural disaster or accident that exceeds the assumptions of this plan and disrupts production, distribution or sales could negatively affect the Group's business performance and financial position.

18. Decrease in Brand Value
The Shiseido Group will continue working to enhance the value of the brands it owns, but a decline in brand value due to the above circumstances or some other unforeseen event could negatively affect the Group's business performance and financial position.

SIGNIFICANT ACCOUNTING ESTIMATES

The Shiseido Group prepares its consolidated financial statements in accordance with accounting principles generally accepted in Japan. In preparing these financial statements, we select and apply accounting policies and necessarily make estimates that affect reported amounts for assets, liabilities, revenue, and expenses. We consider information including historical data in making rational estimates. However, due to the unpredictable nature of these estimates, actual results may vary. The Shiseido Group considers the following significant accounting estimates which exert a significant influence on the consolidated financial statements.

Property, Plant and Equipment
The Shiseido Group reviews property, plant and equipment, for impairment whenever circumstances indicate that their carrying value may not be recoverable. Business-use assets are pooled by business division to estimate future cash flow, and the net sales value of idle assets is estimated for each separate asset. Based on these estimates, assets are devalued from book value to recoverable value. We consider the estimates of future cash flow and recoverable value to be rational. However, unpredictable factors could cause changes in underlying assumptions and estimates. This could change our estimates, decrease future cash flow and recoverable value, and require us to recognize impairment losses.

Goodwill, Trademarks, and Other Intangible Assets
The Shiseido Group reviews goodwill, trademarks, and other intangible assets for impairment periodically. Shiseido employs the opinions of external experts in estimating fair value and examining impairment for goodwill, trademarks, and other intangible assets. The discounted cash flow method primarily used to estimate fair value relies extensively on estimates and assumptions regarding future cash flow and discount rate. These estimates and assumptions may significantly affect measurement and the amount of impairment recognized. We consider the estimates of fair value used for measuring impairment to be rational. However, unforeseen changes to underlying assumptions and estimates could reduce fair value and require us to recognize impairment losses.

Securities

The Shiseido Group recognizes loss on revaluation for securities reported as available-for-sale securities for which fair value or market price has fallen substantially below acquisition cost. Securities deemed recoverable are excluded. Securities with a fair value that is more than 50 percent below acquisition cost as of the balance sheet date are deemed unrecoverable. The recoverability of securities with a fair value from 30 to 50 percent below acquisition cost is evaluated according to the performance and financial condition of the issuing entity. Loss on revaluation is recognized for securities for which fair value is not available if actual value has fallen to more than 50 percent below the acquisition cost due to the financial condition of the issuing entity. Securities deemed recoverable are excluded. We consider the estimates of recoverability to be appropriate. However, in the future the market price of securities deemed recoverable may decrease and the performance and financial condition of the issuing entity may deteriorate, which could require us to recognize loss on revaluation.

Deferred Tax Assets

The Shiseido Group has established a valuation allowance for deferred tax assets deemed unrecoverable using appropriate deferred tax asset accounting. Historical data and future projections are used to evaluate the recoverability of deferred tax assets to sufficiently determine taxable status. We consider these to be appropriate. However, unpredictable factors could cause changes in underlying assumptions that could reduce or eliminate deferred tax assets. This could require us to provide additional allowances for deferred tax assets.

Retirement Benefits and Obligations

The Shiseido Group's domestic retirement benefit plans consist primarily of corporate pension plans and termination allowance plans. Employee benefits and obligations for defined benefits are calculated based on assumptions including discount rate, employee turnover rate, mortality rate, and projected rate of return on pension plan assets. These assumptions are revised annually. Discount rate and expected return on pension plan assets are critical assumptions in determining benefits and obligations. The discount rate is determined based on the market rate as of the balance sheet date for long-term fixed-rate bonds that carry little or no risk. Expected return on pension plan assets is determined based on an expected weighted-average return for the various types of assets held within the plan. We consider these assumptions to be appropriate. However, actual results may vary and changes in the underlying assumptions could occur, which could affect retirement benefits and obligations.

ANALYSIS OF OPERATING RESULTS

NET SALES

Consolidated net sales for the fiscal year 2017 increased 16.0 percent year on year on a local currency basis. This increase resulted from global growth in the prestige market segment, where the Group has increased strategic investment, and from the new brands added to the Group since last fiscal year. After conversion into yen, consolidated net sales were ¥1,005,062 million ($8,890,420 thousand), an increase of 18.2 percent year on year, due to the positive effect of yen depreciation.

Net Sales

(Billions of yen)	2014/3	2015/3	2015/3 (Adjusted)	2015/12	2015/12 (Adjusted)	2016/12	**2017/12**
Net Sales	762.0	777.7	677.5	763.1	863.3	850.3	**1,005.1**

COST OF SALES AND SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Cost of Sales

Cost of sales increased 11.5 percent year on year to ¥231,327 million ($2,046,236 thousand). The ratio for cost of sales to net sales improved 1.4 percentage points to 23.0 percent, which primarily attributable to improvements in the product mix through increased sales of prestige brands and to the effects of cost structure reforms.

Selling, General and Administrative Expenses

Selling, general and administrative (SG&A) expenses increased 14.4 percent to ¥693,298 million ($6,132,666 thousand) compare with last year. Details of SG&A expenses are as follows:

Marketing Costs

The ratio of marketing costs to net sales decreased 0.6 percentage point to 35.7 percent. This was a result of improvement in marketing investment efficiency, which offset investment in growth to rebuild the business foundation and increased investment in new brands.

Personnel Expenses

The ratio of personnel expenses to net sales decreased 0.7 percentage point to 12.5 percent.

Other Expenses

The ratio of other expenses to net sales decreased 1.1 percentage points to 20.7 percent.

R&D expenses, which are included in SG&A expenses, were ¥24,230 million ($214,329 thousand) and represented 2.4 percent of net sales.

Cost of Sales Ratio / SG&A Expenses Ratio / SG&A Expenses

	2014/3	2015/3	2015/3 (Adjusted)	2015/12	2015/12 (Adjusted)	2016/12	**2017/12**
Cost of Sales Ratio (%)	24.9	25.2	26.0	25.7	25.1	24.4	**23.0**
SG&A Expenses Ratio (%)	68.6	71.2	70.9	69.4	69.8	71.3	**69.0**
Marketing Costs	22.2	23.4	24.7	25.2	36.2	36.3	**35.7**
Personnel Expenses	23.9	24.5	27.3	25.7	13.1	13.2	**12.5**
Other Expenses	22.5	23.3	18.9	18.5	20.5	21.8	**20.7**
SG&A Expenses (Billions of yen)	522.8	553.6	480.1	529.4	602.7	606.0	**693.3**
Marketing Costs	169.3	182.2	167.0	192.1	312.1	308.8	**359.2**
Personnel Expenses	181.8	190.6	185.2	196.0	113.5	112.0	**125.8**
Other Expenses	171.7	180.8	127.9	141.3	177.1	185.2	**208.3**

Note: From the fiscal period ended December 31, 2015, counter depreciation expenses and costs of BCs previously included in other expenses and personnel expenses have been reclassified as marketing costs.

OPERATING INCOME

Operating income increased 118.7 percent year on year to ¥80,437 million ($711,517 thousand), which was principally due to an increase in marginal income accompanying the growth in sales, improved efficiency in marketing investment, and the effects of cost structure reforms.

Operating Income / Operating Margin

(Billions of yen)	2014/3	2015/3	2015/3 (Adjusted)	2015/12	2015/12 (Adjusted)	2016/12	**2017/12**
Operating Income	49.6	27.6	21.2	37.7	44.3	36.8	**80.4**
Operating Margin (%)	6.5	3.6	3.1	4.9	5.1	4.3	**8.0**

OTHER INCOME (EXPENSES)

Net other expenses were ¥41,881 million ($370,464 thousand), which was due to impairment loss associated with Bare Escentuals, Inc., in Americas.

INCOME BEFORE INCOME TAXES

Income before income taxes decreased 22.7 percent year on year to ¥38,555 million ($341,043 thousand).

INCOME TAXES, INCLUDING DEFERRED TAXES

Income taxes including deferred taxes decreased 17.2 percent year on year to ¥13,200 million ($116,762 thousand).

NET INCOME ATTRIBUTABLE TO NON-CONTROLLING INTERESTS

Net income attributable to non-controlling interests increased 42.9 percent year on year to ¥2,606 million ($23,051 thousand).

NET INCOME ATTRIBUTABLE TO OWNERS OF PARENT

Net income attributable to owners of parent decreased 29.1 percent year on year to ¥22,749 million ($201,229 thousand).

Net Income Attributable to Owners of Parent / Return on Equity

(Billions of yen)	2014/3	2015/3	2015/3 (Adjusted)	2015/12	2015/12 (Adjusted)	2016/12	**2017/12**
Net Income Attributable to Owners of Parent	26.1	33.7	27.5	23.2	29.5	32.1	**22.7**
ROE (%)	8.4	9.4	—	6.0	—	8.2	**5.6**

Note: Consolidated ROE for the fiscal period ended December 31, 2015 is calculated using consolidated net income attributable to owners of parent for the year as the numerator and the average of equity at March 31, 2015 and December 31, 2015 as the denominator.

LIQUIDITY AND CAPITAL RESOURCES

FINANCING AND LIQUIDITY MANAGEMENT

The Shiseido Group seeks to generate stable operating cash flow and ensure a wide range of funding methods with the aims of securing sufficient capital for operating activities and maintaining sufficient liquidity and a sound financial position. We fund working capital, capital expenditures, and investments and loans needed for sustainable growth primarily with cash on hand and operating cash flow supplemented by bank borrowings and bond issues. Shiseido has set a benchmark of 25 percent for the interest-bearing debt ratio to maintain finances at a level that enables access to capital on favorable terms. Shiseido meets its funding requirements for large-scale investments using optimum, timely methods given factors including operating status, financial position, and market environment.

One of our targets for short-term liquidity is to maintain cash on hand at a level of approximately 1.5 months of consolidated net sales. As of December 31, 2017, cash, time deposits, and short-term investments in securities totaled ¥174,479 million ($1,543,379 thousand) and represented 2.1 months of consolidated net sales for the fiscal year 2017.

Interest-bearing debt as of December 31, 2017 totaled ¥140,615 million ($1,243,830 thousand) (including interest-bearing debt associated with *Dolce&Gabbana*). Shiseido uses diversified funding methods, which include authorized but unissued straight bonds for ¥140,000 million ($1,238,390 thousand). In addition, Shiseido Co., Ltd. and two subsidiaries in EMEA and the Americas have established a syndicated loan program with authorized but unused commitments totaling $300,000 thousand. A subsidiary in the Americas also holds unused commercial paper totaling $100,000 thousand. As of December 31, 2017, the Shiseido Group maintained a sufficient level of liquidity and a high level of financial flexibility through its diversified funding methods.

Total Assets / Operating ROA

(Billions of yen)	2014/3	2015/3	2015/12	2016/12	**2017/12**
Total Assets	801.3	823.6	808.5	934.6	**949.4**
Operating ROA (%)	6.8	3.6	4.8	4.4	**8.7**

Equity / Interest-Bearing Debt

(Billions of yen)	2014/3	2015/3	2015/12	2016/12	**2017/12**
Equity	338.6	386.9	391.7	393.0	**423.4**
Interest-Bearing Debt	155.9	106.9	86.6	120.6	**81.5***

Equity Ratio / Interest-Bearing Debt Ratio

(%)	2014/3	2015/3	2015/12	2016/12	**2017/12**
Equity Ratio	42.2	47.0	48.4	42.0	**44.6**
Interest-Bearing Debt Ratio	31.5	21.6	18.1	23.5	**16.1**

* Since the fiscal year 2016, Shiseido has been recognizing long-term payables associated with *Dolce&Gabbana*.
For the fiscal year 2017, the interest-bearing debt ratio including these long-term payables was 24.9 percent, and interest-bearing debt was ¥140,615 million ($1,243,830 thousand).

CREDIT RATINGS

The Shiseido Group recognizes the need to maintain a certain level of credit rating to secure financial flexibility that is consistent with its capital/liquidity policies and to secure access to sufficient capital resources through capital markets. The Shiseido Group has acquired ratings from Moody's Japan K.K. (Moody's) and Standard and Poor's Global Ratings Japan (S&P) to facilitate fund procurement in global capital markets.

	Moody's	S&P
Long-term	A2 (Outlook: Stable)	A– (Outlook: Stable)
Short-term	P–1	A–2

(As of February 28, 2018)

ASSETS, LIABILITIES, AND NET ASSETS

Assets

As of December 31, 2017, total assets increased 1.6 percent compared with December 31, 2016, to ¥949,425 million ($8,398,275 thousand). Current assets were up 21.8 percent compared with the previous fiscal year to ¥526,245 million ($4,654,975 thousand), due to such factors as increases in cash and time deposits and in notes and accounts receivable. Non-current assets were down 15.8 percent compared with December 31, 2016, to ¥423,179 million ($3,743,290 thousand), largely due to a decrease in intangible assets resulting from declines in goodwill and trademarks associated with the impairment loss on Bare Escentuals.

Liabilities

Total liabilities as of December 31, 2017, were down 3.3 percent from a year earlier, to ¥503,552 million ($4,454,241 thousand), largely due to declines in long-term debt and in liability for retirement benefits.

Net Assets

Total net assets as of December 31, 2017, increased 7.7 percent compared with December 31, 2016, to ¥445,872 million ($3,944,024 thousand), mainly due to an increase in retained earnings.

As of December 31, 2017, net assets per share were up ¥75.71 from a year earlier, to ¥1,059.84 ($9.37). The equity ratio increased 2.6 percentage points, to 44.6 percent.

FORECAST FOR THE FISCAL YEAR 2018

We are forecasting consolidated net sales of ¥1,033,000 million, an increase of 2.8 percent year on year, or 8 percent on a like-for-like basis, excluding the influence of extraordinary factors such as the sale of Zotos International, Inc., in the fiscal year 2017. Due to such factors as higher marginal income accompanying the increase in net sales, operating income is forecasted to reach ¥90,000 million and net income attributable to owners of parent is forecasted to reach ¥54,000 million.

Consolidated Financial Results Forecast for the Fiscal Year 2018

	Net Sales	Operating Income	Net Income Attributable to Owners of Parent	Net Income per Share
Forecast (A)	Billions of yen 1,033.0	Billions of yen 90.0	Billions of yen 54.0	Yen 135.2
(Reference) Results for fiscal year 2017 (B)	1,005.1	80.4	22.7	56.9
Amount of increase or decrease (A–B)	27.9	9.6	31.3	—
Rate of increase or decrease (%)	2.8	11.9	137.4	—

Consolidated Financial Statements
Consolidated Balance Sheets

Shiseido Company, Limited and Subsidiaries
December 31, 2016 and 2017

	Note	Millions of yen 2016/12	Millions of yen 2017/12	Thousands of U.S. dollars (Note 1) 2017/12
ASSETS				
Current Assets:				
Cash and time deposits	27	120,126	**166,698**	**1,474,551**
Short-term investments in securities		7,905	**7,781**	**68,827**
Notes and accounts receivable:				
Trade		136,768	**162,058**	**1,433,507**
Unconsolidated subsidiaries and affiliates		0	**0**	**0**
		136,768	**162,058**	**1,433,507**
Less: allowance for doubtful accounts		(1,933)	**(1,727)**	**(15,276)**
		134,835	**160,331**	**1,418,230**
Inventories	3	115,672	**129,954**	**1,149,526**
Deferred tax assets		21,773	**25,467**	**225,272**
Other current assets		31,589	**36,012**	**318,549**
Total current assets		431,903	**526,245**	**4,654,975**
Property, Plant and Equipment, at Cost:				
Buildings and structures	27	164,817	**162,538**	**1,437,753**
Machinery and equipment	27	167,218	**162,959**	**1,441,477**
Leased assets		7,414	**7,244**	**64,077**
		339,450	**332,742**	**2,943,317**
Less: accumulated depreciation		(238,271)	**(228,228)**	**(2,018,823)**
		101,178	**104,514**	**924,493**
Land		36,604	**36,971**	**327,032**
Construction in progress		18,411	**17,196**	**152,109**
Total property, plant and equipment		156,194	**158,681**	**1,403,635**
Intangible Assets:				
Goodwill		59,795	**12,166**	**107,616**
Leased assets		401	**247**	**2,184**
Trademarks		146,209	**121,347**	**1,073,392**
Other intangible assets		39,927	**34,825**	**308,049**
Total intangible assets		246,333	**168,586**	**1,491,251**
Investments and Other Assets:				
Investments in securities	27	22,532	**23,970**	**212,030**
Investments in unconsolidated subsidiaries and affiliates		2,367	**2,310**	**20,433**
Long-term prepaid expenses		13,377	**13,991**	**123,759**
Deferred tax assets		37,800	**30,658**	**271,189**
Other investments	27	24,081	**24,979**	**220,955**
Total investments and other assets		100,158	**95,910**	**848,385**
Total Assets		934,590	**949,425**	**8,398,275**

The accompanying notes are an integral part of the consolidated financial statements.

	Note	Millions of yen 2016/12	Millions of yen 2017/12	Thousands of U.S. dollars (Note 1) 2017/12
LIABILITIES AND NET ASSETS				
Current Liabilities:				
Short-term debt		11,583	**8,540**	**75,541**
Current portion of long-term debt	27	4,974	**2,122**	**18,770**
Notes and accounts payable:				
Trade		50,149	**47,676**	**421,724**
Unconsolidated subsidiaries and affiliates		930	**1,463**	**12,941**
		51,080	**49,140**	**434,674**
Electronically recorded obligations–operating		32,312	**37,892**	**335,179**
Other payables		43,453	**59,903**	**529,880**
Accrued income taxes		5,561	**25,032**	**221,424**
Reserve for sales returns		12,948	**14,012**	**123,945**
Accrued bonuses for employees		22,110	**25,019**	**221,309**
Accrued bonuses for directors		99	**119**	**1,052**
Provision for liabilities and charges		2,024	**2,005**	**17,735**
Deferred tax liabilities		0	**2**	**17**
Other current liabilities		60,538	**67,587**	**597,850**
Total current liabilities		246,687	**291,379**	**2,577,434**
Long-Term Liabilities:				
Long-term debt	27	104,022	**70,801**	**626,280**
Long-term payables		53,135	**59,255**	**524,148**
Liability for retirement benefits		94,489	**73,745**	**652,321**
Allowance for losses on guarantees		350	**350**	**3,095**
Allowance for environmental measures		376	**260**	**2,299**
Deferred tax liabilities		18,402	**3,762**	**33,277**
Other long-term liabilities		3,257	**3,998**	**35,364**
Total long-term liabilities		274,033	**212,173**	**1,876,806**
Total Liabilities		520,720	**503,552**	**4,454,241**
CONTINGENT LIABILITIES				
NET ASSETS				
Shareholders' Equity:				
Common stock		64,506	**64,506**	**570,597**
Authorized: 1,200,000,000 shares as of December 31, 2016 and 2017				
Issued: 400,000,000 shares as of December 31, 2016 and 2017				
Capital surplus		70,846	**70,808**	**626,342**
Retained earnings		258,005	**271,681**	**2,403,193**
Less: treasury stock, at cost		(1,325)	**(874)**	**(7,731)**
Treasury stock: 700,745 shares as of December 31, 2016 and 460,033 shares as of December 31, 2017				
Total shareholders' equity		392,033	**406,121**	**3,592,401**
Accumulated Other Comprehensive Income:				
Unrealized gains (losses) on available-for-sale securities		7,389	**8,664**	**76,638**
Foreign currency translation adjustments		26,516	**28,726**	**254,099**
Accumulated adjustments for retirement benefits		(32,975)	**(20,064)**	**(177,478)**
Total accumulated other comprehensive income		930	**17,326**	**153,259**
Stock Acquisition Rights		818	**874**	**7,731**
Non-Controlling Interests in Consolidated Subsidiaries		20,087	**21,550**	**190,623**
Total Net Assets		413,870	**445,872**	**3,944,024**
Total Liabilities and Net Assets		934,590	**949,425**	**8,398,275**

Consolidated Statements of Income / Consolidated Statements of Comprehensive Income

Shiseido Company, Limited and Subsidiaries
For the fiscal years 2016 and 2017

CONSOLIDATED STATEMENTS OF INCOME

	Note	2016/12 Millions of yen	2017/12 Millions of yen	2017/12 Thousands of U.S. dollars (Note 1)
Net Sales		850,306	**1,005,062**	**8,890,420**
Cost of Sales		207,553	**231,327**	**2,046,236**
Gross profit		642,753	**773,735**	**6,844,183**
Selling, General and Administrative Expenses	4	605,972	**693,298**	**6,132,666**
Operating income		36,780	**80,437**	**711,517**
Other Income (Expenses):				
Interest and dividend income		1,293	**1,439**	**12,728**
Interest expense		(814)	**(991)**	**(8,766)**
Other interest on debt		(336)	**(1,382)**	**(12,224)**
Foreign exchange gain (loss)		(1,270)	**(216)**	**(1,910)**
Equity in earnings of affiliates		260	**284**	**2,512**
Gain (loss) on sales of investments in securities		402	**1,146**	**10,137**
Loss on revaluation of investments in securities		(21)	**—**	**—**
Gain (loss) on sales and disposal of property, plant and equipment	5	8,122	**(1,013)**	**(8,960)**
Gain on transfer of business	6	8,952	**36,787**	**325,404**
Gain on sales of shares of subsidiaries and affiliates	7	—	**211**	**1,866**
Impairment loss	8	(153)	**(70,922)**	**(627,350)**
Structural reform expenses	9	(4,037)	**(4,479)**	**(39,619)**
Voluntary product recall-related expenses	10	—	**(3,233)**	**(28,597)**
Loss on liquidation of subsidiaries and affiliates	11	—	**(136)**	**(1,203)**
Temporary expenses associated with reforms to human resource systems	12	—	**(130)**	**(1,149)**
Information security expenses	13	(574)	**—**	**—**
Other, net		1,262	**755**	**6,678**
Subtotal		13,086	**(41,881)**	**(370,464)**
Income before income taxes		49,866	**38,555**	**341,043**
Income Taxes				
Current		17,507	**29,416**	**260,203**
Deferred		(1,565)	**(16,215)**	**(143,432)**
Subtotal		15,941	**13,200**	**116,762**
Net income		33,925	**25,355**	**224,281**
Net Income Attributable to Non-Controlling Interests		(1,823)	**(2,606)**	**(23,051)**
Net Income Attributable to Owners of Parent		32,101	**22,749**	**201,229**

		2016/12 Yen	2017/12 Yen	2017/12 U.S. dollars (Note 1)
Per Share				
Net income attributable to owners of parent — basic		80.4	**56.9**	**0.50**
— diluted		80.3	**56.9**	**0.50**
Cash dividend		20.0	**27.5**	**0.24**
Weighted Average Number of Shares (thousands)		399,227	**399,466**	

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Shiseido Company, Limited and Subsidiaries
For the fiscal years ended December 31, 2016 and 2017

	Note	2016/12 Millions of yen	2017/12 Millions of yen	2017/12 Thousands of U.S. dollars (Note 1)
Net Income		33,925	**25,355**	**224,281**
Other Comprehensive Income				
Unrealized gains (losses) on available-for-sale securities		(813)	**1,166**	**10,314**
Foreign currency translation adjustments		(14,906)	**3,073**	**27,182**
Adjustments for retirement benefits		(9,136)	**12,890**	**114,020**
Share of other comprehensive income of associates accounted for under the equity method		(90)	**(30)**	**(265)**
Total other comprehensive income (loss)	14	(24,946)	**17,100**	**151,260**
Comprehensive Income		8,978	**42,456**	**375,550**
(Breakdown)				
Comprehensive income attributable to owners of parent		8,367	**39,145**	**346,262**
Comprehensive income attributable to non-controlling interests		611	**3,310**	**29,279**

The accompanying notes are an integral part of the consolidated financial statements.

Consolidated Statements of Changes in Net Assets

Shiseido Company, Limited and Subsidiaries
For the fiscal years 2016 and 2017

	Thousands	Millions of yen								
	Number of shares of common stock	Common stock	Capital surplus	Retained earnings	Treasury stock, at cost	Unrealized gains (losses) on available-for-sale securities	Foreign currency translation adjustments	Accumulated adjustments for retirement benefit	Stock acquisition rights	Non-controlling interests in consolidated subsidiaries
Balance as of January 1, 2016	400,000	64,506	70,258	233,933	(1,700)	8,144	40,374	(23,854)	863	20,806
Net income attributable to owners of parent	—	—	—	32,101	—	—	—	—	—	—
Cash dividend from retained earnings	—	—	—	(7,983)	—	—	—	—	—	—
Equity transactions with non-controlling interests and others	—	—	575	(46)	—	—	—	—	—	—
Acquisition of treasury stock	—	—	—	—	(6)	—	—	—	—	—
Disposal of treasury stock	—	—	11	—	380	—	—	—	—	—
Net changes of items other than shareholders' equity	—	—	—	—	—	(755)	(13,858)	(9,120)	(44)	(718)
Balance as of December 31, 2016	**400,000**	**64,506**	**70,846**	**258,005**	**(1,325)**	**7,389**	**26,516**	**(32,975)**	**818**	**20,087**
Net income attributable to owners of parent	**—**	**—**	**—**	**22,749**	**—**	**—**	**—**	**—**	**—**	**—**
Cash dividend from retained earnings	**—**	**—**	**—**	**(8,986)**	**—**	**—**	**—**	**—**	**—**	**—**
Equity transactions with non-controlling interests and others	**—**	**—**	**(81)**	**(87)**	**—**	**—**	**—**	**—**	**—**	**—**
Acquisition of treasury stock	**—**	**—**	**—**	**—**	**(17)**	**—**	**—**	**—**	**—**	**—**
Disposal of treasury stock	**—**	**—**	**43**	**—**	**468**	**—**	**—**	**—**	**—**	**—**
Net changes of items other than shareholders' equity	**—**	**—**	**—**	**—**	**—**	**1,275**	**2,210**	**12,910**	**55**	**1,462**
Balance as of December 31, 2017	**400,000**	**64,506**	**70,808**	**271,681**	**(874)**	**8,664**	**28,726**	**(20,064)**	**874**	**21,550**

	Thousands	Thousands of U.S. dollars (Note 1)								
	Number of shares of common stock	Common stock	Capital surplus	Retained earnings	Treasury stock, at cost	Unrealized gains (losses) on available-for-sale securities	Foreign currency translation adjustments	Accumulated adjustments for retirement benefit	Stock acquisition rights	Non-controlling interests in consolidated subsidiaries
Balance as of January 1, 2017	**400,000**	**570,597**	**626,678**	**2,282,220**	**(11,720)**	**65,360**	**234,551**	**(291,685)**	**7,235**	**177,682**
Net income attributable to owners of parent	**—**	**—**	**—**	**201,229**	**—**	**—**	**—**	**—**	**—**	**—**
Cash dividend from retained earnings	**—**	**—**	**—**	**(79,486)**	**—**	**—**	**—**	**—**	**—**	**—**
Equity transactions with non-controlling interests and others	**—**	**—**	**(716)**	**(769)**	**—**	**—**	**—**	**—**	**—**	**—**
Acquisition of treasury stock	**—**	**—**	**—**	**—**	**(150)**	**—**	**—**	**—**	**—**	**—**
Disposal of treasury stock	**—**	**—**	**380**	**—**	**4,139**	**—**	**—**	**—**	**—**	**—**
Net changes of items other than shareholders' equity	**—**	**—**	**—**	**—**	**—**	**11,278**	**19,548**	**114,197**	**486**	**12,932**
Balance as of December 31, 2017	**400,000**	**570,597**	**626,342**	**2,403,193**	**(7,731)**	**76,638**	**254,099**	**(177,478)**	**7,731**	**190,623**

The accompanying notes are an integral part of the consolidated financial statements.

Consolidated Statements of Cash Flows

Shiseido Company, Limited and Subsidiaries
For the fiscal years 2016 and 2017

	Note	Millions of yen 2016/12	Millions of yen 2017/12	Thousands of U.S. dollars (Note 1) 2017/12
Cash Flows from Operating Activities:				
Income before income taxes		49,866	**38,555**	**341,043**
Depreciation		34,480	**39,614**	**350,411**
Amortization of goodwill		4,916	**4,235**	**37,461**
Impairment loss		153	**70,922**	**627,350**
(Gain) loss on sales and disposal of property, plant and equipment		(7,132)	**1,013**	**8,960**
(Gain) loss on sales of investments in securities		(402)	**(1,146)**	**(10,137)**
(Gain) loss on revaluation of investments in securities		21	**—**	**—**
Gain on transfer of business		(8,952)	**(36,787)**	**(325,404)**
(Gain) loss on liquidation of subsidiaries and affiliates		—	**(211)**	**(1,866)**
Increase (decrease) in allowance for doubtful accounts		233	**17**	**150**
Increase (decrease) in reserve for sales returns		(1,526)	**934**	**8,261**
Increase (decrease) in accrued bonuses for employees		3,917	**3,207**	**28,367**
Increase (decrease) in accrued bonuses for directors		44	**19**	**168**
Increase (decrease) in provision for liabilities and charges		896	**(207)**	**(1,831)**
Increase (decrease) in provision for structural reforms		(990)	**—**	**—**
Increase (decrease) in liability for retirement benefits		(2,168)	**(2,472)**	**(21,866)**
Increase (decrease) in allowance for environmental measures		(1)	**(115)**	**(1,017)**
Interest and dividend income		(1,293)	**(1,439)**	**(12,728)**
Interest expense		814	**991**	**8,766**
Other interest on debt		336	**1,382**	**12,224**
Equity in earnings of affiliates		(260)	**(284)**	**(2,512)**
(Increase) decrease in notes and accounts receivable		(10,578)	**(25,447)**	**(225,095)**
(Increase) decrease in inventories		(9,500)	**(13,287)**	**(117,532)**
Increase (decrease) in notes and accounts payable		19,058	**22,082**	**195,329**
Other		2,898	**4,916**	**43,485**
Subtotal		74,831	**106,494**	**942,007**
Interest and dividends received		1,552	**1,516**	**13,409**
Interest paid		(838)	**(984)**	**(8,704)**
Interest paid on other debt		—	**(1,736)**	**(15,356)**
Income taxes paid		(16,415)	**(9,898)**	**(87,554)**
Net cash provided by operating activities		59,129	**95,392**	**843,803**
Cash Flows from Investing Activities:				
Transfers to time deposits		(14,207)	**(17,439)**	**(154,259)**
Proceeds from maturity of time deposits		17,641	**15,148**	**133,993**
Acquisition of short-term investments in securities		(4)	**(3)**	**(26)**
Acquisition of investments in securities		(430)	**(4)**	**(35)**
Proceeds from sales of investments in securities		650	**1,922**	**17,001**
Proceeds from transfer of business	16	10,938	**53,549**	**473,675**
Acquisition of property, plant and equipment		(31,366)	**(36,015)**	**(318,575)**
Proceeds from sales of property, plant and equipment		8,832	**1,703**	**15,064**
Acquisition of intangible assets		(32,340)	**(8,618)**	**(76,231)**
Payments of long-term prepaid expenses		(6,124)	**(6,581)**	**(58,213)**
Acquisition of shares in subsidiaries resulting in change in scope of consolidation	16	(24,426)	**(5,226)**	**(46,227)**
Sales of shares in subsidiaries resulting in change in scope of consolidation		—	**500**	**4,422**
Other		197	**4**	**35**
Net cash used in investing activities		(70,640)	**(1,061)**	**(9,385)**
Cash Flows from Financing Activities:				
Net increase (decrease) in short-term debt		529	**(3,170)**	**(28,040)**
Proceeds from long-term debt		40,000	**10,000**	**88,456**
Repayment of long-term debt		(5,738)	**(45,762)**	**(404,794)**
Repayment of lease obligations		(2,187)	**(2,125)**	**(18,796)**
Acquisition of treasury stock		(6)	**(17)**	**(150)**
Disposal of treasury stock		392	**511**	**4,520**
Cash dividend paid		(8,214)	**(8,977)**	**(79,407)**
Cash dividend paid to non-controlling interests		(3,359)	**(2,390)**	**(21,141)**
Repayment of long-term accounts payable		—	**(1,145)**	**(10,128)**
Sales of shares in subsidiaries not resulting in change in scope of consolidation		962	**—**	**—**
Other		0	**(39)**	**(344)**
Net cash provided by (used in) financing activities		22,378	**(53,117)**	**(469,854)**
Effect of Exchange Rate Changes on Cash and Cash Equivalents		(2,672)	**2,498**	**22,096**
Net Change in Cash and Cash Equivalents		8,196	**43,711**	**386,651**
Cash and Cash Equivalents at Beginning of Year		104,926	**113,122**	**1,000,636**
Cash and Cash Equivalents at End of Year	16	113,122	**156,834**	**1,387,297**

The accompanying notes are an integral part of the consolidated financial statements.

Notes to the Consolidated Financial Statements

Shiseido Company, Limited and Subsidiaries

1. BASIS OF PRESENTING CONSOLIDATED FINANCIAL STATEMENTS

(1) Accounting Principles and Presentation

The financial statements of Shiseido Company, Limited (the "Company") and its consolidated subsidiaries have been prepared in accordance with the provisions set forth in the Financial Instruments and Exchange Law and Companies Act and in conformity with accounting principles generally accepted in Japan. Therefore, application and disclosure requirements are different from International Financial Reporting Standards in certain respects.

Certain items presented in the consolidated financial statements filed with the Director of the Kanto Finance Bureau in Japan have been reclassified for the convenience of the reader.

Amounts in U.S. dollars are included solely for the convenience of the reader. The rate of ¥113.05 = US$1 prevailing on December 31, 2017 has been used in translating the consolidated financial statements expressed in Japanese yen into U.S. dollars. Such translations should not be construed as representations that the Japanese yen amounts could be readily converted, realized or settled in U.S. dollars at this rate.

(2) Scope of Consolidation

Number of consolidated subsidiaries: 79

Apart from the change described below, principal subsidiaries are listed in the Group's most recent Securities Report (submitted March 27, 2018). Since there are no other major changes, the list is omitted from this report. Please refer to the Shiseido Group's website for the list of principal subsidiaries.

[Additions: 4 companies]

MATCHCo. and JWALK, LLC have been included in the scope of consolidation following the new acquisition of shares. In addition, KODOMOLOGY Co., Ltd. and Shiseido Group Middle East LLC have been included in the scope of consolidation since they were established as subsidiaries. Furthermore, Giaran, Inc. has been merged with Shiseido Americas Corporation by way of absorption after the acquisition of new shares during the fiscal year 2017.

[Exclusions: 15 companies]

KINARI Inc., Shiseido Irica Technology Inc., Zotos International, Inc., Piidea Canada, Ltd., Joico Holdings B.V., Joico Laboratories Europe B.V., and Joico Belgium N.V. were excluded from the scope of consolidation following the transfer of shares held. The following companies were excluded from the scope of consolidation following absorption-type mergers into other companies: Shiseido Information Network Co., Ltd. into Shiseido Japan Co., Ltd., Shiseido Professional Korea into Shiseido Korea Co., Ltd., Shiseido España S.A. into Beauté Prestige International S.A.U., Shiseido Europe S.A.S. into Beauté Prestige International S.A., Beauté Prestige International S.p.A. (Italy) into Shiseido Group Italy S.p.A., and Beauté Prestige International GmbH (Germany) into Shiseido Group Germany GmbH.

InterAct Co., Ltd. was excluded from the scope of consolidation due to its liquidation.

Shiseido India Private Limited was excluded from the scope of consolidation because it is not materially significant.

Names, etc., of main subsidiaries excluded from consolidation

Main unconsolidated subsidiary: Beauté Prestige International Ltd. (UK)

(Reason for Exclusion from Consolidation)

Unconsolidated subsidiaries are excluded from the scope of consolidation because they are small in size or are not involved in the main business of the Company. They are materially insignificant in terms of total assets, net sales, net income (portion attributable to equity interest), and retained earnings (portion attributable to equity interest), etc., have a minimal impact on the consolidated financials, and are materially insignificant in general.

(3) Matters Concerning Application of the Equity Method

Number of affiliated companies accounted for by the equity method: 3

Major company name: Pierre Fabre Japon Co., Ltd.

Nonconsolidated subsidiaries that are not accounted for by the equity method

Nonconsolidated subsidiaries that are not accounted for by the equity method including Beauté Prestige International Ltd. (UK) are small in scale and do not engage in full-scale operations, and net income (the Company's interest share) and retained earnings (the Company's interest share) have a minimal effect on the Company's consolidated financial statements. Also, these subsidiaries are insignificant in general, thus these companies are excluded from the scope of equity method application.

Matters Concerning the Business Terms and Other Items of Consolidated Subsidiaries

The account settlement dates of consolidated subsidiaries match the consolidated account settlement date.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(1) Inventories

Inventories are generally valued at cost, determined by the periodic average method. The carrying amount in the balance sheet is calculated with consideration of write-downs due to decreased profitability.

(2) Property, Plant and Equipment (Excluding Leased Assets)

Tangible fixed assets are, in principle, depreciated using the straight-line method. The main estimated useful lives are as follows:

Buildings and structures:	2-50 years
Machinery, equipment and vehicles:	2-12 years
Tools, furniture and fixtures:	2-15 years

(3) Intangible Assets (Excluding Leased Assets)

Intangible assets are, in principle, amortized using the straight-line method. The main estimated useful lives are as follows:

Software:	5 years
Customer relationships:	10 years
Trademarks:	10-15 years (except for those with indefinite useful lives)

(4) Leased Assets

Finance leased assets that are not deemed to transfer ownership of the leased property to the lessee are depreciated using the straight-line method over the period of the lease, with zero residual value.

(5) Long-Term Prepaid Expenses

Long-term prepaid expenses are primarily amortized using the straight-line method.

(6) Goodwill

Amortization of goodwill is determined on a case by case basis and is generally amortized using the straight-line method over a period not exceeding 20 years.

(7) Securities

The Company and its consolidated subsidiaries categorize their existing securities as available-for-sale securities. Those securities with market prices are carried at fair value prevailing at the fiscal year end, with net unrealized gains and losses, net of taxes, reported separately in net assets. The cost of securities sold is mainly calculated using the moving-average method.

If fair value is not available, securities are carried at cost, which is determined mainly by the moving-average method. Investments in limited partnerships are recorded as investments in securities at the amount of interest in such partnerships calculated based on ownership percentage. Investment gain or loss is included in net income or loss in proportion to the ownership interests in the net asset value of the partnership.

Securities with remaining maturities of one year or less and securities that are recognized as cash equivalents are classified as short-term investments in securities. Those with maturities extending beyond one year are included in investments in securities as non-current assets.

(8) Net Income and Cash Dividend per Share

Net income per share of common stock is based on the weighted average number of shares of common stock outstanding during each year. The computation of diluted net income per share of common stock reflects the maximum possible dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock.

Cash dividend per share shown for each year in the consolidated statements of income represents the dividend declared as applicable to the respective year, rather than that paid in each year.

(9) Accounting for Consumption Tax

In Japan, consumption tax is imposed at a flat rate on all domestic consumption of goods, assets and services (with certain exemptions). The consumption tax withheld upon sales is recorded as a liability. Consumption tax, which is paid by the Company and its domestic consolidated subsidiaries on purchases of goods, assets and services, is offset against the balance withheld, and the net amount is subsequently paid to the national government.

Transactions subject to consumption taxes are recorded at amounts exclusive of consumption taxes.

(10) Allowance for Doubtful Accounts

The Company and its domestic consolidated subsidiaries provide an allowance for doubtful accounts based on the historic percentage of actual bad debt losses against the balance of total receivables and the amount of uncollectible receivables estimated on an individual basis. Overseas consolidated subsidiaries record the allowance based primarily on the amount of uncollectible receivables estimated on an individual basis.

(11) Reserve for Sales Returns

The Companies provide a reserve for sales returns for future losses considering the past return ratios and distributors' stock.

(12) Accrued Bonuses for Employees

The Companies provide accrued bonuses for employees based on the estimated amounts to be paid in respect of the fiscal year. This reserve includes bonuses for corporate officers who are non-Board members, for whom the calculations are the same as those described in Accrued Bonuses for Directors.

(13) Accrued Bonuses for Directors

The Companies provide accrued bonuses for members of the Board of Directors who concurrently serve as corporate executive officers based on the estimated amounts to be paid in respect of the fiscal year.

(14) Provision for Liabilities and Charges

To provide for losses due to legal risks, product guarantee risks, tax risks, and other factors, certain overseas consolidated subsidiaries record provisions, the amount of which is based on estimated losses to be incurred considering the likelihood of such losses in the future.

(15) Allowance for Losses on Guarantees

The Company provides an allowance for estimated probable losses on guarantees based on the financial status of the parties for which guarantees have been provided.

(16) Allowance for Environmental Measures

The Company and its domestic consolidated subsidiaries provide a reserve for the estimated cost to treat polychlorinated biphenyl (PCB) waste as required by the "Act on Special Measures Concerning Promotion of Proper Treatment of PCB Wastes" (Act No. 65 of 2001).

(17) Provision for Structural Reforms

The Company provides a reserve for the estimated amount of expenses and the losses to be incurred in association with structural reforms.

(18) Liability for Retirement Benefits

① Periodic allocation method for the estimated retirement benefits
The retirement benefit obligation is calculated by allocating the estimated retirement benefits until the end of the current fiscal year on a benefit formula basis.

② Amortization of past service cost and actuarial gains/losses
Past service cost is primarily amortized on a straight-line basis over a 10-year period, which is shorter than the average remaining years of service of the eligible employees.

Net actuarial gain or loss is primarily amortized from the following year on a straight-line basis over a 10-year period, which is shorter than the average remaining years of service of the eligible employees.

(19) Foreign Currency Translation

Receivables and payables denominated in foreign currencies are translated into Japanese yen at the exchange rate prevailing on the respective balance sheet dates, and resulting exchange gains or losses are included in net income or loss for the fiscal year.

(20) Derivatives and Hedging Activities

The Companies use derivatives such as foreign exchange forward contracts, foreign currency options, interest rate swap contracts, and interest rate and currency swap contracts to reduce market risks and maintain stable profits. The Companies limit their use of derivative transactions to the amounts of foreign currency denominated receivables and payables and actual requirements, and do not use derivatives for speculative trading.

The Companies execute and manage derivatives within the limits of established internal rules and regulations, and reduce credit risk by limiting counterparties to highly creditworthy financial institutions.

Derivatives are carried at fair value with gains or losses recognized in the consolidated statements of income. For derivatives used for hedging purposes, if derivatives meet the requirements for hedge accounting, gains or losses on derivatives are deferred until recognition of the hedged transactions.

If interest rate swap contracts are used as a hedge and meet certain hedging criteria, the interest rate swaps are not stated at fair value, and instead the amount to be received under the interest rate swap contract is added to or deducted from the interest on the liabilities for which the swap contract was executed (special accounting).

If interest rate and currency swap contracts are used as a hedge and meet certain hedging criteria, the interest rate and currency swap contracts are not stated at fair value, and instead the amount to be received under the interest rate and currency swap contracts is added to or deducted from the interest on the liabilities for which the swap contracts were executed, and the liabilities denominated in foreign currencies, for which the interest rate and currency swap contracts were executed, are translated at the contracted rate (integral accounting).

Measurement of hedge effectiveness is not considered necessary for interest rate swap contracts that meet the requirements for special accounting and interest rate and currency swap contracts that meet the requirements for integral accounting.

(21) Foreign Currency Denominated Financial Statements

Financial statements of overseas consolidated subsidiaries and affiliates that are denominated in foreign currencies are translated into Japanese yen at the exchange rates prevailing at the respective balance sheet dates of those subsidiaries for assets and liabilities, and at the historical exchange rates for shareholders' equity. All income and expense amounts are translated at the average rates of exchange during the fiscal year of those subsidiaries and affiliates.

The resulting translation adjustments are included in net assets as foreign currency translation adjustments and non-controlling interests.

(22) Definition of "Cash and Cash Equivalents" in Consolidated Statements of Cash Flows

Cash and cash equivalents as shown in the consolidated statements of cash flows are composed of cash in hand, readily available time deposits, and short-term investments with maturities of 3 months or less at the time of purchase that are exposed to insignificant risk of change in value.

(23) Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries for Consolidated Financial Statements

The Company has applied "Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries for Consolidated Financial Statements" (ASBJ Practical Issues Task Force No. 18, March 26, 2015 amendment), and necessary modifications have been made for consolidation.

(24) Application of Consolidated Taxation System

The Company and certain domestic consolidated subsidiaries applied a consolidated taxation system.

(25) Additional Information

Effective from the first quarter of the current fiscal year, the Company and domestic affiliates have been adopting "Implementation Guidance on Recoverability of Deferred Tax Assets Accounting Standards Boards of Japan" (ASBJ Guidance No. 26, March 28, 2016).

(26) Changes in Presentation

① In November 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2015-17, "Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes" ("ASU 2015-17"). The standard requires that deferred tax assets and liabilities be classified as non-current on the balance sheet rather than being separated into current and non-current. Effective from the first quarter of the current fiscal year, affiliates in Americas have been adopting ASU 2015-17 on a retrospective basis. Accordingly, the Company reclassified the current deferred taxes to non-current on the December 31, 2016 Consolidated Balance Sheet. As a result, ¥11,845 million recorded as "Deferred tax assets" on the consolidated balance sheets for the previous fiscal year has been reclassified from current to non-current and offset for ¥11,416 million by the non-current "Deferred tax liabilities."

② Due to the increase in quantitative significance of "Other interest on debt " which was included in "Other, net" in "Other Income

(Expenses)" in the previous fiscal year, the Company has changed to record it separately for this fiscal year.

In order to reflect this alteration, the consolidated financial statements for the fiscal year ended December 31, 2016 have been rearranged. As a result, ¥926 million recorded as "Other, net" on the consolidated statements of income for the previous fiscal year has been reclassified into ¥336 million of "Other interest on debt" and ¥1,262 million of "Other, net" respectively.

On the other hand, ¥3,235 million recorded as "Other" in cash flow from operating activities on the consolidated statements of cash flows for previous fiscal year has been reclassified into ¥336 million of "Other interest on debt" and ¥2,898 million of "Other," respectively.

(27) Accounting Standard Issued but Not Yet Adopted

Foreign Affiliates

Standard / interpretation		Outline of the new / revised standards	To be adopted by the Group
IFRS 16	Lease	Revision to accounting treatment for lease	From the beginning of the year ending December 31, 2019
ASU 2016-12	Lease	Revision to accounting treatment for lease	From the beginning of the year ending December 31, 2019

The impact of the Company's consolidated financial statements from the adoption of standards lease is under evaluation at the time of the preparation of the consolidated financial statements.

3. INVENTORIES

Inventories held by the Companies as of December 31, 2016 and 2017 are as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	**2017/12**	**2017/12**
Merchandise and finished products	81,432	**88,620**	**783,900**
Work in process	5,657	**5,450**	**48,208**
Raw materials and supplies	28,583	**35,884**	**317,417**
	115,672	**129,954**	**1,149,526**

4. RESEARCH AND DEVELOPMENT EXPENSES

Research and development expenses are expensed as incurred.

Research and development expenses, which are included in selling, general and administrative expenses, totaled ¥18,264 million and ¥24,230 million ($214,329 thousand) for the fiscal years 2016 and 2017, respectively.

There are no research and development expenses included in total manufacturing expenses for the fiscal years 2016 and 2017.

5. GAIN (LOSS) ON SALES AND DISPOSAL OF PROPERTY, PLANT AND EQUIPMENT

For the fiscal year ended December 31, 2016

Mainly the gain on the sale of land at the closed Kamakura Factory.

6. GAIN ON TRANSFER OF BUSINESS

For the fiscal year ended December 31, 2016

It resulted from the transfer of Jean Paul GAULTIER fragrance intellectual property rights.

For the fiscal year ended December 31, 2017

This gain is attributed mainly to the transfer of the shares of Zotos International, Inc. and related business assets.

7. GAIN ON SALES OF SHARES OF SUBSIDIARIES AND AFFILIATES

For the fiscal year ended December 31, 2017

The gain is attributed to the transfer of KINARI Inc.

8. IMPAIRMENT LOSS

For the fiscal year 2016

The Company recognized impairment losses on the fixed assets of overseas subsidiaries.

Use	Type	Location
Unutilized assets, etc.	Other intangible assets, etc.	China, etc.

The Group groups its business-use assets according to the minimum independent cash-flow-generating units, based on business classifications. Unutilized assets are grouped by the individual property.

Regarding unutilized assets, the Group's assets that are no longer expected to be used in the future have been devalued to their recoverable amount, resulting in ¥153 million of other expenses. The recoverable amount was estimated based on the net sales value, which was assessed based on the expected selling price.

For the fiscal year 2017

The Company recognized impairment losses on the fixed assets of domestic and overseas subsidiaries.

Use	Type	Location
Assets for business use	**Goodwill, trademarks, other intangible assets, and buildings and structures, etc.**	**United States**
Unutilized assets, etc.	**Other intangible assets, etc.**	**China, etc.**

The Group groups its business-use assets according to the minimum independent cash-flow-generating units, based on business classifications. Unutilized assets are grouped by the individual property.

As a result, the goodwill, etc. recorded at the time Bare Escentuals, Inc. was acquired in the Americas business, which are considered among the assets for business use, was written down to fair value after an impairment test based on U.S. accounting standards was performed, after consideration of all facts, including the fact that sales were trending below the plan. The breakdown is shown below. Primarily, fair value was determined by the income approach, and a discount rate of 10% was used.

	Millions of yen	Thousands of U.S. dollars (Note 1)
Goodwill	43,195	382,087
Trademarks	23,711	209,739
Customer-related intangible assets	2,418	21,388
Buildings and structures, etc.	1,548	13,693
	70,874	626,926

Unutilized group assets that are no longer expected to be used in the future have been written down to their recoverable value, resulting in a ¥48 million ($424 thousand) other expenses. The recoverable amount is estimated based on the expected selling price after calculating net sale value.

9. STRUCTURAL REFORM EXPENSES

For the fiscal year ended December 31, 2016

Structural reform expenses refer to retirement premiums paid to early retirees and other expenses included in temporary expenses attributable to structural reforms in progress worldwide.

For the fiscal year ended December 31, 2017

Structural reform expenses mainly reflect early retiree retirement premiums and the closure of the Company's stores of Bare Escentuals Beauty, Inc. included in temporary expenses incurred as a result of ongoing structural reforms across all global regions.

10. VOLUNTARY PRODUCT RECALL-RELATED EXPENSES

For the fiscal year ended December 31, 2017

The expenses reflect voluntary recalls of products that do not meet the Company's quality standards.

11. LOSS ON LIQUIDATION OF SUBSIDIARIES AND AFFILIATES

For the fiscal year ended December 31, 2017

A loss on the ongoing liquidation of a subsidiary in India.

12. TEMPORARY EXPENSES ASSOCIATED WITH REFORMS TO HUMAN RESOURCE SYSTEMS

For the fiscal year ended December 31, 2017

Temporary expenses associated with the reorganization of the human resource systems of certain employees working at the Company's factories.

13. INFORMATION SECURITY EXPENSES

For the fiscal year ended December 31, 2016

Information security expenses refer to the costs incurred due to illegal access by a third party to the official online shopping website of a consolidated subsidiary. Expenses comprise the costs required to properly identify the causes, apologize to consumers and put in place countermeasures.

14. OTHER COMPREHENSIVE INCOME

The components of other comprehensive income including reclassification adjustments and tax (expense) or benefit for the fiscal years 2016 and 2017 are as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	**2017/12**	**2017/12**
Unrealized gains (losses) on available-for-sale securities, net of taxes:			
Increase (decrease) during the fiscal year	(1,661)	**3,003**	**26,563**
Reclassification adjustments	(402)	**(1,000)**	**(8,845)**
Amount before tax	(2,064)	**2,002**	**17,708**
Tax (expense) or benefit	1,250	**(835)**	**(7,386)**
Subtotal	(813)	**1,166**	**10,314**
Foreign currency translation adjustments:			
Increase (decrease) during the fiscal year	(14,897)	**3,037**	**26,864**
Reclassification adjustments	0	**97**	**858**
Amount before tax	(14,897)	**3,135**	**27,731**
Tax (expense) or benefit	(9)	**(62)**	**(548)**
Subtotal	(14,906)	**3,073**	**27,182**
Adjustments for retirement benefits:			
Increase (decrease) during the fiscal year	(20,739)	**10,097**	**89,314**
Reclassification adjustments	7,294	**8,956**	**79,221**
Amount before tax	(13,445)	**19,054**	**168,544**
Tax (expense) or benefit	4,309	**(6,164)**	**(54,524)**
Subtotal	(9,136)	**12,890**	**114,020**
Share of other comprehensive income of associates accounted for under the equity method:			
Increase (decrease) during the fiscal year	(51)	**(49)**	**(433)**
Reclassification adjustments	(38)	**19**	**168**
Subtotal	(90)	**(30)**	**(265)**
Total other comprehensive income (loss)	(24,946)	**17,100**	**151,260**

15. NET ASSETS

Under Japanese laws and regulations, the entire amount paid for new shares must be designated as common stock. However, a company may, by a resolution of the Board of Directors, designate an amount not exceeding one half of the price of the new shares as additional paid-in capital, which is included in capital surplus.

Under the Japanese Companies Act ("the Act"), in cases where dividend distribution of surplus is made, the lesser of an amount equal to 10% of the dividend or the excess, if any, of 25% of common stock over the total of additional paid-in capital and legal earnings reserve, must be set aside as additional paid-in capital or legal earnings reserve. Legal earnings reserve is included in retained earnings in the accompanying consolidated balance sheets. Under the Act, both legal earnings reserve and additional paid-in capital used to eliminate or reduce a deficit generally require a resolution of the shareholders' meeting.

Additional paid-in capital and legal earnings reserve may not be distributed as dividends. Under the Act, all additional paid-in capital and legal earnings reserve may be transferred to other capital surplus and retained earnings under certain conditions.

The maximum amount that the Company can distribute as dividends is calculated based on the non-consolidated financial statements of the Company in accordance with the Act. Under the Act, companies can pay a dividend at any time during the fiscal year in addition to the year-end dividend upon resolution at the shareholders' meeting. For companies that meet certain criteria such as: (1) having a Board of Directors, (2) having accounting auditors, (3) having a Board of Corporate Auditors, and (4) the term of service of the directors is prescribed as one year rather than two years as the normal term by its articles of incorporation, the Board of Directors may declare a dividend if the company has prescribed so in its articles of incorporation.

A semi-annual interim dividend may also be paid once a year upon resolution by the Board of Directors if the articles of incorporation of the company so stipulate. Cash dividends charged to retained earnings during the fiscal year were the year-end cash dividend for the preceding fiscal year and the interim cash dividend for the current fiscal year.

Appropriations are not accrued in the consolidated financial statements for the corresponding period, but are recorded in the subsequent accounting period after shareholders' meeting approval has been obtained.

Retained earnings at December 31, 2017 include amounts representing year-end cash dividend of ¥5,993 million ($53,011 thousand), ¥15.0 ($0.13) per share, which was approved at the shareholders' meeting held on March 27, 2018.

16. CASH FLOW INFORMATION

(1) The reconciliation of cash and time deposits shown in the consolidated balance sheets and cash and cash equivalents shown in the consolidated statements of cash flows as of December 31, 2016 and 2017 is as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	**2017/12**	**2017/12**
Cash and time deposits	120,126	**166,698**	**1,474,551**
Short-term investments in securities	7,905	**7,781**	**68,827**
Total	128,032	**174,479**	**1,543,379**
Time deposits with maturities exceeding 3 months	(13,004)	**(15,863)**	**(140,318)**
Debt securities with maturities exceeding 3 months	(1,905)	**(1,781)**	**(15,754)**
Cash and cash equivalents	113,122	**156,834**	**1,387,297**

(2) The main breakdown of assets and liabilities for a transfer or acquisition of business exchange for cash and cash equivalents

For the fiscal year 2017

The main breakdown of assets and liabilities transferred and the transfer price and cash in-flow from the sale of Zotos International Inc. is as follows:

	Millions of yen	Thousands of U.S. dollars (Note 1)
Current assets	**11,578**	**102,414**
Fixed assets	**11,647**	**103,025**
Current liabilities	**(3,752)**	**(33,188)**
Long-term liabilities	**(987)**	**(8,730)**
Gain on transfer of business	**35,999**	**318,434**
Transfer price of business	**54,485**	**481,954**
Other	**(595)**	**(5,263)**
Cash and cash equivalents	**(1,541)**	**(13,631)**
Proceeds from the transfer of business	**52,348**	**463,051**

(3) The main breakdown of assets and liabilities possessed by a company newly consolidated as a result of the acquisition of shares

For the fiscal year 2016

For the main breakdown of assets, liabilities and the acquisition cost of Gurwitch Products, LLC., which was newly consolidated as a result of the acquisition of shares is as follows:

	Millions of yen
Current assets	8,658
Non-current assets	19,024
Current liabilities	(1,965)
Acquisition cost of newly consolidated subsidiaries	25,717
Cash and cash equivalents of newly consolidated subsidiaries	(1,291)
Acquisition of shares in subsidiaries resulting in change in scope of consolidation	24,426

(4) Significant non-cash transactions are as follows:

Newly recorded assets and liabilities related to finance lease transactions are as follows:

For the fiscal year 2016	Millions of yen
Lease assets	1,700
Lease obligations	1,700

For the fiscal year 2017	Millions of yen	Thousands of U.S. dollars (Note 1)
Lease assets	1,917	16,957
Lease obligations	1,917	16,957

Newly recorded assets and liabilities related to licence agreement are as follows:

For the fiscal year 2016

	Millions of yen
Intangible assets	61,608
Long-term payables (including other payables)	61,608

17. ACCOUNTING FOR LEASES

The Companies have various lease agreements whereby the Companies act both as a lessee and a lessor.

(1) Finance leases

Non-ownership-transfer finance lease transactions

① As lessee:

Leased assets mainly consist of mold tools, fixtures, and software.

② As lessor:

None applicable

(2) Operating leases

Lease obligations under operating leases on December 31, 2016 and 2017 are as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	2017/12	2017/12
① As lessee:			
The scheduled maturities of future lease rental payments on such non-cancelable lease contracts are as follows:			
Due within 1 year	9,033	9,994	88,403
Due after 1 year	32,202	68,211	603,370
	41,235	78,205	691,773
② As lessor:			
The scheduled maturities of future lease rental payments on such non-cancelable lease contracts are as follows:			
Due within 1 year	172	172	1,521
Due after 1 year	3,753	3,580	31,667
	3,925	3,753	33,197

18. FINANCIAL INSTRUMENTS

(1) Financial Instruments

① Policy for financial instruments

The Companies limit fund management to short-term deposits, investments in securities and other methods.

As a matter of policy, the Companies procure funds using bank loans, commercial papers, bonds and other methods.

The Companies use derivatives to avoid the risk of foreign exchange rate fluctuations associated with receivables and payables denominated in foreign currencies and the risk of interest rate fluctuations associated with loans. The Companies limit the use of derivatives to the volume of receivables and payables and actual requirements, and do not engage in speculative transactions.

② Types of financial instruments, risks and risk management system

Notes and accounts receivable are exposed to customer credit risk. The Companies mitigate this risk by managing settlement date and amount due for each counterparty.

Investments in securities, primarily the equity securities of corporations with which the Companies do business, are exposed to the risk of fluctuations in market price. The Companies manage this risk by periodically examining market prices and the financial condition of the issuing entities.

Notes, electronically recorded obligations and accounts payable are due within one year.

Interest-bearing debt includes short-term borrowings and commercial papers, which the Companies use to procure funds for operating transactions, as well as long-term borrowings, bonds and lease obligations, which the Companies use to fund investments and loans, capital expenditures and operating transactions. Long-term payables, which are mostly liabilities incurred in connection with the execution of a license agreement, are not exposed to foreign exchange risk and interest rate risk. Floating-rate debt is exposed to the risk of interest rate fluctuations. The Companies hedge this risk for specific long-term borrowings by using derivatives (interest rate swap contracts and interest rate and currency swap contracts) to avoid the risk of interest rate fluctuations and fix interest payments.

The Companies use foreign exchange forward contracts and foreign currency options to hedge the risk of foreign exchange rate fluctuations associated with receivables and payables denominated in foreign currencies. In addition, we have entered interest rate swap contracts to hedge the risk of interest rate fluctuations associated with floating-rate debt. Also, we use interest rate and currency swap contracts to hedge the risk of foreign exchange fluctuations and fluctuations in interest rates associated with debt in foreign currencies.

(20) Derivatives and Hedging Activities in Note 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES explains hedge accounting, hedging instruments and methods, hedging policy, hedged items, and assessment of hedging effectiveness.

The Companies execute and manage derivatives within the limits of established internal rules and regulations, and reduce credit risk by limiting counterparties to highly creditworthy financial institutions.

Payables and interest-bearing debt are exposed to liquidity risk that the Companies manage in ways such as preparing monthly capital deployment reports.

③ Supplemental information on the fair value of financial instruments

The Companies calculate the fair value of financial instruments based on market prices, or by using reasonable estimates when market prices are not available. These estimates include variable factors, and are subject to fluctuation due to changes in the underlying assumptions. The contract amounts of the derivatives discussed in Note 20. DERIVATIVE FINANCIAL INSTRUMENTS are not an indicator of the market risk associated with derivative transactions.

(2) Fair Value of Financial Instruments

Fair value and variance with carrying value presented on the consolidated balance sheets are as follows. Fair values that are not readily determinable are not included in the following table (See *2 for additional information).

	Millions of yen		
	2016/12		
	Carrying value (*)	Fair value (*)	Variance
① Cash and time deposits	120,126	120,126	—
② Notes and accounts receivable (less allowance for doubtful accounts)	134,835	134,835	—
③ Short-term investments in securities and investments in securities Available-for-sale securities	28,961	28,961	—
④ Notes and accounts payable, electrically recorded obligations and other payables	(126,845)	(126,845)	—
⑤ Short-term borrowings from banks and other financial institutions	(6,339)	(6,339)	—
⑥ Commercial papers	(5,243)	(5,243)	—
⑦ Bonds	(40,000)	(40,165)	(165)
⑧ Long-term borrowings from banks and other financial institutions	(65,426)	(66,160)	(734)
⑨ Lease obligations	(3,570)	(3,605)	(35)
⑩ Derivative instruments			
i. Hedge accounting not applied	(601)	(601)	—
ii. Hedge accounting applied	—	(22)	(22)
⑪ Long-term payables	(53,135)	(53,135)	—

	Millions of yen		
	2017/12		
	Carrying value (*)	Fair value (*)	Variance
① Cash and time deposits	166,698	166,698	—
② Notes and accounts receivable (less allowance for doubtful accounts)	160,331	160,331	—
③ Short-term investments in securities and investments in securities Available-for-sale securities	30,325	30,325	—
④ Notes and accounts payable, electrically recorded obligations and other payables	(146,936)	(146,936)	—
⑤ Short-term borrowings from banks and other financial institutions	(8,540)	(8,540)	—
⑥ Commercial papers	—	—	—
⑦ Bonds	(40,000)	(40,128)	(128)
⑧ Long-term borrowings from banks and other financial institutions	(29,566)	(29,566)	(0)
⑨ Lease obligations	(3,357)	(3,380)	(23)
⑩ Derivative instruments			
i. Hedge accounting not applied	53	53	—
ii. Hedge accounting applied	—	(611)	(611)
⑪ Long-term payables	(59,255)	(59,255)	—

Thousands of U.S. dollars (Note 1)

	2017/12		
	Carrying value (*)	Fair value (*)	Variance
① Cash and time deposits	**1,474,551**	**1,474,551**	**—**
② Notes and accounts receivable (less allowance for doubtful accounts)	**1,418,230**	**1,418,230**	**—**
③ Short-term investments in securities and investments in securities Available-for-sale securities	**268,244**	**268,244**	**—**
④ Notes and accounts payable, electronically recorded obligations and other payables	**(1,299,743)**	**(1,299,743)**	**—**
⑤ Short-term borrowings from banks and other financial institutions	**(75,541)**	**(75,541)**	**—**
⑥ Commercial papers	**—**	**—**	**—**
⑦ Bonds	**(353,825)**	**(354,957)**	**(1,132)**
⑧ Long-term borrowings from banks and other financial institutions	**(261,530)**	**(261,530)**	**(0)**
⑨ Lease obligations	**(29,694)**	**(29,898)**	**(203)**
⑩ Derivative instruments			
i. Hedge accounting not applied	**468**	**468**	**—**
ii. Hedge accounting applied	**—**	**(5,404)**	**(5,404)**
⑪ Long-term payables	**(524,148)**	**(524,148)**	**—**

* Liabilities are in parentheses. Derivative instruments are presented as net amounts receivable or payable, with net amounts payable in parentheses.

*1: Method for calculating the fair value of financial instruments, derivative instruments and securities

① Cash and time deposits; ② Notes and accounts receivable
Carrying value is used for fair value for these short-term items because these amounts are approximately the same.

③ Short-term investments in securities and investments in securities
Short-term investments in securities are held as available-for-sale securities. Market prices on exchanges are used to determine the fair value of equity securities. Prices quoted by financial institutions are used to determine the fair value of bonds. Carrying value is used for fair value for instruments with short-term maturities included in available-for-sale securities because these amounts are approximately the same.

④ Notes, accounts payable, electronically recorded obligations and other payables; ⑤ Short-term borrowings from banks and other financial institutions; ⑥ Commercial papers
Carrying value approximates fair value for these short-term items.

⑦ Bonds
Fair value of bonds issued by the Company is calculated based on market prices.

⑧ Long-term borrowings from banks and other financial institutions
Floating-rate long-term borrowing reflects market interest rates. In addition, fair value approximates carrying value because the Company's creditworthiness does not vary significantly after assuming long-term borrowings. Therefore, carrying value is used for fair value of floating-rate long-term borrowing. Fair value of fixed-rate long-term borrowing is the discounted value of total principal and interest using an assumed interest rate on equivalent new borrowings.

⑨ Lease obligations
The fair value of lease obligations is the discounted present value of total principal and interest using an assumed interest rate on equivalent new lease transactions.

⑩ Derivative instruments
Please refer to Note 20. DERIVATIVE FINANCIAL INSTRUMENTS.

⑪ Long-term payables
Carrying value and fair value of long-term payables are measured and calculated as the present value discounted using the interest rate that is assumed to be applied when an additional loan is taken out from banks, etc. for future cash flows.

*2: Fair values that are difficult to determine as of December 31, 2016 and December 31, 2017

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	2017/12	2017/12
	Carrying value		
Shares of subsidiaries and affiliates	2,367	**2,310**	**20,433**
Unlisted equity securities	552	**516**	**4,564**
Investment in limited partnership and others	924	**910**	**8,049**

Market prices do not exist for these items, and estimating future cash flows is cost prohibitive. Therefore, these items are not included in ③ Short-term investments in securities and investments in securities, because their fair values are not readily determinable.
Loss on revaluation for securities stated at cost was recognized in the amounts of ¥21 million for the fiscal year ended December 31, 2016. There are no securities to be revaluated for the fiscal year ended December 31, 2017.

*3: Maturity dates of financial assets are as follows:

Millions of yen

	2016/12			
	Due in 1 year or less	Due after 1 year through 5 years	Due after 5 years through 10 years	Due after 10 years
Cash and time deposits	120,126	—	—	—
Notes and accounts receivable	134,835	—	—	—
Short-term investments in securities and investments in securities				
Available-for-sale securities with maturity (Negotiable certificate of deposit)	6,000	—	—	—
Available-for-sale securities with maturity (Corporate bonds)	—	—	—	—
Available-for-sale securities with maturity (Investment trust)	1,905	—	—	—
Available-for-sale securities with maturity (Investment in limited partnership and others)	77	846	—	—
Other	—	—	—	—
	262,945	846	—	—

Millions of yen

	2017/12			
	Due in 1 year or less	Due after 1 year through 5 years	Due after 5 years through 10 years	Due after 10 years
Cash and time deposits	**166,698**	**—**	**—**	**—**
Notes and accounts receivable	**160,331**	**—**	**—**	**—**
Short-term investments in securities and investments in securities				
Available-for-sale securities with maturity (Negotiable certificate of deposit)	**6,000**	**—**	**—**	**—**
Available-for-sale securities with maturity (Corporate bonds)	**—**	**—**	**—**	**—**
Available-for-sale securities with maturity (Investment trust)	**1,781**	**—**	**—**	**—**
Available-for-sale securities with maturity (Investment in limited partnership and others)	**910**	**—**	**—**	**—**
Other	**—**	**—**	**—**	**—**
	335,721	**—**	**—**	**—**

Thousands of U.S. dollars (Note 1)

	2017/12			
	Due in 1 year or less	Due after 1 year through 5 years	Due after 5 years through 10 years	Due after 10 years
Cash and time deposits	**1,474,551**	—	—	—
Notes and accounts receivable	**1,418,230**	—	—	—
Short-term investments in securities and investments in securities				
Available-for-sale securities with maturity (Negotiable certificate of deposit)	**53,073**	—	—	—
Available-for-sale securities with maturity (Corporate bonds)	—	—	—	—
Available-for-sale securities with maturity (Investment trust)	**15,754**	—	—	—
Available-for-sale securities with maturity (Investment in limited partnership and others)	**8,049**	—	—	—
Other	—	—	—	—
	2,969,668	—	—	—

19. SECURITIES

The acquisition cost, carrying amount, and gross unrealized gains and losses for securities stated at fair value by security type on December 31, 2016 and 2017 are as follows:
Available-for-sale securities:

Millions of yen

	2016/12			
	Carrying amount	Acquisition cost	Gross unrealized gains	Gross unrealized losses
Equity securities	19,899	10,123	9,899	(123)
Other	9,061	8,785	275	—
	28,961	18,909	10,175	(123)

Millions of yen

	2017/12			
	Carrying amount	Acquisition cost	Gross unrealized gains	Gross unrealized losses
Equity securities	**21,387**	**9,382**	**12,032**	**(27)**
Other	**8,937**	**8,875**	**62**	—
	30,325	**18,257**	**12,094**	**(27)**

Thousands of U.S. dollars (Note 1)

	2017/12			
	Carrying amount	Acquisition cost	Gross unrealized gains	Gross unrealized losses
Equity securities	**189,181**	**82,989**	**106,430**	**(238)**
Other	**79,053**	**78,505**	**548**	—
	268,244	**161,494**	**106,979**	**(238)**

Note: There is no loss on revaluation of investments in securities stated at fair value for the fiscal years 2016 and 2017, respectively.

Proceeds from sales, and gross realized gains and losses from sales of available-for-sale securities in the years ended December 31, 2016 and 2017 are as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	2017/12	2017/12
Proceeds from sales	650	**1,922**	**17,001**
Gross realized gains	403	**1,173**	**10,375**
Gross realized losses	0	**27**	**238**

20. DERIVATIVE FINANCIAL INSTRUMENTS

The contract amount, estimated fair value and unrealized gain (loss) of the derivative instruments as of December 31, 2016 are as follows:
① Derivatives that do not meet the criteria for hedge accounting

Millions of yen

		2016/12			
		Contract amount			
		Total	Settled over 1 year	Estimated fair value	Unrealized gain (loss)
Foreign exchange contracts: Selling	US$	12,828	—	(593)	(593)
	GBP	1,602	—	(19)	(19)
	AU$	159	—	1	1
Foreign exchange contracts: Buying	US$	1,048	—	10	10
		—	—	(601)	(601)

Note: Calculation method of fair value
Based on the amount presented by the financial institution

② Derivatives that meet the criteria for hedge accounting

Millions of yen

	2016/12			
		Contract amount		
	Main hedged item	Total	Settled over 1 year	Estimated fair value
Interest rate and currency swap contracts: To pay fixed yen / receive variable US$	Foreign currency long-term debt	2,500	—	718
Interest rate swap contracts: To pay fixed / receive variable	Long-term debt	20,295	19,565	(741)

Note: Calculation method of fair value
Based on the amount presented by the financial institution

The contract amount, estimated fair value and unrealized gain (loss) of the derivative instruments as of December 31, 2017 are as follows:

① Derivatives that do not meet the criteria for hedge accounting

Millions of yen

		2017/12			
		Contract amount			
		Total	Settled over 1 year	Estimated fair value	Unrealized gain (loss)
Foreign exchange contracts: Selling	US$	**24,447**	**—**	**69**	**69**
	EUR	**3,915**	**—**	**(2)**	**(2)**
	GBP	**3,049**	**—**	**(6)**	**(6)**
	AU$	**157**	**—**	**(0)**	**(0)**
Foreign exchange contracts: Buying	US$	**677**	**—**	**(1)**	**(1)**
	GBP	**469**	**—**	**(3)**	**(3)**
		—	**—**	**53**	**53**

Note: Calculation method of fair value
Based on the amount presented by the financial institution

Thousands of U.S. dollars (Note 1)

		2017/12			
		Contract amount			
		Total	Settled over 1 year	Estimated fair value	Unrealized gain (loss)
Foreign exchange contracts: Selling	US$	**216,249**	**—**	**610**	**610**
	EUR	**34,630**	**—**	**(17)**	**(17)**
	GBP	**26,970**	**—**	**(53)**	**(53)**
	AU$	**1,388**	**—**	**(0)**	**(0)**
Foreign exchange contracts: Buying	US$	**5,988**	**—**	**(8)**	**(8)**
	GBP	**4,148**	**—**	**(26)**	**(26)**
		—	**—**	**468**	**468**

② Derivatives that meet the criteria for hedge accounting

Millions of yen

	2017/12			
		Contract amount		
	Main hedged item	Total	Settled over 1 year	Estimated fair value
Interest rate swap contracts: To pay fixed / receive variable	**Long-term debt**	**19,565**	**18,835**	**(611)**

Note: Calculation method of fair value
Based on the amount presented by the financial institution

Thousands of U.S. dollars (Note 1)

	2017/12			
		Contract amount		
	Main hedged item	Total	Settled over 1 year	Estimated fair value
Interest rate swap contracts: To pay fixed / receive variable	**Long-term debt**	**173,065**	**166,607**	**(5,404)**

21. RETIREMENT BENEFITS

(1) The Company and its domestic consolidated subsidiaries have contributory funded pension plans, unfunded termination allowance plans, defined contribution plans and a retirement benefit prepayment plan. In some cases, additional voluntary retirement benefits were paid when an employee retired, which were accounted for as retirement benefit expenses when incurred. In addition, certain overseas subsidiaries have defined benefit plans, retirement allowance plans and defined contribution plans. The Company and certain consolidated subsidiaries use the simplified method to determine retirement benefits obligations.

(2) Details of defined benefit plans, including plans applying a simplified method as of December 31, 2016 and 2017 are as follows:

① Change in retirement benefit obligations

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	**2017/12**	**2017/12**
Balance at the beginning of the year	265,825	**282,348**	**2,497,549**
Service cost	6,996	**7,075**	**62,582**
Interest cost	3,015	**1,931**	**17,080**
Actuarial loss (gain)	17,571	**(5,289)**	**(46,784)**
Benefits paid	(10,706)	**(10,520)**	**(93,056)**
Other	(353)	**(1,605)**	**(14,197)**
Balance at the end of the year	282,348	**273,940**	**2,423,175**

② Change in plan assets

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	**2017/12**	**2017/12**
Balance at the beginning of the year	182,168	**187,859**	**1,661,733**
Expected return on plan assets	7,260	**5,595**	**49,491**
Actuarial loss (gain)	(3,168)	**4,806**	**42,512**
Contributions paid by the employer	9,567	**9,657**	**85,422**
Benefits paid	(7,879)	**(7,907)**	**(69,942)**
Other	(89)	**183**	**1,618**
Balance at the end of the year	187,859	**200,195**	**1,770,853**

③ Reconciliation of retirement benefit obligations and plan assets to liability for retirement benefits

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	**2017/12**	**2017/12**
Funded retirement benefit obligations	220,405	**221,291**	**1,957,461**
Plan assets	(187,859)	**(200,195)**	**(1,770,853)**
	32,546	**21,096**	**186,607**
Unfunded retirement benefit obligations	61,943	**52,649**	**465,714**
Total net liability for retirement benefits	94,489	**73,745**	**652,321**
Liability for retirement benefits	94,489	**73,745**	**652,321**
Total net liability for retirement benefits	94,489	**73,745**	**652,321**

④ Retirement benefit costs

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	2017/12	2017/12
Service cost	6,996	**7,075**	**62,582**
Interest cost	3,015	**1,931**	**17,080**
Expected return on plan assets	(7,260)	**(5,595)**	**(49,491)**
Net actuarial gain and loss amortization	7,190	**8,930**	**78,991**
Past service costs amortization	103	**25**	**221**
Other	2,200	**1,330**	**11,764**
Total retirement benefit costs	12,246	**13,698**	**121,167**

⑤ Adjustments for retirement benefits before tax

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	2017/12	2017/12
Net actuarial gain and loss amortization	13,445	**(19,054)**	**(168,544)**

⑥ Accumulated adjustments for retirement benefits before tax

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	2017/12	2017/12
Past service costs that are yet to be recognized	25	**0**	**0**
Actuarial gain and loss that are yet to be recognized	49,052	**30,152**	**226,713**
Total balance at the end of the year	49,078	**30,152**	**226,713**

⑦ Plan assets

I Plan assets comprise:

	2016/12	2017/12
Bonds	57.5%	**51.0%**
Equity securities	20.4%	**22.6%**
Other	22.1%	**26.4%**
Total	100.0%	**100.0%**

II Long-term expected rate of return

Terms of payment, portfolio of plan assets, historical returns, operating policy, market trends and other factors have been considered in determining the long-term expected rate of return.

⑧ Actuarial assumptions

The principal actuarial assumptions (expressed as weighted averages) are as follows:

	2016/12	2017/12
Discount rate	0.6%~0.8%	**0.5%~0.8%**
Long-term expected rate of return	4.0%	**3.0%**

(3) Defined contribution plans

Contributions to defined contribution plans and retirement benefit prepayment plans are ¥1,438 million and ¥428 million, respectively, for the year ended December 31, 2016.

Contributions to defined contribution plans and retirement benefit prepayment plans are ¥3,479 million ($30,773 thousand) and ¥457 million ($4,042 thousand), respectively, for the year ended December 31, 2017.

22. STOCK OPTION PLAN

Summary of stock options granted as of December 31, 2017 is as follows:

① Stock option plan approved by the shareholders on June 24, 2009 and resolved by the Board of Directors on July 30, 2009

	Stock options granted on August 28, 2009	Stock options granted on August 28, 2009	Total
Number of shares for options granted	81,400 shares	53,500 shares	134,900 shares
Number of shares for options outstanding	3,700 shares	11,400 shares	15,100 shares
Exercise price	¥1	¥1	
Exercisable period	August 1, 2012 – July 31, 2019	August 1, 2012 – July 31, 2019	

② Stock option plan approved by the shareholders on June 25, 2010 and resolved by the Board of Directors on July 29, 2010

	Stock options granted on August 30, 2010	Stock options granted on August 30, 2010	Total
Number of shares for options granted	59,100 shares	46,800 shares	105,900 shares
Number of shares for options outstanding	5,400 shares	9,700 shares	15,100 shares
Exercise price	¥1	¥1	
Exercisable period	August 1, 2013 – July 31, 2020	August 1, 2013 – July 31, 2020	

③ Stock option plan approved by the shareholders on June 24, 2011 and resolved by the Board of Directors on July 29, 2011

	Stock options granted on August 30, 2011	Stock options granted on August 30, 2011	Total
Number of shares for options granted	90,800 shares	63,600 shares	154,400 shares
Number of shares for options outstanding	7,300 shares	37,100 shares	44,400 shares
Exercise price	¥1	¥1	
Exercisable period	August 1, 2014 – July 31, 2026	August 1, 2014 – July 31, 2026	

④ Stock option plan approved by the shareholders on June 26, 2012 and resolved by the Board of Directors on July 31, 2012

	Stock options granted on August 30, 2012	Stock options granted on August 30, 2012	Total
Number of shares for options granted	108,600 shares	100,400 shares	209,000 shares
Number of shares for options outstanding	16,200 shares	40,000 shares	56,200 shares
Exercise price	¥1	¥1	
Exercisable period	August 1, 2015 – July 31, 2027	August 1, 2015 – July 31, 2027	

⑤ Stock option plan approved by the shareholders on June 25, 2013 and resolved by the Board of Directors on July 31, 2013

	Stock options granted on August 29, 2013	Stock options granted on August 29, 2013	Total
Number of shares for options granted	44,100 shares	39,500 shares	83,600 shares
Number of shares for options outstanding	28,800 shares	31,900 shares	60,700 shares
Exercise price	¥1	¥1	
Exercisable period	August 1, 2016 – July 31, 2028	August 1, 2016 – July 31, 2028	

⑥ Stock option plan approved by the shareholders on June 25, 2014 and resolved by the Board of Directors on July 31, 2014

	Stock options granted on August 28, 2014	Stock options granted on August 28, 2014	Total
Number of shares for options granted	76,900 shares	57,400 shares	134,300 shares
Number of shares for options outstanding	70,100 shares	56,900 shares	127,000 shares
Exercise price	¥1	¥1	
Exercisable period	August 1, 2017 – July 31, 2029	August 1, 2017 – July 31, 2029	

⑦ Stock option plan approved by the shareholders on June 23, 2015 and resolved by the Board of Directors on February 23, 2016

	Stock options granted on March 30, 2016	Stock options granted on March 30, 2016	Total
Number of shares for options granted	23,700 shares	46,300 shares	70,000 shares
Number of shares for options outstanding	23,700 shares	46,300 shares	70,000 shares
Exercise price	¥1	¥1	
Exercisable period	September 1, 2018 – February 28, 2031	September 1, 2018 – February 28, 2031	

⑧ Stock option plan approved by the shareholders on March 25, 2016 and resolved by the Board of Directors on February 23, 2017

	Stock options granted on March 30, 2017	Stock options granted on March 30, 2017	Total
Number of shares for options granted	40,400 shares	71,600 shares	112,000 shares
Number of shares for options outstanding	40,400 shares	71,600 shares	112,000 shares
Exercise price	¥1	¥1	
Exercisable period	September 1, 2019 – February 29, 2032	September 1, 2019 – February 29, 2032	

23. INCOME TAXES

Income taxes applicable to the Company and its domestic consolidated subsidiaries consist of corporation, inhabitants and enterprise taxes. The statutory income tax rate was 31% for the fiscal year ended December 31, 2017.

Reconciliation of the statutory tax rate and the effective tax rate for the years ended December 31, 2016 and 2017 is as follows:

	2016/12	2017/12
Statutory tax rate	33.0%	**31.0%**
Increase (decrease) due to:		
Permanently non-deductible expenses	0.8	**0.3**
Permanently non-taxable incomes	0.9	**1.3**
Unrealized intercompany profit	(4.2)	**(0.4)**
Adjustment of deferred tax assets for enacted changes in tax laws and rates	0.6	**—**
Tax credits	(2.9)	**(3.5)**
Differences of statutory tax rates for domestic consolidated subsidaries	0.6	**5.3**
Differences of statutory tax rates for overseas consolidated subsidiaries	1.4	**(10.1)**
Change in valuation allowance	1.0	**(0.1)**
Impairment of goodwill	—	**34.7**
Gain on transfer of business in tax	—	**(17.6)**
Impact of the Tax Reform Act in the United States	—	**(8.1)**
Others	0.8	**1.4**
Effective tax rate	32.0%	**34.2%**

(Changes in Presentation)

Due to the increase in quantitative significance of "Differences of statutory tax rates for domestic consolidated subsidiaries" which was included in "Others" in the previous fiscal year, the Company has changed to record it separately for this fiscal year.

In order to reflect this alteration, the consolidated financial statements for the fiscal year 2016 have been rearranged. As a result, 1.4% presented as "Others" in the chart above for the previous fiscal year has been reclassified into 0.6% of "Differences of statutory tax rates for domestic consolidated subsidiaries" and 0.8% of "Others" respectively.

Deferred tax assets and liabilities (both current and non-current) as of December 31, 2016 and 2017 are as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	2017/12	2017/12
Deferred tax assets:			
Liability for retirement benefits	30,854	**23,921**	**211,596**
Unrealized intercompany profit in inventory and property, plant and equipment	6,768	**6,240**	**55,196**
Inventories	12,845	**12,149**	**107,465**
Loss on revaluation of financial instruments	1,025	**405**	**3,582**
Accrued expenses	8,191	**8,548**	**75,612**
Accrued bonuses for employees	5,207	**5,872**	**51,941**
Tax losses carried forward	4,118	**2,753**	**24,352**
Depreciation	1,602	**3,024**	**26,749**
Reserve for sales returns	958	**724**	**6,404**
Accrued enterprise tax	781	**2,056**	**18,186**
Other	12,955	**9,246**	**81,786**
Total gross deferred tax assets	85,309	**74,943**	**662,919**
Less: valuation allowance	(6,474)	**(4,137)**	**(36,594)**
Total deferred tax assets	78,835	**70,805**	**626,315**
Deferred tax liabilities:			
Goodwill and other intangible assets	26,545	**9,136**	**80,813**
Unrealized gains (losses) on available-for-sale securities	2,812	**3,636**	**32,162**
Undistributed earnings of overseas consolidated subsidiaries	1,918	**2,167**	**19,168**
Special tax-purpose reserve	2,544	**2,511**	**22,211**
Other	3,843	**991**	**8,766**
Total deferred tax liabilities	37,664	**18,444**	**163,149**
Net deferred tax assets	41,170	**52,361**	**463,166**

Net deferred tax assets are included in the consolidated balance sheets as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	2017/12	2017/12
Current assets–deferred tax assets	21,773	**25,467**	**225,272**
Investments and other assets–deferred tax assets	37,800	**30,658**	**271,189**
Current liabilities–deferred tax liabilities	(0)	**(2)**	**(17)**
Long-term liabilities–deferred tax liabilities	(18,402)	**(3,762)**	**(33,277)**
Net deferred tax assets	41,170	**52,361**	**463,166**

(Impact of the Tax Reform Act in the United States)

In December 2017, the Tax Reform Act was passed in the United States, and the federal income tax rate will be reduced from 35% to 21% effective from January 1, 2018. As a result, "Deferred tax liabilities" decreased by ¥3,296 million ($29,155 thousand), "Deferred income taxes" decreased by ¥3,271 million ($28,934 thousand), "Accrued income taxes" increased by ¥158 million ($1,397 thousand), "Current income taxes" increased by ¥157 million ($1,388 thousand), and Foreign currency translation adjustments" increased by ¥23 million ($203 thousand).

24. BUSINESS COMBINATIONS

(Business Divestiture)

The Group concluded an agreement on transferring the shares of its consolidated subsidiary, Zotos International, Inc. (hereinafter "Zotos"), which operates a professional hair care business globally, and related business assets to Henkel AG & Co. KGaA (hereinafter, Henkel) on October 26, 2017, and completed the sale of the business on December 28, 2017.

1. Reason for the Transfer:

The Group has been promoting a selection and concentration strategy in order to enhance its brand portfolio across the globe and drive growth under its mid- to long-term business strategy VISION 2020, with which the Group aims to "Be a Global Winner with Our Heritage." The Group's Professional business plays an important role in its brand portfolio, and it plans to concentrate and boost its investment in the professional market in Asia.

While pursuing the selection and concentration strategy, the Group underwent a thorough review with Henkel regarding the transfer of Zotos, which is based in North America and generates the majority of its sales from the North American market. As a result, it arrived at the conclusion that transferring Zotos to Henkel would be the best option for Zotos and the Group, and thus, decided to sign the transfer agreement.

2. Name of the Transferee:

Henkel AG & Co. KGaA

3. Date of the Transfer:

December 28, 2017

4. Outline of Transaction Including Legal Form:

Share transfer for which consideration is funded only by cash

5. Name of the Subsidiary and Business Description:

(1) Name: Zotos International, Inc.

(2) Business description: Manufacturing and distribution of professional hair care, hair color and styling products

6. Summary of Accounting Treatment Used:

(1) Amount of gain on transfer

Gain on transfer of business ¥35,999 million ($318,434 thousand)

(2) Book value of assets and liabilities related to the transferred business and main breakdown

	Millions of yen	Thousands of U.S. dollars (Note 1)
Current assets	11,578	102,414
Fixed assets	11,647	103,025
Total assets	23,225	205,440
Current liabilities	3,752	33,188
Long-term liabilities	987	8,730
Total liabilities	4,739	41,919

(3) Accounting treatment

The difference between book value and sales price of the transferred shares, etc. is recorded in "Gain on transfer of business" under other income.

7. Reporting Segment of the Separated Business:

Professional Business

8. Estimated Profit Related to the Separated Business Recorded in the Consolidated Statements of Income for the Fiscal Year 2017:

	Millions of yen	Thousands of U.S. dollars (Note 1)
Net sales	26,982	238,673
Operating income	2,381	21,061

25. SEGMENT INFORMATION

(1) General information about reportable segments

With respect to its reportable segments, the Company is able to obtain delineated financial data from its structural units through co-administration. Accordingly, its segments are subject to regular examination in order to assist decision-making on allocation of managerial resources and evaluation of business performance by the Board of Directors.

Shiseido's main business is the production and sale of cosmetics. The Company engages in business activities under a matrix organization encompassing five brand categories based on consumer purchasing style (Prestige, Fragrance, Cosmetics, Personal Care and Professional) and six regions (Japan, China, Asia Pacific, the Americas, EMEA and Travel Retail). This matrix organization gives the leader in each region broad authority as well as responsibility for sales and profits to ensure flexible decision-making. In specific terms, the Company's seven reportable segments, which are mainly regions, are comprised of the "Japan Business," "China Business," "Asia Pacific Business," "Americas Business," "EMEA Business," "Travel Retail Business" and "Professional Business."

The Japan Business is mainly comprised of the domestic business by brand category (Prestige, Cosmetics and Personal Care, etc.) and the healthcare business (production and sale of health & beauty foods as well as over-the-counter drugs).

The China Business covers business in China by brand category (Prestige, Cosmetics and Personal Care, etc.).

The Asia Pacific Business covers business in the Asia and Oceania regions excluding Japan and China by brand category (Prestige, Cosmetics and Personal Care, etc.).

The Americas Business covers business in the Americas region by brand category (Prestige and Fragrance).

The EMEA Business covers business in Europe, the Middle East and African regions by brand category (Prestige and Fragrance, etc.).

The Travel Retail Business covers the operation of worldwide duty-free stores excluding Japan by brand category (Prestige, Fragrance and Cosmetics).

The Professional Business encompasses the manufacture and sale of hair and beauty salon products in the Americas, Japan, China, and the rest of Asia.

Other includes the manufacturing business, the frontier science business (production and sale of cosmetic raw materials, etc.), and the restaurant business.

(Changes in the Method of Classifying Reportable Segment)

The Company has revised its reportable segment classification method in line with the Group's internal financial management structure. As a result, the "Japan Business," "China Business," "Asia Pacific Business," "Americas Business," "EMEA Business" and "Travel Retail Business" reportable segments have been changed to the "Japan Business," "China Business," "Asia Pacific Business," "Americas Business," "EMEA Business," "Travel Retail Business" and "Professional Business" segments effective from the fiscal year ended December 31, 2017.

In line with this change, manufacturing operations, Frontier Science business, Restaurant business, etc. included in the "Japan Business" have been included in the "Other."

According to the change in the Company's management structure in line with our matrix organization approach, *bareMinerals, NARS* etc. in the United Kingdom included in the "Americas Business" have been included in the "EMEA Business." The Fragrance business in Latin America included in the "EMEA Business" has been included in the "Americas Business."

Segment information for the previous fiscal year has been restated in line with changes in the method of classifying reportable segments.

(2) Basis of measurement for reported segment sales, profit or loss and other material items

The accounting treatment for the Group's reported business segments is generally the same as described in 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES. Segment income is based on operating income.

The prices of intersegment transactions and transfers are determined by price negotiations based on the Company's submission of preferred prices after taking marketing conditions into account.

(3) Information about reported segment sales, profit or loss and other material items

Segment information for the fiscal year 2016 is as follows:

Millions of yen

	Reportable Segment					
	Japan Business	China Business	Asia Pacific Business	Americas Business	EMEA Business (*1)	Travel Retail Business
Net Sales						
Sales to Outside Customers	381,232	118,087	45,593	127,499	94,138	24,811
Intersegment Sales or Transfers	19,489	153	161	9,010	4,828	3
Total	400,721	118,240	45,754	136,510	98,966	24,815
Segment Income / (Loss)	56,356	3,629	1,064	(12,799)	(6,712)	5,368
Other Items						
Depreciation and Amortization	7,088	4,190	1,659	8,176	3,002	409
Amortization of Goodwill	141	385	61	3,702	—	—

	Reportable Segment	Other (*2)	Total	Adjustments (*3)	Total Shown in Consolidated Financial Statements (*4)
	Professional Business				
Net Sales					
Sales to Outside Customers	44,947	13,997	850,306	—	850,306
Intersegment Sales or Transfers	382	44,178	78,207	(78,207)	—
Total	45,329	58,176	928,514	(78,207)	850,306
Segment Income / (Loss)	1,103	(11,940)	36,071	708	36,780
Other Items					
Depreciation and Amortization	1,183	8,769	34,480	—	34,480
Amortization of Goodwill	624	—	4,916	—	4,916

*1 The EMEA Business includes the Middle East and African regions.
*2 "Other" includes head office administration departments, manufacturing operations as well as the activities of the Frontier Science business (production and sale of cosmetic raw materials, medical-use drugs, medical cosmetics, precision and analytical equipment), the Restaurant business, etc.
*3 Segment income/(loss) adjustment is mainly intersegment transaction eliminations.
*4 Segment income/(loss) is adjusted for operating income described in the consolidated statements of income.
*5 Assets and liabilities by segment are not provided because they are not subject to reallocation and appraisal of management resources on a periodic basis.

Segment information for the fiscal year 2017 is as follows:

Millions of yen

	Reportable Segment					
	Japan Business	China Business	Asia Pacific Business	Americas Business	EMEA Business (*1)	Travel Retail Business
Net Sales						
Sales to Outside Customers	431,026	144,266	54,169	140,413	128,418	44,495
Intersegment Sales or Transfers	30,574	305	1,471	19,000	9,153	349
Total	461,600	144,572	55,640	159,413	137,572	44,844
Segment Income / (Loss)	83,154	11,329	5,745	(10,288)	(3,181)	12,361
Other Items						
Depreciation and Amortization	6,928	3,964	1,933	9,795	6,679	396
Amortization of Goodwill	141	396	61	3,304	—	—

	Reportable Segment	Other (*2)	Total	Adjustments (*3)	Total Shown in Consolidated Financial Statements (*4)
	Professional Business				
Net Sales					
Sales to Outside Customers	47,959	14,314	1,005,062	—	1,005,062
Intersegment Sales or Transfers	399	78,728	139,982	(139,982)	—
Total	48,359	93,042	1,145,045	(139,982)	1,005,062
Segment Income / (Loss)	2,958	(12,926)	89,154	(8,716)	80,437
Other Items					
Depreciation and Amortization	856	9,059	39,614	—	39,614
Amortization of Goodwill	331	—	4,235	—	4,235

Thousands of U.S. dollars (Note 1)

	Reportable Segment					
	Japan Business	China Business	Asia Pacific Business	Americas Business	EMEA Business (*1)	Travel Retail Business
Net Sales						
Sales to Outside Customers	3,812,702	1,276,125	479,159	1,242,043	1,135,939	393,586
Intersegment Sales or Transfers	270,446	2,697	13,011	168,067	80,964	3,087
Total	4,083,149	1,278,832	492,171	1,410,110	1,216,912	396,674
Segment Income / (Loss)	735,550	100,212	50,818	(91,003)	(28,137)	109,340
Other Items						
Depreciation and Amortization	61,282	35,064	17,098	86,643	59,080	3,502
Amortization of Goodwill	1,247	3,502	539	29,226	—	—

	Reportable Segment	Other (*2)	Total	Adjustments (*3)	Total Shown in Consolidated Financial Statements (*4)
	Professional Business				
Net Sales					
Sales to Outside Customers	424,228	126,616	8,890,420	—	8,890,420
Intersegment Sales or Transfers	3,529	696,399	1,238,230	(1,238,230)	—
Total	427,766	823,016	10,128,659	(1,238,230)	8,890,420
Segment Income / (Loss)	26,165	(114,338)	788,624	(77,098)	711,517
Other Items					
Depreciation and Amortization	7,571	80,132	350,411	—	350,411
Amortization of Goodwill	2,927	—	37,461	—	37,461

*1 The EMEA Business includes the Middle East and African regions.
*2 "Other" includes head office administration departments, manufacturing operations as well as the activities of the Frontier Science business (production and sale of cosmetic raw materials, medical-use drugs, medical cosmetics, precision and analytical equipment), the Restaurant business, etc.
*3 Segment income/(loss) adjustment is mainly intersegment transaction eliminations.
*4 Segment income/(loss) is adjusted for operating income described in the consolidated statements of income.
*5 Assets and liabilities by segment are not provided because they are not subject to reallocation and appraisal of management resources on a periodic basis.

(Related Information)

For the fiscal year 2016

① Information on products and services

Sales to outside customers in the cosmetics business exceed 90% of net sales of the consolidated statement of income and, therefore, the Company omits this disclosure.

② Geographical information

I Net sales

Millions of yen

2016/12						
Japan	Americas		Europe	Asia / Oceania		Total
		U.S.A.			China	
407,735	148,351	130,176	95,301	198,918	129,820	850,306

Note: Classification of net sales is determined by country or geographical location.

II Property, Plant and Equipment

Millions of yen

2016/12						
Japan	Americas		Europe	Asia / Oceania		Total
		U.S.A.			China	
102,054	23,290	23,213	7,425	23,423	11,972	156,194

③ Main customers information

There is no outside customer representing 10% or more of net sales of the consolidated statement of income and, therefore, the Company omits this disclosure.

For the fiscal year 2017

① Information on products and services

Sales to outside customers in the cosmetics business exceed 90% of net sales of the consolidated statement of income and, therefore, the Company omits this disclosure.

② Geographical information

I Net sales

Millions of yen

2017/12						
Japan	Americas		Europe	Asia / Oceania		Total
		U.S.A.			China	
456,929	**163,934**	**137,788**	**128,334**	**255,865**	**160,951**	**1,005,062**

Thousands of U.S. dollars (Note 1)

2017/12						
Japan	Americas		Europe	Asia / Oceania		Total
		U.S.A.			China	
4,041,831	**1,450,101**	**1,218,823**	**1,135,196**	**2,263,290**	**1,423,715**	**8,890,420**

Note: Classification of net sales is determined by country or geographical location.

II Property, Plant and Equipment

Millions of yen

2017/12						
Japan	Americas		Europe	Asia / Oceania		Total
		U.S.A.			China	
111,601	**15,195**	**15,119**	**8,606**	**23,278**	**10,901**	**158,681**

Thousands of U.S. dollars (Note 1)

2017/12						
Japan	Americas		Europe	Asia / Oceania		Total
		U.S.A.			China	
987,182	**134,409**	**133,737**	**76,125**	**205,908**	**96,426**	**1,403,635**

③ Main customers information

There is no outside customer representing 10% or more of net sales of the consolidated statement of income and, therefore, the Company omits this disclosure.

(4) Information about segment loss on impairment of fixed assets

Millions of yen

2016/12								
Japan Business	China Business	Asia Pacific Business	Americas Business	EMEA Business	Travel Retail Business	Professional Business	Other	Total
—	153	0	—	—	—	—	—	153

Millions of yen

2017/12								
Japan Business	China Business	Asia Pacific Business	Americas Business	EMEA Business	Travel Retail Business	Professional Business	Other	Total
—	**47**	**—**	**70,874**	**—**	**—**	**0**	**—**	**70,922**

Thousands of U.S. dollars (Note 1)

2017/12								
Japan Business	China Business	Asia Pacific Business	Americas Business	EMEA Business	Travel Retail Business	Professional Business	Other	Total
—	**415**	**—**	**626,926**	**—**	**—**	**0**	**—**	**627,350**

(5) Information about segment unamortized goodwill

Millions of yen

2016/12								
Japan Business	China Business	Asia Pacific Business	Americas Business	EMEA Business	Travel Retail Business	Professional Business	Other	Total
745	2,836	195	54,403	2	—	1,612	—	59,795

Millions of yen

2017/12								
Japan Business	China Business	Asia Pacific Business	Americas Business	EMEA Business	Travel Retail Business	Professional Business	Other	Total
603	**2,331**	**128**	**9,100**	**2**	**—**	**—**	**—**	**12,166**

Thousands of U.S. dollars (Note 1)

2017/12								
Japan Business	China Business	Asia Pacific Business	Americas Business	EMEA Business	Travel Retail Business	Professional Business	Other	Total
5,333	**20,619**	**1,132**	**80,495**	**17**	**—**	**—**	**—**	**107,616**

26. TRANSACTIONS WITH RELATED PARTIES

Director and auditor of the significant corporate affiliate

For the fiscal year 2016

Type	Name	Location	Capital or Investments	Business or Profession	Voting Rights Held (%)	Relationship with the Related Parties	Transactions	Amount	Account Name	Balance as of December 31, 2016
Company with a majority of the voting rights held by an executive or close relative	Lucien Henri S.A.S (*1)	France	130 thousand EUR	Sales of cosmetics and fragrances	—	Sales of products	Sales of cosmetics and fragrances (*2)	¥20 million	Account Receivable	¥0 million

*1 100% directly held by an executive of Beauté Prestige International S.A. (BPI S.A.), Mr. Eric HENRY and close relatives
*2 Transactions are under normal terms and conditions, and considered as independent third-party transactions.

For the fiscal year 2017

Type	Name	Location	Capital or Investments	Business or Profession	Voting Rights Held (%)	Relationship with the Related Parties	Transactions	Amount	Account Name	Balance as of December 31, 2017
Company with a majority of the voting rights held by an executive or close relative	**Lucien Henri S.A.S (*1)**	**France**	**130 thousand EUR**	**Sales of cosmetics and fragrances**	**—**	**Sales of products**	**Sales of cosmetics and fragrances (*2)**	**¥24 million ($212 thousand)**	**Account Receivable**	**¥0 million ($0 thousand)**

*1 100% directly held by an executive of BPI S.A., Mr. Eric HENRY and close relatives
*2 Transactions are under normal terms and conditions, and considered as independent third-party transactions.

27. SHORT-TERM AND LONG-TERM DEBT

Short-term and long-term debt as of December 31, 2016 and 2017 are as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	**2017/12**	**2017/12**
Short-term borrowings from banks and other financial institutions			
(weighted average interest rate 5.10%)	6,339	**8,540**	**75,541**
Commercial papers	5,243	**—**	**—**
Short-term debt	11,583	**8,540**	**75,541**
Long-term borrowings from banks and other financial institutions			
(Borrowings due within one year, weighted average interest rate 0.54%)	3,230	**731**	**6,466**
(Borrowings due after one year, weighted average interest rate 0.37%)	62,196	**28,835**	**255,064**
0.001% unsecured yen bonds due in December 2019	10,000	**10,000**	**88,456**
0.237% unsecured yen bonds due in June 2020	15,000	**15,000**	**132,684**
0.374% unsecured yen bonds due in June 2022	15,000	**15,000**	**132,684**
Lease obligations			
(Borrowings due within one year, weighted average interest rate 2.05%)	1,744	**1,391**	**12,304**
(Borrowings due after one year, weighted average interest rate 2.15%)	1,826	**1,966**	**17,390**
Long-term payables (including other payables)			
(due within and after one year, weighted average interest rate 2.50%)	55,251	**59,151**	**523,228**
	164,248	**132,075**	**1,168,288**
Less: portion due within one year	(7,819)	**(3,663)**	**(32,401)**
Long-term debt	156,428	**128,411**	**1,135,877**

The aggregate annual maturities of short-term and long-term debt as of December 31, 2017 are as follows:

For the years ending December 31	Millions of yen	Thousands of U.S. dollars (Note 1)
2018	**12,203**	**107,943**
2019	**13,356**	**118,142**
2020	**18,360**	**162,406**
2021	**13,487**	**119,301**
2022	**19,149**	**169,385**
2023 and thereafter	**64,058**	**566,634**
	140,615	**1,243,830**

Assets pledged as collateral as of December 31, 2016 and 2017 are as follows:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	**2017/12**	**2017/12**
Cash and time deposits	1,808	**1,815**	**16,054**
Buildings and structures	13,161	**12,709**	**112,419**
Machinery and equipment	0	**0**	**0**
Investments in securities	1,155	**1,155**	**10,216**
Other investments	15,200	**15,200**	**134,453**
	31,327	**30,881**	**273,162**

The above assets are pledged as collateral for derivative transactions (interest rate swaps) and the following collateralized liabilities as of December 31, 2016 and 2017:

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2016/12	**2017/12**	**2017/12**
Current portion of long-term debt	730	**730**	**6,457**
Long-term debt	19,565	**18,835**	**166,607**
	20,295	**19,565**	**173,065**

28. CONTINGENT LIABILITIES

There are no significant contingent liabilities to be disclosed.

Independent Auditor's Report

To the Shareholders and Board of Directors of
Shiseido Company, Limited:

We have audited the accompanying consolidated financial statements of Shiseido Company, Limited and its consolidated subsidiaries, which comprise the consolidated balance sheets as at December 31, 2016 and 2017, and the consolidated statements of income, statements of comprehensive income, statements of changes in net assets and statements of cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

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 accounting principles generally accepted in Japan, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatements, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in Japan. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatements of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider 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, while the objective of the financial statement audit is 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 present fairly, in all material respects, the financial position of Shiseido Company, Limited and its consolidated subsidiaries as at December 31, 2016 and 2017, and their financial performance and cash flows for the years then ended in accordance with accounting principles generally accepted in Japan.

Convenience Translation

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended December 31, 2017 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 1 to the consolidated financial statements.

KPMG AZSA LLC

March 30, 2018
Tokyo, Japan