# Consolidated Financial Statements and Notes

## Consolidated Financial Statements

### Consolidated Statement of Profit or Loss and Other Comprehensive Income

Santen Pharmaceutical Co., Ltd. and Its Consolidated Subsidiaries

For the year ended March 31, 2018

| | | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|---|
| | Note | 2017 | 2018 | 2018 |
| Revenue | 6, 7 | ¥199,096 | ¥224,942 | $2,117,301 |
| Cost of sales | 8 | (74,966) | (86,378) | (813,046) |
| Gross profit | | 124,130 | 138,564 | 1,304,254 |
| Selling, general and administrative expenses | 8 | (62,193) | (68,788) | (647,474) |
| Research and development expenses | 8 | (22,786) | (24,398) | (229,649) |
| Amortization on intangible assets associated with products | 16 | (6,412) | (6,740) | (63,441) |
| Other income | 9 | 468 | 417 | 3,927 |
| Other expenses | 10 | (728) | (364) | (3,428) |
| Operating profit | | 32,479 | 38,691 | 364,189 |
| Finance income | 11 | 1,105 | 1,004 | 9,447 |
| Finance expenses | 11 | (3,529) | (434) | (4,087) |
| Profit before tax | | 30,055 | 39,261 | 369,548 |
| Income tax expenses | 12 | (8,331) | (4,000) | (37,649) |
| Net profit for the year | | 21,724 | 35,261 | 331,900 |
| Other comprehensive income for the year, net of tax | | | | |
| Items that will not be reclassified subsequently to profit or loss | | | | |
| Remeasurements of defined benefit plans | 13 | 297 | 284 | 2,671 |
| Net gain or loss on financial assets measured at fair value through other comprehensive income | 13 | (6,825) | 5,867 | 55,221 |
| Items that may be reclassified subsequently to profit or loss | | | | |
| Foreign currency translation adjustments | 13 | 2,715 | (686) | (6,461) |
| Other comprehensive income | 13 | (3,813) | 5,464 | 51,431 |
| Total comprehensive income for the year | | 17,911 | 40,725 | 383,330 |
| Profit attributable to | | | | |
| Owners of the company | | 21,731 | 35,247 | 331,769 |
| Non-controlling interests | | (7) | 14 | 131 |
| Net profit for the year | | 21,724 | 35,261 | 331,900 |
| Total comprehensive income attributable to | | | | |
| Owners of the company | | 17,924 | 40,648 | 382,607 |
| Non-controlling interests | | (13) | 77 | 724 |
| Total comprehensive income for the year | | ¥17,911 | ¥40,725 | $383,330 |

| Earnings per share | | Yen | | U.S. dollars |
|---|---|---|---|---|
| | | 2017 | 2018 | 2018 |
| Basic earnings per share | 14 | ¥52.96 | ¥86.73 | $0.82 |
| Diluted earnings per share | 14 | 52.76 | 86.42 | 0.81 |

## Consolidated Statement of Financial Position

Santen Pharmaceutical Co., Ltd. and Its Consolidated Subsidiaries
As of March 31, 2018

| | Note | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|---|
| | | 2017 | 2018 | 2018 |
| Assets | | | | |
| Non-current assets | | | | |
| Property, plant and equipment | 15 | ¥28,550 | ¥29,706 | $279,615 |
| Intangible assets | 16 | 138,935 | 134,495 | 1,265,952 |
| Financial assets | 17 | 29,889 | 35,775 | 336,736 |
| Deferred tax assets | 12 | 2,396 | 2,264 | 21,311 |
| Other non-current assets | | 2,124 | 2,855 | 26,878 |
| Total non-current assets | | 201,894 | 205,095 | 1,930,492 |
| Current assets | | | | |
| Inventories | 18 | 28,502 | 30,636 | 288,366 |
| Trade and other receivables | 19 | 70,970 | 78,654 | 740,344 |
| Other financial assets | 17 | 333 | 472 | 4,446 |
| Other current assets | | 3,909 | 4,322 | 40,677 |
| Cash and cash equivalents | 26 | 53,297 | 69,283 | 652,137 |
| Total current assets | | 157,011 | 183,367 | 1,725,971 |
| Total assets | | 358,906 | 388,463 | 3,656,462 |
| Equity and liabilities | | | | |
| Equity | | | | |
| Equity attributable to owners of the company | | | | |
| Share capital | 20 | 7,792 | 8,032 | 75,600 |
| Capital surplus | 20 | 8,417 | 8,657 | 81,486 |
| Treasury shares | 20 | (10) | (11) | (105) |
| Retained earnings | 20 | 223,283 | 249,225 | 2,345,863 |
| Other components of equity | 20, 21 | 15,628 | 19,921 | 187,512 |
| Total equity attributable to owners of the company | | 255,110 | 285,823 | 2,690,356 |
| Non-controlling interests | | 819 | 1,734 | 16,322 |
| Total equity | | 255,929 | 287,557 | 2,706,678 |
| Liabilities | | | | |
| Non-current liabilities | | | | |
| Financial liabilities | 22 | 26,288 | 21,244 | 199,961 |
| Net defined benefit liabilities | 23 | 1,900 | 1,804 | 16,983 |
| Provisions | 24 | 1,426 | 1,367 | 12,868 |
| Deferred tax liabilities | 12 | 17,963 | 12,909 | 121,510 |
| Other non-current liabilities | | 1,919 | 1,380 | 12,990 |
| Total non-current liabilities | | 49,496 | 38,704 | 364,311 |
| Current liabilities | | | | |
| Trade and other payables | 25 | 23,937 | 29,743 | 279,959 |
| Other financial liabilities | 22 | 17,649 | 14,404 | 135,576 |
| Income tax payable | | 3,279 | 7,656 | 72,061 |
| Provisions | 24 | 1,372 | 1,508 | 14,196 |
| Other current liabilities | | 7,244 | 8,890 | 83,681 |
| Total current liabilities | | 53,481 | 62,201 | 585,473 |
| Total liabilities | | 102,977 | 100,905 | 949,784 |
| Total equity and liabilities | | ¥358,906 | ¥388,463 | $3,656,462 |

## Consolidated Statement of Changes in Equity

Santen Pharmaceutical Co., Ltd. and Its Consolidated Subsidiaries

For the year ended March 31, 2017

Millions of yen

| | Note | Share capital | Capital surplus | Treasury shares | Retained earnings | Other components of equity | |
|---|---|---|---|---|---|---|---|
| | | | | | | Remeasurements of defined benefit plans | Net gain or loss on financial assets measured at fair value through other comprehensive income |
| Balance at April 1, 2016 | | ¥7,695 | ¥8,389 | ¥(24) | ¥221,945 | ¥— | ¥18,676 |
| Comprehensive income | | | | | | | |
| Net profit for the year | | | | | 21,731 | | |
| Other comprehensive income | 13 | | | | | 297 | (6,825) |
| Total comprehensive income for the year | | — | — | — | 21,731 | 297 | (6,825) |
| Transactions with owners | | | | | | | |
| Issuance of new shares | 20 | 97 | 97 | | | | |
| Acquisition of treasury shares | 20 | | (69) | (12,311) | | | |
| Disposal of treasury shares | 20 | | (0) | 0 | | | |
| Cancellation of treasury shares | 20 | | (0) | 12,325 | (12,325) | | |
| Dividends | 20 | | | | (10,751) | | |
| Establishment of subsidiary with non-controlling interests | | | | | | | |
| Share-based payments | 20, 21 | | | | | | |
| Other | | | | | 2,682 | (297) | (2,381) |
| Total transactions with owners | | 97 | 28 | 14 | (20,393) | (297) | (2,381) |
| Balance at March 31, 2017 | | ¥7,792 | ¥8,417 | ¥(10) | ¥223,283 | ¥— | ¥9,470 |

Millions of yen

| | Note | Other components of equity | | | Total equity attributable to owners of the company | Non-controlling interests | Total equity |
|---|---|---|---|---|---|---|---|
| | | Foreign currency translation adjustments | Subscription rights to shares | Total | | | |
| Balance at April 1, 2016 | | ¥2,611 | ¥716 | ¥22,003 | ¥260,009 | ¥— | ¥260,009 |
| Comprehensive income | | | | | | | |
| Net profit for the year | | | | — | 21,731 | (7) | 21,724 |
| Other comprehensive income | 13 | 2,721 | | (3,807) | (3,807) | (6) | (3,813) |
| Total comprehensive income for the year | | 2,721 | — | (3,807) | 17,924 | (13) | 17,911 |
| Transactions with owners | | | | | | | |
| Issuance of new shares | 20 | | (24) | (24) | 169 | | 169 |
| Acquisition of treasury shares | 20 | | | — | (12,380) | | (12,380) |
| Disposal of treasury shares | 20 | | | — | 0 | | 0 |
| Cancellation of treasury shares | 20 | | | — | — | | — |
| Dividends | 20 | | | — | (10,751) | | (10,751) |
| Establishment of subsidiary with non-controlling interests | | | | — | — | 832 | 832 |
| Share-based payments | 20, 21 | | 138 | 138 | 138 | | 138 |
| Other | | | (4) | (2,682) | — | | — |
| Total transactions with owners | | — | 110 | (2,568) | (22,823) | 832 | (21,991) |
| Balance at March 31, 2017 | | ¥5,332 | ¥825 | ¥15,628 | ¥255,110 | ¥819 | ¥255,929 |

Santen Pharmaceutical Co., Ltd. and Its Consolidated Subsidiaries
For the year ended March 31, 2018

Millions of yen

| | Note | Share capital | Capital surplus | Treasury shares | Retained earnings | Other components of equity | |
|---|---|---|---|---|---|---|---|
| | | | | | | Remeasurements of defined benefit plans | Net gain or loss on financial assets measured at fair value through other comprehensive income |
| Balance at April 1, 2017 | | ¥7,792 | ¥8,417 | ¥(10) | ¥223,283 | ¥— | ¥9,470 |
| Comprehensive income | | | | | | | |
| Net profit for the year | | | | | 35,247 | | |
| Other comprehensive income | 13 | | | | | 284 | 5,867 |
| Total comprehensive income for the year | | — | — | — | 35,247 | 284 | 5,867 |
| Transactions with owners | | | | | | | |
| Issuance of new shares | 20 | 240 | 240 | | | | |
| Acquisition of treasury shares | 20 | | | (1) | | | |
| Dividends | 20 | | | | (10,563) | | |
| Changes for equity of subsidiary with non-controlling interests | | | | | | | |
| Share-based payments | 20, 21 | | | | | | |
| Other | | | | | 1,257 | (284) | (973) |
| Total transactions with owners | | 240 | 240 | (1) | (9,306) | (284) | (973) |
| Balance at March 31, 2018 | | ¥8,032 | ¥8,657 | ¥(11) | ¥249,225 | ¥— | ¥14,364 |

Millions of yen

| | Note | Other components of equity | | | Total equity attributable to owners of the company | Non-controlling interests | Total equity |
|---|---|---|---|---|---|---|---|
| | | Foreign currency translation adjustments | Subscription rights to shares | Total | | | |
| Balance at April 1, 2017 | | ¥5,332 | ¥825 | ¥15,628 | ¥255,110 | ¥819 | ¥255,929 |
| Comprehensive income | | | | | | | |
| Net profit for the year | | | | — | 35,247 | 14 | 35,261 |
| Other comprehensive income | 13 | (749) | | 5,401 | 5,401 | 63 | 5,464 |
| Total comprehensive income for the year | | (749) | — | 5,401 | 40,648 | 77 | 40,725 |
| Transactions with owners | | | | | | | |
| Issuance of new shares | 20 | | (68) | (68) | 412 | | 412 |
| Acquisition of treasury shares | 20 | | | — | (1) | | (1) |
| Dividends | 20 | | | — | (10,563) | | (10,563) |
| Changes for equity of subsidiary with non-controlling interests | | | | — | — | 838 | 838 |
| Share-based payments | 20, 21 | | 218 | 218 | 218 | | 218 |
| Other | | | | (1,257) | — | | — |
| Total transactions with owners | | — | 150 | (1,107) | (9,934) | 838 | (9,096) |
| Balance at March 31, 2018 | | ¥4,583 | ¥975 | ¥19,921 | ¥285,823 | ¥1,734 | ¥287,557 |

Santen Pharmaceutical Co., Ltd. and Its Consolidated Subsidiaries

For the year ended March 31, 2018

Thousands of U.S. dollars

| | Note | Share capital | Capital surplus | Treasury shares | Retained earnings | Other components of equity | |
|---|---|---|---|---|---|---|---|
| | | | | | | Remeasurements of defined benefit plans | Net gain or loss on financial assets measured at fair value through other comprehensive income |
| Balance at April 1, 2017 | | $73,341 | $79,226 | ($93) | $2,101,685 | $- | $89,139 |
| Comprehensive income | | | | | | | |
| Net profit for the year | | | | | 331,769 | | |
| Other comprehensive income | 13 | | | | | 2,671 | 55,221 |
| Total comprehensive income for the year | | — | — | — | 331,769 | 2,671 | 55,221 |
| Transactions with owners | | | | | | | |
| Issuance of new shares | 20 | 2,259 | 2,259 | | | | |
| Acquisition of treasury shares | 20 | | | (12) | | | |
| Dividends | 20 | | | | (99,423) | | |
| Changes for equity of subsidiary with non-controlling interests | | | | | | | |
| Share-based payments | 20, 21 | | | | | | |
| Other | | | | | 11,832 | (2,671) | (9,161) |
| Total transactions with owners | | 2,259 | 2,259 | (12) | (87,591) | (2,671) | (9,161) |
| Balance at March 31, 2018 | | $75,600 | $81,486 | ($105) | $2,345,863 | $- | $135,200 |

Thousands of U.S. dollars

| | Note | Other components of equity | | | Total equity attributable to owners of the company | Non-controlling interests | Total equity |
|---|---|---|---|---|---|---|---|
| | | Foreign currency translation adjustments | Subscription rights to shares | Total | | | |
| Balance at April 1, 2017 | | $50,190 | $7,769 | $147,098 | $2,401,258 | $7,711 | $2,408,969 |
| Comprehensive income | | | | | | | |
| Net profit for the year | | | | — | 331,769 | 131 | 331,900 |
| Other comprehensive income | 13 | (7,055) | | 50,837 | 50,837 | 593 | 51,431 |
| Total comprehensive income for the year | | (7,055) | — | 50,837 | 382,607 | 724 | 383,330 |
| Transactions with owners | | | | | | | |
| Issuance of new shares | 20 | | (643) | (643) | 3,876 | | 3,876 |
| Acquisition of treasury shares | 20 | | | — | (12) | | (12) |
| Dividends | 20 | | | — | (99,423) | | (99,423) |
| Changes for equity of subsidiary with non-controlling interests | | | | — | — | 7,887 | 7,887 |
| Share-based payments | 20, 21 | | 2,051 | 2,051 | 2,051 | | 2,051 |
| Other | | | | (11,832) | — | | — |
| Total transactions with owners | | — | 1,408 | (10,424) | (93,508) | 7,887 | (85,621) |
| Balance at March 31, 2018 | | $43,135 | $9,177 | $187,512 | $2,690,356 | $16,322 | $2,706,678 |

## Consolidated Statement of Cash Flows

Santen Pharmaceutical Co., Ltd. and Its Consolidated Subsidiaries

For the year ended March 31, 2018

| | | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|---|
| | Note | 2017 | 2018 | 2018 |
| Cash flows from operating activities | | | | |
| Net profit for the year | | ¥21,724 | ¥35,261 | $331,900 |
| Depreciation and amortization | | 9,882 | 10,896 | 102,556 |
| Impairment losses | | 475 | 150 | 1,415 |
| Finance expenses (income) | | 983 | (327) | (3,080) |
| Income tax expenses | | 8,331 | 4,000 | 37,649 |
| Decrease (increase) in trade and other receivables | | (5,489) | (7,116) | (66,981) |
| Decrease (increase) in inventories | | (4,120) | (1,435) | (13,508) |
| Increase (decrease) in trade and other payables | | (425) | 5,697 | 53,628 |
| Increase (decrease) in provisions and net defined benefit liabilities | | (200) | 285 | 2,682 |
| Other | | 2,877 | 1,706 | 16,061 |
| Subtotal | | 34,039 | 49,117 | 462,320 |
| Interest received | | 74 | 145 | 1,360 |
| Dividends received | | 681 | 598 | 5,628 |
| Interest paid | | (52) | (27) | (256) |
| Income tax paid | | (23,900) | (6,990) | (65,790) |
| Net cash flows from (used in) operating activities | | 10,843 | 42,843 | 403,262 |
| Cash flows from investing activities | | | | |
| Proceeds from withdrawal of time deposits | | 19 | — | — |
| Payments for acquisition of investments | | (478) | (565) | (5,319) |
| Proceeds from sale of investments | | 1,364 | 2,879 | 27,103 |
| Payments for acquisition of subsidiary | 27 | (19,064) | — | — |
| Payments for acquisition of property, plant and equipment | | (4,145) | (3,984) | (37,500) |
| Proceeds from sales of property, plant and equipment | | 4 | — | — |
| Payments for acquisition of intangible assets | | (5,355) | (5,953) | (56,033) |
| Other | | (545) | (636) | (5,990) |
| Net cash flows from (used in) investing activities | | (28,201) | (8,259) | (77,739) |
| Cash flows from financing activities | | | | |
| Proceeds from long-term loans payable | | 3,000 | — | — |
| Repayments of long-term loans payable | | (9,524) | (8,316) | (78,276) |
| Payments for acquisition of treasury shares | 20 | (12,380) | (1) | (12) |
| Capital contribution from non-controlling interests | | 832 | 838 | 7,887 |
| Dividends paid | | (10,751) | (10,559) | (99,393) |
| Other | | 167 | 408 | 3,840 |
| Net cash flows from (used in) financing activities | | (28,657) | (17,631) | (165,954) |
| Net increase (decrease) in cash and cash equivalents | | (46,015) | 16,953 | 159,569 |
| Cash and cash equivalents at the beginning of period | 26 | 99,798 | 52,282 | 492,114 |
| Effect of exchange rate changes on cash and cash equivalents | | (1,501) | 48 | 454 |
| Cash and cash equivalents at the end of period | 26 | ¥52,282 | ¥69,283 | $652,137 |

# Notes to Consolidated Financial Statements

## 1. Reporting Entity

Santen Pharmaceutical Co., Ltd. and its consolidated subsidiaries (the"Santen Group") conduct businesses centered on the production and sale of prescription pharmaceuticals.

Santen Pharmaceutical Co., Ltd. (the"Company") is a company incorporated in Japan. The addresses of the Company's headquarters and its major operating sites are disclosed on its corporate website (http://www.santen.com/en/).

The shares of the Company are listed on the Tokyo Stock Exchange.

## 2. Basis of Preparation

### (1) Compliance with IFRS

The Santen Group has prepared its consolidated financial statements under International Financial Reporting Standards ("IFRS").

### (2) Basis of Measurement

The Santen Group's consolidated financial statements have been prepared on a historical cost basis, except for the financial instruments stated in Note 3"Significant Accounting Policies."

### (3) Functional Currency and Presentation Currency

The Santen Group's consolidated financial statements are presented in Japanese yen, which is the Company's functional currency. All financial information presented in Japanese yen has been rounded to the nearest million, except when otherwise indicated.

For the convenience of readers outside Japan, the accompanying consolidated financial statements are also presented in U.S. dollars by translating Japanese yen amounts at the exchange rate of ¥106.24 to US $1.00, the approximate rate of exchange at the end of March 31, 2018. Such translations should not be construed as representations that the Japanese yen amounts could be converted into U.S. dollars at the above or any other rate.

### (4) Early Adoption of New Standards

The Santen Group has early adopted IFRS 9 *Financial Instruments* ("IFRS 9") (amended in October 2010 and December 2011) since the transition date (April 1, 2013).

IFRS 9 replaces IAS 39 *Financial Instruments: Recognition and Measurement* and divides financial instruments into two classifications: those measured at amortized cost and those measured at fair value. Changes in the fair value of financial assets measured at fair value are recognized in profit or loss. Changes in fair value with respect to investments in equity instruments are recognized in other comprehensive income, except for equity instruments held for trading purposes.

### (5) Approval of Consolidated Financial Statements

The Santen Group's consolidated financial statements for the fiscal year ended March 31, 2018 were approved by Chairman and CEO Akira Kurokawa and Senior Corporate Officer, Corporate Administration, Chief Financial Officer(CFO), Head of Finance and Administration Division Kazuo Koshiji on August 3, 2018.

## 3. Significant Accounting Policies

Unless otherwise stated, the Santen Group has consistently applied the accounting policies set forth below to all periods presented on the consolidated financial statements.

### 1) Basis of Consolidation

The Santen Group's consolidated financial statements have been prepared based on the financial statements of the Company, subsidiaries and associates.

A. Subsidiaries

Subsidiaries are entities controlled by the Santen Group.

Control means that the Santen Group has power over the investee, has exposure to variable returns from involvement with the investee, and has the ability to use its power over the investee to affect the amount of the investors' returns.

The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control is lost.

In the case of changes in the ownership interest in subsidiaries, if the Company retains control over the subsidiaries, they are accounted for as equity transactions.

All intra-group balances and transactions, and any unrealized income and expenses arising from intra-group transactions are eliminated in preparing consolidated financial statements.

The financial statements of subsidiaries that have different fiscal year-ends than the Santen Group are consolidated using financial statements based on a provisional closing as of the Santen Group's fiscal year-end.

B. Associates

Associates are entities over which the Santen Group has significant influence over the financial and operating policies, but does not have control or joint control over it.

Investments in associates are accounted for using the equity method, from the date on which the Group obtains significant influence to the date on which the Santen Group loses significant influence.

**2) Business Combinations**

Business combinations are accounted for using the acquisition method.

The identifiable assets acquired and the liabilities assumed are measured at the fair values at the acquisition date.

The Santen Group measures the consideration for an acquisition as the sum of (1) the consideration transferred in a business combination, (2) the amount of any non-controlling interest and (3) in a business combination achieved in stages, the acquisition-date fair value of the acquirer's previously held equity interest in the acquiree. The Santen Group recognizes goodwill as any excess of this consideration for acquisition over the net amount of the identifiable assets acquired and the liabilities assumed at the acquisition date. If the net amount of the identifiable assets and liabilities of the acquiree exceeds the consideration for acquisition, the acquirer recognizes the excess amount as profit or loss on the acquisition date. The consideration transferred in the business combination is calculated as the sum of the acquisition-date fair values of the assets transferred by the acquirer, the liabilities incurred by the acquirer to former owners of the acquiree and the equity interests issued by the acquirer.

Any expenses arising in connection with business combinations are accounted for as cost when incurred.

**3) Foreign Currency Translation**

Foreign currency transactions are translated into the functional currency using exchange rates at the dates of transactions or rates that approximate the exchange rates at the dates of the transactions.

Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency using the exchange rate at the fiscal year-end, and exchange differences are recognized as profit or loss.

Assets and liabilities of foreign operations are translated into the presentation currency using the exchange rate at the fiscal year-end. Income and expenses of foreign operations are translated into the presentation currency using the average exchange rate during the fiscal year, except for cases of significant exchange rate movements. Exchange differences are recognized in other comprehensive income. If a foreign operation is discontinued, the cumulative exchange differences of the relevant foreign operation are reclassified to profit or loss when it is discontinued.

**4) Revenue**

A. Revenue

Revenue is measured at the fair value of the consideration received or receivable, less trade discounts, returns, and taxes such as consumption taxes. The Santen Group primarily recognizes the following as revenue:

*i Sale of goods*

Revenue from the sale of goods is recognized when all the following conditions have been satisfied:

(a) The Santen Group has transferred to the buyer the significant risks and rewards of ownership of the goods;

(b) The Santen Group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;

(c) The amount of revenue can be measured reliably;

(d) It is probable that the economic benefits associated with the transaction will flow to the entity;

(e) The costs incurred or to be incurred in respect of the transaction can be measured reliably.

*ii Intellectual property*

Revenue from intellectual property is recognized on an accrual basis in accordance with the substance of the relevant agreement.

B. Other Income

Revenue that is based on factors other than the aforementioned revenue and finance income is recognized as other income.

C. Finance Income

*i Interest*

Interest is recognized using the effective interest method.

*ii Dividends*

Dividends are recognized when the Group's right to receive the dividend is established.

**5) Research and Development Expenses**

Internally generated development expenses are recognized as an intangible asset only if the capitalisation criteria under IAS 38 are satisfied.

Therefore, internal expenditure incurred for ongoing internal development projects is not capitalised until marketing approval is obtained from the regulatory authorities in a major market, which is considered the time at which the criteria of capitalisation under IAS 38 are met.

Expenditure on research and development of an internal project is fully expensed as "Research and development expenses" when incurred.

**6) Government Grants**

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

Government grants related to income are recognized in profit or loss on a systematic basis over the periods in which the entity recognizes as expenses the related costs for which the grants are intended to compensate.

Government grants related to assets are recognized as deferred income that is recognized in profit or loss on a systematic basis over the useful life of the asset.

**7) Income Taxes**

Income taxes consist of current income taxes and deferred taxes.

Current income tax is measured at the amount that is expected to be paid to or recoverd from the taxation authorities using the tax rates enacted or substantively enacted at the end of the reporting period. Current income tax is recognized in profit or loss, except for taxes that arise from transactions or events that are recognized in other comprehensive income or directly in equity as well as those that arise from business combinations.

Deferred taxes are calculated based on the temporary differences between the carrying amounts for financial reporting purposes and the amounts used for taxation purposes at the end of the reporting period. Deferred tax assets are recognized for deductible temporary differences, unused tax credits and unused tax losses to the extent that it is probable that future taxable profit will be available against which they can be utilized. Deferred tax liabilities are basically recognized for taxable temporary differences.

Deferred tax assets and deferred tax liabilities are not recognized for temporary differences on the initial recognition of assets or liabilities in a transaction that is not a business combination and affects neither accounting profit nor taxable profit on the transaction date. Deferred tax liabilities are not recognized for taxable temporary differences on initial recognition of goodwill.

Deferred tax liabilities are not recognized for taxable temporary differences associated with investments in subsidiaries and associates when the parent company is able to control the timing of the reversal of the temporary difference and it is probable that the temporary difference will not be reversed within the foreseeable future. Moreover, deferred tax assets are not recognized for deductible temporary differences when the temporary difference will be reversed in the foreseeable future or taxable profit will be available against which the temporary difference can be utilized.

Deferred tax assets and liabilities are calculated based on the tax rates that are expected to apply to the period when the deferred tax assets will be realized or the deferred tax liabilities will be settled.

Deferred tax assets and deferred tax liabilities are offset when there is a legally enforceable right to offset current tax assets and current tax liabilities and the deferred tax assets and liabilities are related to income taxes levied by the same taxation authority on the same taxable entity.

**8) Property, Plant and Equipment**

Property, plant and equipment is recognized at cost, which includes any costs directly attributable to the acquisition of the asset and dismantlement, removal and restoration costs, as well as borrowing costs eligible for capitalization.

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

Property, plant and equipment other than land are depreciated using the straight-line method over the estimated useful lives of each item from the date the assets are available for use. The estimated useful lives of major property, plant and equipment are as follows:

| | |
|---|---|
| Buildings and structures | :3 to 50 years |
| Machinery and vehicles | :3 to 10 years |
| Tools, furniture and fixtures | :4 to 10 years |

The depreciation methods, residual values and estimated useful lives are reviewed annually and adjusted as necessary.

Impairment losses are stated in“10)Impairment of Property, Plant and Equipment and Intangible Assets.”

**9) Intangible Assets**

Intangible assets are identifiable non-monetary assets without physical substance and have been acquired individually or through business combinations. The major intangible assets are goodwill, intangible assets associated with products, and software.

<u>A. Goodwill</u>

The measurement of goodwill on initial recognition is stated in“2) Business combinations.”After initial recognition, goodwill is not amortized and is measured at cost less any accumulated impairment losses. Goodwill is allocated to the cash-generating units that are expected to benefit from synergies derived from business combinations.

B. Intangible Assets Other than Goodwill

Intangible assets other than goodwill that are acquired individually are recognized at cost, specifically any cost directly attributable to the acquisition of the asset. Intangible assets other than goodwill that are acquired through business combinations are recognized based on the fair value at the business combination date.

After recognition, intangible assets are measured using the cost model and are stated at cost less accumulated amortization and accumulated impairment losses.

These intangible assets are amortized using the straight-line method over the estimated useful lives (within approximately 20 years) from the date the assets are available for use. The estimated useful lives are calculated based on the term of legal protection or the economical life, and are regularly reviewed.

Impairment losses are shown in“10)Impairment of Property, Plant and Equipment and Intangible Assets.”

The treatment of expenditures related to research and development incurred within the Santen Group is shown in“5) Research and Development Expenses.”

**10) Impairment of Property, Plant and Equipment and Intangible Assets**

At the end of each reporting period, the Santen Group assesses whether there is any indication of impairment that property, plant and equipment and intangible assets available for use may be impaired for each asset or cash-generating unit. If there is an indication of impairment, the Santen Group performs impairment test and assesses the recoverability of each asset or cash-generating unit.

Goodwill and intangible assets that are not yet available for use are performed impairment test annually, irrespective of whether there is any indication of impairment.

The cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflow from other assets or groups of assets.

The recoverable amount of an asset or a cash-generating unit is determined at the higher of its fair value less cost of disposal or its value in use. In determining the value in use, the estimated future cash flow is discounted to the present value using a discount rate that reflects the time value of money and the risks specific to the asset. If the carrying amount of the asset or cash-generating unit exceeds the recoverable amount, impairment loss is recognized in profit or loss and the carrying amount is reduced to the recoverable amount.

An asset or a cash-generating unit other than goodwill for which impairment loss was recognized in prior years is assessed at the end of the reporting period to determine whether there is any indication that the impairment loss recognized in prior periods may no longer exist or may have decreased. If any such indication exists, the recoverable amount of the asset or cash-generating unit is estimated. In cases in which the recoverable amount exceeds the carrying amount of the asset or cash-generating unit, the impairment loss is reversed up to the lower of the estimated recoverable amount or the carrying amount that would have been determined if no impairment loss had been recognized in prior years.

**11) Leases**

Leases are classified as finance leases when substantially all the risks and rewards incidental to ownership of an asset are transferred to the lessee. Leases other than finance leases are classified as operating leases.

At the commencement of the lease term, the Companies recognize finance leases as assets and liabilities in the consolidated statement of financial position at amounts equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments, each determined at the inception of the lease. The lease assets that have been recognized are depreciated on a straight-line basis over the shorter of the estimated useful life and the lease term of the asset.

Lease payments under an operating lease shall be recognized as an expense on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit.

**12) Financial Instruments**

A. Financial Assets

*i Initial recognition and measurement*

The Santen Group recognizes financial assets on the trade date when the Group becomes party to the contractual provisions of the financial asset.

If the following conditions (a) and (b) are met, the financial assets that have been initially recognized are classified as financial assets measured at amortized cost; otherwise, they are classified as financial assets measured at fair value. Equity investment other than held for trading is measured at fair value through other comprehensive income.

(a) The asset is held within a business model whose objective is to hold assets in order to collect contractual cash flows;

(b) The contractual terms of the instrument give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding

Financial assets are initially measured at fair value plus transaction costs directly attributable to the financial assets, except for financial assets measured at fair value through profit or loss.

*ii Subsequent measurement*

The financial assets measured at amortized cost are calculated using the effective interest method.

The financial assets measured at fair value are measured with any changes in fair value recognized through profit or loss. In addition, changes in the fair value of equity instruments other than held for trading are recognized through other comprehensive income and presented as"Net gain or loss on financial assets measured at fair value through other comprehensive income"in other components of equity. The amount of other components of equity is transferred directly to retained earnings, not to profit or loss, when the equity investment is derecognized or the decline in its fair value compared to its acquisition cost is significant and other than temporary.

*iii Impairment losses*

Financial assets that are measured at amortized cost are assessed whether there is any objective evidence of impairment at the end of each reporting period. If there is objective evidence of impairment, impairment loss is recognized in profit or loss as the difference between the financial asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate.

If an impairment loss is reduced by an event occurring after the recognition of impairment losses, the reduction in the impairment loss is reversed through profit or loss.

*iv Derecognition*

The Santen Group derecognizes a financial asset only when the contractual right to receive the cash flows from the asset expires or when the Companies transfer the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. On derecognition of a financial asset, the difference between the carrying amount and the consideration received or receivable is recognized in profit or loss, and the cumulative gain or loss that was previously accumulated in other comprehensive income (loss) is reclassified to retained earnings.

B. Financial Liabilities

*i Initial recognition and measurement*

The Santen Group recognizes financial liabilities on the trade date when the Group becomes a party to the contractual provisions of the financial liability.

Financial liabilities that have been initially recognized are classified as financial liabilities measured at amortized cost, except for financial liabilities measured at fair value through profit or loss.

Financial liabilities except for financial liabilities at fair value through profit or loss are initially measured at fair value less transaction costs that are directly attributable to the issuance.

*ii Subsequent measurement*

The financial liabilities measured at amortized cost are measured using the effective interest method.

The financial liabilities measured at fair value through profit or loss are measured at fair value and any gains or losses arising on remeasurement are recognized in profit or loss.

*iii Derecognition*

The Santen Group derecognizes financial liabilities when the obligation specified in the contract is exempted, cancelled, or expired.

C. Offsetting of Financial Assets and Financial Liabilities

Financial assets and financial liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Santen Group:

(a) Currently has a legally enforceable right to set off the recognized amounts;

(b) Intends either to settle on a net basis, or realize the asset and settle the liability simultaneously.

D. Derivatives

The Company utilizes derivatives for hedging the risk arising from fluctuation in foreign currency exchange rates, interest rates and share price. Derivatives are initially measured at fair value on the date when the derivative contracts are entered into and are subsequently remeasured to fair value at each reporting date. The Santen Group does not enter into derivatives for trading or speculative purposes.

E. Hedge Accounting

The Santen Group designates certain derivatives as cash flow hedges and adopts hedge accounting for the derivatives.

At the inception of the hedge, the Santen Group documents the relationship between the hedging instrument and the hedged item, and the risk management objectives and strategies for undertaking the hedge. The Santen Group also assesses whether the derivatives used in hedging transactions are highly effective in achieving offsetting changes in cash flows of hedged items both at the hedge inception and on an ongoing basis. When a hedging instrument is designated as a cash flow hedge and meets the criteria for hedge accounting, the effective portion of the gains or losses on the hedging instrument is recognized in other comprehensive income. The ineffective portion of gains or losses on the hedging instrument is recognized in profit or loss.

The cumulative gain or loss that was previously recognized in other comprehensive income is reclassified to profit or loss in the same period when the cash flows of the hedged items are recognized in profit or loss and at the same line item in the consolidated statement of profit or loss and other comprehensive income.

Hedge accounting is discontinued when the Santen Group revokes the hedge designation, when the hedging instrument expires or is sold, terminated or exercised, or when the hedge no longer qualifies for hedge accounting.

**13) Inventories**

Inventories are measured at the lower of cost and net realizable value.

The cost of inventories is calculated based on the weighted-average cost method, including raw materials, direct labor and other direct costs as well as relevant overhead expenses. The net realizable value is determined based on the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

**14) Cash and Cash Equivalents**

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

**15) Assets Held for Sale**

The Santen Group classifies a non-current asset or disposal group which must be available for immediate sale in its present condition and its sale must be highly probable as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use.

The Santen Group measures a non-current asset or disposal group classified as held for sale at the lower of its carrying amount and fair value less costs to sell.

**16) Capital**

A. Ordinary Shares

Proceeds from the issuance of ordinary shares are included in share capital and capital surplus. The transaction costs (net of tax) of equity transactions are deducted from capital surplus.

B. Treasury Shares

Treasury shares purchased by the Company are measured as the amount of the consideration paid for the shares and are recognized as a deduction from capital. The Company does not recognize any gains or losses on the acquisition, sale or cancellation of treasury shares. If the Company sells treasury shares, any differences between the carrying amount and the sales amount are recorded under capital surplus.

**17) Share-based Payments**

The Santen Group has a share option plan as equity-settled share-based payments for its directors and corporate officers. Share options are measured at fair value on the grant date and the fair value is calculated using the Black-Scholes model. The fair value of share options are recognized as expenses and the corresponding amount as an increase in equity on the grant date.

**18) Employee Benefits**

A. Post-employment Benefits

The Santen Group has adopted defined benefit plans and defined contribution plans as post-employment benefit plans for employees.

*i Defined benefit plans*

The present value of defined benefit obligation and the related current service costs and past service cost are calculated based on the projected unit credit method.

The discount rates are determined with reference to the market yields of high-quality corporate bonds at the end of each reporting period. Service cost and net interest on the net defined benefit liabilities are recognized in profit or loss.

Actuarial gains and losses, return on plan assets excluding amounts included in net interest on the net defined benefit liabilities, and changes in the effect of the asset ceiling are recognized in other comprehensive income and reclassified to retained earnings in the period in which they are recognized.

*ii Defined contribution plans*

Costs for defined contribution plans are recognized as expenses when they are paid.

B. Short-term Employee Benefits

The undiscounted amount of short-term employee benefits expected to be paid in exchange for that service are recognized as expenses when employees have rendered services to the Santen Group.

**19) Provisions**

A provision is recognized when the Santen Group has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and the amount of the obligations can be estimated reliably. When the effect of the time value of money is material, the amount of a provision shall be the present value of the expenditures expected to be required to settle the obligation.

**4. Use of Judgments, Estimates and Assumptions**

In preparing the Santen Group's consolidated financial statements, management makes judgments, estimates and assumptions that affect the adoption of accounting policies and the reported amounts of assets and liabilities, and income and expenses. Actual results may differ from these estimates.

Judgments, estimates and assumptions made by management that may have a significant effect on the amounts recognized in the consolidated financial statements are as follows:

• Impairment of property, plant and equipment and intangible assets
• Recoverability of deferred tax assets
• Provisions
• Measurement of defined benefit obligations
• Fair value of financial instruments
• Measurement of the fair value of assets acquired and liabilities assumed through business combinations
• Evaluation of the fair value of contingent consideration from business combinations
• Share-based payments

**5. New Standards and Interpretations Not Yet Adopted**

The new standards, interpretations and amendments that have been issued for the consolidated financial statements, which the Santen Group has not yet adopted as of the approval date of the consolidated financial statements are set forth in the table below.
The impact of the adoption of IFRS 15 Revenue from Contracts with Customers ("IFRS 15") and IFRS 9 Financial Instruments ("IFRS 9") (amended in November 2013 and July 2014) on the Santen Group is estimated to be negligible. The impact of the adoption of IFRS 16 Leases ("IFRS 16") is currently under review and cannot be estimated at this time.

| IFRS | | Mandatory adoption (From the fiscal year beginning on or after) | To be adopted by the Santen Group | Description of new standards, interpretations and amendments |
|---|---|---|---|---|
| IFRS 15 | Revenue from Contracts with Customers | January 1, 2018 | Fiscal year ending March 2019 | New revenue standards which supersede IAS 18"Revenue,"IAS 11"Construction Contracts"and a number of revenue-related interpretations |
| IFRS 9 | Financial Instruments | January 1, 2018 | Fiscal year ending March 2019 | Amendments to classification, measurement, impairment and hedge accounting of financial instruments |
| IFRS 16 | Lease | January 1, 2019 | Fiscal year ending March 2020 | Amendments to accounting treatment for lease arrangements |

## 6. Operating Segments

### (1) Reportable Segments

The reportable segments of the Santen Group are segments for which separate financial information is available, and that are evaluated regularly by the Board of Directors in order to decide on resource allocation and assess performance.

Previously, the Santen Group's reportable segment comprised the pharmaceuticals segment, with all operating segments other than the reportable segments classified in the other segment. From the fiscal year ended March 31, 2018, the Santen Group has reclassified its businesses into a single integrated operating segment, which it has designated as its reportable segment.

This reclassification was made after the Santen Group determined that it would be more reasonable to present the Santen Group's businesses as an integrated whole, as a result of reviewing the operating segments in light of factors such as the actual state of business development and the management structure.

### (2) Products and Services Information

For the year ended March 31, 2017 (April 1, 2016 to March 31, 2017)

Millions of yen

| | Prescription pharmaceuticals | OTC pharmaceu ticals | Medical devices | Other | Total |
|---|---|---|---|---|---|
| Revenue from external customers | ¥183,469 | ¥12,553 | ¥2,536 | ¥537 | ¥199,096 |

For the year ended March 31, 2018 (April 1, 2017 to March 31, 2018)

Millions of yen

| | Prescription pharmaceuticals | OTC pharmaceu ticals | Medical devices | Other | Total |
|---|---|---|---|---|---|
| Revenue from external customers | ¥206,967 | ¥14,594 | ¥2,583 | ¥798 | ¥224,942 |

For the year ended March 31, 2018 (April 1, 2017 to March 31, 2018)

Thousands of U.S. dollars

| | Prescription pharmaceuticals | OTC pharmaceu ticals | Medical devices | Other | Total |
|---|---|---|---|---|---|
| Revenue from external customers | $1,948,110 | $137,370 | $24,312 | $7,509 | $2,117,301 |

### (3) Geographical Areas Information

For the year ended March 31, 2017 (April 1, 2016 to March 31, 2017)

Millions of yen

| | Japan | EMEA | Americas | Asia | Total |
|---|---|---|---|---|---|
| Revenue from external customers*1 | ¥145,358 | ¥28,657 | ¥1,433 | ¥23,647 | ¥199,096 |
| Non-current assets*2 | 112,933 | 8,405 | 44,793 | 3,479 | 169,609 |

Notes:

1. Revenue is classified into countries or regions based on customer location.
2. Non-current assets are classified into countries or regions based on the asset location. Financial instruments and deferred tax assets are excluded. The non-current assets in the Americas are located in the U.S.A.
3. The table above has been retrospectively adjusted following the completion of the purchase price allocation for the acquisition of InnFocus, Inc.
4. The table above has been restated to reflect a reclassification of geographical areas.

For the year ended March 31, 2018 (April 1, 2017 to March 31, 2018)

Millions of yen

| | Japan | EMEA | Americas | Asia | Total |
|---|---|---|---|---|---|
| Revenue from external customers*1 | ¥158,653 | ¥35,015 | ¥371 | ¥30,903 | ¥224,942 |
| Non-current assets*2 | 110,912 | 9,089 | 42,430 | 4,626 | 167,057 |

For the year ended March 31, 2018 (April 1, 2017 to March 31, 2018)

Thousands of U.S. dollars

| | Japan | EMEA | Americas | Asia | Total |
|---|---|---|---|---|---|
| Revenue from external customers*1 | $1,493,348 | $329,588 | $3,490 | $290,875 | $2,117,301 |
| Non-current assets*2 | 1,043,973 | 85,553 | 399,378 | 43,541 | 1,572,445 |

Notes:

1. Revenue is classified into countries or regions based on customer location.
2. Non-current assets are classified into countries or regions based on the asset location. Financial instruments and deferred tax assets are excluded. The non-current assets in the Americas are located in the U.S.A.
3. From the fiscal year ended March 31, 2018, Middle East and Africa have been integrated into the previously shown Europe area to form the new EMEA area. Previously, the Middle East and Africa were included in Asia and Other. This reclassification was made to better reflect the Group’s management structure in the geographical areas.

**(4) Information on Major Customers**

For the year ended March 31, 2017 (April 1, 2016 to March 31, 2017)

Millions of yen

| Major customers | Revenue |
|---|---|
| Suzuken Co., Ltd. | ¥38,506 |
| Mediceo Corporation | 31,411 |

For the year ended March 31, 2018 (April 1, 2017 to March 31, 2018)

Millions of yen

| Major customers | Revenue |
|---|---|
| Suzuken Co., Ltd. | ¥42,463 |
| Mediceo Corporation | 33,680 |

For the year ended March 31, 2018 (April 1, 2017 to March 31, 2018)

Thousands of U.S. dollars

| Major customers | Revenue |
|---|---|
| Suzuken Co., Ltd. | $399,691 |
| Mediceo Corporation | 317,015 |

**7. Revenue**

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Sale of goods | ¥197,939 | ¥224,519 | $2,113,319 |
| Other | 1,157 | 423 | 3,982 |
| Total | ¥199,096 | ¥224,942 | $2,117,301 |

**8. Nature of Major Expenses**

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Wages and bonuses | ¥30,726 | ¥33,834 | $318,466 |
| Advertising and sales promotion expenses | 16,515 | 19,109 | 179,866 |
| Legal welfare expenses | 4,279 | 4,671 | 43,965 |
| Post-employment benefit cost | 2,212 | 2,401 | 22,604 |
| Depreciation and amortization | 3,470 | 4,156 | 39,119 |

Note: The amounts in the above table are recorded in cost of sales, selling, general and administrative expenses, and research and development expenses.

**9. Other Income**

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Gain on disposal of non-current assets | ¥4 | ¥− | $− |
| Government grants | 176 | 69 | 652 |
| Other | 288 | 348 | 3,275 |
| Total | ¥468 | ¥417 | $3,927 |

**10. Other Expenses**

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Loss on disposal of non-current assets | ¥130 | ¥30 | $279 |
| Impairment losses *1 | 475 | 150 | 1,415 |
| Other | 123 | 184 | 1,734 |
| Total | ¥728 | ¥364 | $3,428 |

Note: Impairment losses are stated in Note 15 "Property, Plant and Equipment 2)" and Note 16 "Intangible Assets 2)."

## 11. Finance Income and Expenses

### (1) Finance Income

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Interest income | | | |
| Financial assets measured at amortized cost | ¥81 | ¥147 | $1,380 |
| Financial assets measured at fair value through profit or loss | — | 10 | 98 |
| Dividend income | | | |
| Financial assets measured at fair value through other comprehensive income | 684 | 598 | 5,628 |
| Life insurance | 144 | 154 | 1,452 |
| Total dividend income | 828 | 752 | 7,080 |
| Foreign exchange gains | — | 94 | 889 |
| Changes in the fair value of contingent consideration | 197 | — | — |
| Other | 0 | 0 | 0 |
| Total | ¥1,105 | ¥1,004 | $9,447 |

Note: The table above has been retrospectively adjusted following the completion of the purchase price allocation for the acquisition of InnFocus, Inc.

### (2) Finance Expenses

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Interest expense | | | |
| Financial liabilities measured at amortized cost | ¥50 | ¥24 | $230 |
| Other | 0 | 1 | 10 |
| Total interest expense | 51 | 25 | 240 |
| Foreign exchange losses | 3,460 | — | — |
| Net interest related to post-employment benefits | 8 | 6 | 60 |
| Changes in the fair value of financial assets measured at fair value through profit or loss | — | 231 | 2,179 |
| Other | 10 | 171 | 1,608 |
| Total | ¥3,529 | ¥434 | $4,087 |

Note: The table above has been retrospectively adjusted following the completion of the purchase price allocation for the acquisition of InnFocus, Inc.

## 12. Deferred Taxes and Income Taxes

### 1) Deferred Taxes

i. Major items and changes in deferred tax assets and liabilities

Millions of yen

| | As of April 1, 2016 | Recognized through profit or loss | Recognized in other comprehensive income | Changes of business combinations | As of March 31, 2017 |
|---|---|---|---|---|---|
| Deductible temporary differences | | | | | |
| Retirement benefit liabilities | ¥3,243 | ¥72 | ¥(141) | ¥－ | ¥3,173 |
| Inventories | 447 | 415 | － | － | 862 |
| Accrued bonuses | 788 | 41 | － | － | 829 |
| Depreciation and amortization | 1,116 | (390) | － | － | 726 |
| Research and development expenses | 1,934 | (1,303) | － | － | 631 |
| Accrued enterprise taxes | 1,277 | (1,088) | － | － | 188 |
| Paid absences | 136 | (4) | － | － | 132 |
| Impairment losses | 73 | (5) | － | － | 69 |
| Unearned revenue | 100 | (71) | － | － | 29 |
| Other | 1,221 | 360 | － | － | 1,581 |
| Subtotal | 10,334 | (1,973) | (141) | － | 8,219 |
| Taxable temporary differences | | | | | |
| Financial assets measured at fair value through other comprehensive income | (8,335) | － | 3,093 | － | (5,242) |
| Intangible assets associated with products | (4,596) | (1,664) | － | (14,675) | (20,935) |
| Other | (33) | 5 | － | － | (28) |
| Subtotal | (12,965) | (1,658) | 3,093 | (14,675) | (26,204) |
| Unused tax losses and tax credits | | | | | |
| Unused tax credits | 933 | (93) | － | － | 840 |
| Unused tax losses | 54 | 539 | － | 985 | 1,578 |
| Subtotal | 987 | 446 | － | 985 | 2,418 |
| Net amount | ¥(1,643) | ¥(3,185) | ¥2,951 | ¥(13,690) | ¥(15,567) |

Notes:

1. The difference between the net amount of temporary differences recognized through profit or loss in the table above and the total deferred income taxes stated in “2) Income Tax Expenses i. Income Taxes Recognized through Profit or Loss” is attributable to foreign exchange fluctuations.
2. The table above has been retrospectively adjusted following the completion of the purchase price allocation for the acquisition of InnFocus, Inc.

Millions of yen

| | As of March 31, 2017 | Recognized through profit or loss | Recognized in other comprehensive income | As of March 31, 2018 |
|---|---|---|---|---|
| Deductible temporary differences | | | | |
| Retirement benefit liabilities | ¥3,173 | ¥217 | ¥(141) | ¥3,248 |
| Inventories | 862 | 90 | － | 952 |
| Accrued bonuses | 829 | (20) | － | 809 |
| Depreciation and amortization | 726 | 48 | － | 774 |
| Research and development expenses | 631 | (50) | － | 581 |
| Accrued enterprise taxes | 188 | 224 | － | 413 |
| Paid absences | 132 | (5) | － | 127 |
| Impairment losses | 69 | 12 | － | 80 |
| Unearned revenue | 29 | 3 | － | 32 |
| Other | 1,581 | 144 | － | 1,725 |
| Subtotal | 8,219 | 664 | (141) | 8,741 |
| Taxable temporary differences | | | | |
| Financial assets measured at fair value through other comprehensive income | (5,242) | － | (2,150) | (7,391) |
| Intangible assets associated with products | (20,935) | 6,591 | － | (14,344) |
| Other | (28) | (2) | － | (29) |
| Subtotal | (26,204) | 6,589 | (2,150) | (21,764) |
| Unused tax losses and tax credits | | | | |
| Unused tax credits | 840 | (54) | － | 786 |
| Unused tax losses | 1,578 | 14 | － | 1,593 |
| Subtotal | 2,418 | (40) | － | 2,378 |
| Net amount | ¥(15,567) | ¥7,213 | ¥(2,291) | ¥(10,645) |

Note: The difference between the net amount of temporary differences recognized through profit or loss in the table above and the total deferred income taxes stated in “2) Income Tax Expenses i. Income Taxes Recognized through Profit or Loss” is attributable to foreign exchange fluctuations.

Thousands of U.S. dollars

| | As of March 31, 2017 | Recognized through profit or loss | Recognized in other comprehensive income | As of March 31, 2018 |
|---|---|---|---|---|
| Deductible temporary differences | | | | |
| Retirement benefit liabilities | $29,865 | $2,045 | $(1,327) | $30,574 |
| Inventories | 8,111 | 846 | — | 8,958 |
| Accrued bonuses | 7,804 | (184) | — | 7,620 |
| Depreciation and amortization | 6,833 | 456 | — | 7,289 |
| Research and development expenses | 5,940 | (470) | — | 5,470 |
| Accrued enterprise taxes | 1,774 | 2,110 | — | 3,884 |
| Paid absences | 1,243 | (49) | — | 1,195 |
| Impairment losses | 645 | 112 | — | 757 |
| Unearned revenue | 269 | 32 | — | 301 |
| Other | 14,882 | 1,353 | — | 16,234 |
| Subtotal | 77,365 | 6,252 | (1,327) | 82,280 |
| Taxable temporary differences | | | | |
| Financial assets measured at fair value through other comprehensive income | (49,338) | — | (20,237) | (69,571) |
| Intangible assets associated with products | (197,050) | 62,037 | — | (135,013) |
| Other | (260) | (16) | — | (276) |
| Subtotal | (246,649) | 62,021 | (20,237) | (204,860) |
| Unused tax losses and tax credits | | | | |
| Unused tax credits | 7,903 | (509) | — | 7,394 |
| Unused tax losses | 14,857 | 134 | — | 14,990 |
| Subtotal | 22,760 | (375) | — | 22,384 |
| Net amount | $(146,524) | $67,898 | $(21,564) | $(100,196) |

Note: The difference between the net amount of temporary differences recognized through profit or loss in the table above and the total deferred income taxes stated in "2) Income Tax Expenses i. Income Taxes Recognized through Profit or Loss" is attributable to foreign exchange fluctuations.

ii. Deductible temporary differences, unused tax losses and unused tax credits for which no deferred tax assets are recognized in the statement of financial position

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Deductible temporary differences | ¥642 | ¥764 | $7,187 |
| Carry-forwards of unused tax losses | 7,076 | 6,090 | 57,327 |
| Carry-forwards of unused tax credits | 1,261 | 1,553 | 14,621 |

Note: The table above has been retrospectively adjusted following the completion of the purchase price allocation for the acquisition of InnFocus, Inc.

iii. The expiry schedule for unused tax losses for which no deferred tax assets are recognized in the statement of financial position

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| 1st year | ¥2 | ¥10 | $94 |
| 2nd year | 6 | 52 | 493 |
| 3rd year | 53 | 47 | 444 |
| 4th year | 7 | 41 | 388 |
| 5th year onward | 7,008 | 5,940 | 55,908 |
| Total | ¥7,076 | ¥6,090 | $57,327 |

Note: The table above has been retrospectively adjusted following the completion of the purchase price allocation for the acquisition of InnFocus, Inc.

iv. In the fiscal years ended March 31, 2018 and 2017, there were subsidiaries that recognized carry-forwards of unused tax losses. In the fiscal year ended March 31, 2018, deferred tax assets of ¥1,593 million ($14,990 thousand) were recognized to the extent that future taxable profit is expected (¥1,578 million as of March 31, 2017). The recoverability of deferred tax assets depends on future taxable profit. The future taxable profit used to recognize these deferred tax assets has been projected in line with business plans approved by management, and is highly likely to be achieved based on a comparison of actual performance trends against previous plans. Accordingly, management believes that the recoverability of deferred tax assets presents no particular issues.

v. In the fiscal years ended March 31, 2018 and 2017, the Company did not recognize deferred tax liabilities related to the taxable temporary differences associated with investment in subsidiaries, because the Company was able to control the timing of the reversal of the temporary differences and it was probable that such differences would not be reversed in the foreseeable future. The taxable temporary differences associated with investments in subsidiaries for which deferred tax liabilities have not been recognized amounted to ¥13,581 million ($127,837 thousand) as of March 31, 2018 and ¥9,342 million as of March 31, 2017.

**2) Income Tax Expenses**

i. Income Taxes Recognized through Profit or Loss

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Current income taxes | | | |
| Current | ¥6,667 | ¥10,963 | $103,189 |
| Subtotal | 6,667 | 10,963 | 103,189 |
| Deferred income taxes | | | |
| Occurrence and reversal of temporary differences | 1,663 | (1,414) | (13,309) |
| Change in tax rate | — | (5,549) | (52,231) |
| Subtotal | 1,663 | (6,963) | (65,540) |
| Total income tax expenses | ¥8,331 | ¥4,000 | $37,649 |

Current income taxes include tax benefits arising from previously unrecognized carry-forwards of unused tax losses, tax credits or temporary differences of a prior period. As a result of these tax benefits, current income taxes were reduced by ¥12 million ($118 thousand) in the fiscal year ended March 31, 2018 and ¥105 million in the fiscal year ended March 31, 2017.

Deferred taxes do not contain tax benefits arising from previously unrecognized carry-forwards of tax losses, tax credits or temporary differences of a prior period, as well as deferred tax expenses arising from the write-down, or reversals of previous write-down of deferred tax assets.

ii. Reconciliation of Applicable Income Tax Rate

The Company is subject mainly to corporate tax, inhabitant tax and enterprise tax, and the effective statutory tax rate calculated on those taxes was 30.8% for the fiscal years ended March 31, 2018 and 2017 respectively. Foreign subsidiaries are subject to income taxes in their respective countries.

| | 2017 | 2018 |
|---|---|---|
| Effective statutory income tax rate | 30.8% | 30.8% |
| Non-deductible items / non-taxable income | 1.4% | 1.0% |
| Tax credit for research and development expenses | (5.9)% | (6.8)% |
| Differences in tax rates applied to subsidiaries | (1.8)% | (2.2)% |
| Effect of changes in tax rates | — | (14.0)% |
| Movements in unrecognized deferred tax assets | 1.1% | 1.5% |
| Effect of changes in contingent consideration | 1.8% | (0.8)% |
| Other | 0.3% | 0.7% |
| Actual tax rate | 27.7% | 10.2% |

The Tax Cuts and Jobs Act was enacted on December 22, 2017 (local time) in the United States. The major changes introduced by the new Act included a reduction in the federal corporate tax rate from 35% to 21% from January 1, 2018. In line with this change, the Santen Group has performed a revaluation of deferred tax assets and deferred tax liabilities at its U.S. subsidiaries based on the new corporate tax rate. As a result, income tax expenses were reduced by ¥5,105 million ($48,053 thousand).

## 13. Other Comprehensive Income

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Remeasurements of defined benefit plans | | | |
| Amounts arising during the year | ¥438 | ¥424 | $3,994 |
| Reclassification adjustments to profit or loss | — | — | — |
| Before tax effects | 438 | 424 | 3,994 |
| Tax effects | (141) | (141) | (1,323) |
| Remeasurements of defined benefit plans | 297 | 284 | 2,671 |
| Net gain or loss on financial assets measured at fair value through other comprehensive income | | | |
| Amounts arising during the year | (9,820) | 8,449 | 79,523 |
| Reclassification adjustments to profit or loss | — | — | — |
| Before tax effects | (9,820) | 8,449 | 79,523 |
| Tax effects | 2,995 | (2,582) | (24,302) |
| Net gain or loss on financial assets measured at fair value through other comprehensive income | (6,825) | 5,867 | 55,221 |
| Foreign currency translation adjustments | | | |
| Amounts arising during the year | 2,715 | (686) | (6,461) |
| Reclassification adjustments to profit or loss | — | — | — |
| Before tax effects | 2,715 | (686) | (6,461) |
| Tax effects | — | — | — |
| Foreign currency translation adjustments | 2,715 | (686) | (6,461) |
| Total other comprehensive income | ¥(3,813) | ¥5,464 | $51,431 |

**14. Earnings Per Share**

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Basis of calculating basic earnings per share | | | |
| Profit attributable to owners of the Company | ¥21,731 | ¥35,247 | $331,769 |
| Profit not attributable to ordinary shareholders of the Company | — | — | — |
| Profit used to calculate basic earnings per share | 21,731 | 35,247 | 331,769 |
| Basis of calculating diluted earnings per share | | | |
| Profit used to calculate basic earnings per share | ¥21,731 | ¥35,247 | $331,769 |
| Adjustment | — | — | — |
| Profit used to calculate diluted earnings per share | 21,731 | 35,247 | 331,769 |

| | Thousands of shares | |
|---|---|---|
| | 2017 | 2018 |
| Weighted average number of shares during the year | 410,343 | 406,415 |
| Subscription rights to shares | 1,537 | 1,456 |
| Weighted average number of diluted ordinary shares during the year | 411,880 | 407,871 |

| | Yen | | U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Earnings per share (attributable to owners of the Company): | | | |
| Basic | ¥52.96 | ¥86.73 | $0.82 |
| Diluted | 52.76 | 86.42 | 0.81 |

## 15. Property, Plant and Equipment

### 1) Statements of Changes in Acquisition Cost, Accumulated Depreciation and Accumulated Impairment Losses and the Carrying Amount by Category

A. Acquisition Cost

Millions of yen

| | Buildings and structures | Machinery, equipment and vehicles | Tools, fixtures and fittings | Land | Construction in progress | Total |
|---|---|---|---|---|---|---|
| Balance as of April 1, 2016 | ¥45,872 | ¥14,669 | ¥13,107 | ¥6,939 | ¥3,106 | ¥83,693 |
| Additions | 844 | 143 | 1,006 | − | 2,050 | 4,043 |
| Business combinations | 6 | 5 | 1 | − | − | 13 |
| Transfers | 100 | 701 | 148 | − | (949) | − |
| Disposals | (269) | (358) | (354) | − | (307) | (1,287) |
| Foreign currency translation differences | ¥(341) | ¥(139) | ¥(167) | ¥(4) | ¥(203) | ¥(854) |
| Balance as of March 31, 2017 | 46,212 | 15,022 | 13,741 | 6,935 | 3,698 | 85,609 |
| Additions | 399 | 352 | 621 | − | 2,793 | 4,164 |
| Transfers | 872 | 2,258 | 274 | − | (3,404) | − |
| Disposals | (53) | (219) | (375) | − | (2) | (649) |
| Foreign currency translation differences | 310 | 60 | 133 | 5 | 100 | 608 |
| Balance as of March 31, 2018 | ¥47,740 | ¥17,474 | ¥14,394 | ¥6,940 | ¥3,185 | ¥89,732 |

Thousands of U.S. dollars

| | Buildings and structures | Machinery, equipment and vehicles | Tools, fixtures and fittings | Land | Construction in progress | Total |
|---|---|---|---|---|---|---|
| Balance as of March 31, 2017 | $434,981 | $141,396 | $129,344 | $65,277 | $34,810 | $805,809 |
| Additions | 3,754 | 3,317 | 5,842 | − | 26,285 | 39,198 |
| Transfers | 8,205 | 21,254 | 2,581 | − | (32,040) | − |
| Disposals | (503) | (2,057) | (3,533) | − | (20) | (6,113) |
| Foreign currency translation differences | 2,918 | 566 | 1,250 | 46 | 942 | 5,723 |
| Balance as of March 31, 2018 | $449,355 | $164,477 | $135,484 | $65,322 | $29,978 | $844,617 |

B. Accumulated Depreciation and Impairment Losses

Millions of yen

| | Buildings and structures | Machinery, equipment and vehicles | Tools, fixtures and fittings | Land | Construction in progress | Total |
|---|---|---|---|---|---|---|
| Balance as of April 1, 2016 | ¥(32,666) | ¥(12,098) | ¥(10,909) | ¥ー | ¥(31) | ¥(55,703) |
| Depreciation | (1,111) | (582) | (829) | ー | ー | (2,523) |
| Impairment losses | (14) | (55) | (54) | ー | (328) | (452) |
| Disposals | 256 | 337 | 343 | ー | 307 | 1,243 |
| Foreign currency translation differences | 165 | 115 | 96 | ー | (0) | 375 |
| Others | ー | ー | (27) | ー | 27 | ー |
| Balance as of March 31, 2017 | ¥(33,370) | ¥(12,283) | ¥(11,380) | ¥ー | ¥(26) | ¥(57,059) |
| Depreciation | (1,210) | (884) | (933) | ー | ー | (3,028) |
| Impairment losses | (5) | (14) | (24) | ー | (3) | (47) |
| Disposals | 48 | 194 | 339 | ー | ー | 580 |
| Foreign currency translation differences | (196) | (175) | (98) | ー | (4) | (472) |
| Others | ー | ー | (10) | ー | 10 | ー |
| Balance as of March 31, 2018 | ¥(34,733) | ¥(13,162) | ¥(12,106) | ¥ー | ¥(24) | ¥(60,026) |

Thousands of U.S. dollars

| | Buildings and structures | Machinery, equipment and vehicles | Tools, fixtures and fittings | Land | Construction in progress | Total |
|---|---|---|---|---|---|---|
| Balance as of March 31, 2017 | $(314,101) | $(115,615) | $(107,114) | $ー | $(246) | $(537,076) |
| Depreciation | (11,393) | (8,325) | (8,783) | ー | ー | (28,501) |
| Impairment losses | (50) | (128) | (230) | ー | (32) | (440) |
| Disposals | 448 | 1,822 | 3,191 | ー | ー | 5,460 |
| Foreign currency translation differences | (1,838) | (1,643) | (920) | ー | (40) | (4,441) |
| Others | ー | ー | (91) | ー | 91 | ー |
| Balance as of March 31, 2018 | $(326,934) | $(123,890) | $(113,948) | $ー | $(227) | $(564,998) |

C. Carrying Amount

Millions of yen

| | Buildings and structures | Machinery, equipment and vehicles | Tools, fixtures and fittings | Land | Construction in progress | Total |
|---|---|---|---|---|---|---|
| As of April 1, 2016 | ¥13,206 | ¥2,572 | ¥2,198 | ¥6,939 | ¥3,076 | ¥27,991 |
| As of March 31, 2017 | 12,842 | 2,739 | 2,362 | 6,935 | 3,672 | 28,550 |
| As of March 31, 2018 | ¥13,006 | ¥4,312 | ¥2,288 | ¥6,940 | ¥3,161 | ¥29,706 |

Thousands of U.S. dollars

| | Buildings and structures | Machinery, equipment and vehicles | Tools, fixtures and fittings | Land | Construction in progress | Total |
|---|---|---|---|---|---|---|
| As of March 31, 2018 | $122,418 | $40,587 | $21,537 | $65,322 | $29,751 | $279,615 |

**2) Impairment Losses**

In the fiscal year ended March 31, 2018, the Santen Group recorded impairment losses of ¥47 million ($440 thousand)for that period, along with ¥452 million for the period ended March 31, 2017. Impairment losses are included in other expenses in the consolidated statement of profit or loss and other comprehensive income.

The major assets for which impairment losses were recognized for the year ended March 31, 2017 were mainly “Construction in progress.” The carrying amounts of these assets were written down to the recoverable amounts due to the decline in expected profitability. Those recoverable amounts were measured at the value in use.

The major assets for which impairment losses were recognized for the year ended March 31, 2018 were mainly “Tools, fixtures and fittings.” The carrying amounts of these assets were written down to the recoverable amounts due to the decline in expected profitability. Those recoverable amounts were measured at the value in use.

**3) Other Disclosures**

The Santen Group has contractual commitments for the acquisition of property, plant and equipment as of March 31, 2018 totaling ¥1,172 million ($11,030 thousand) and ¥487 million as of March 31, 2017.

## 16. Intangible Assets

### 1) Statements of Changes in Acquisition Cost, Accumulated Amortization and Accumulated Impairment Losses and the Carrying Amount by Category

A. Acquisition Cost

Millions of yen

| | Goodwill | Intangible assets associated with products | Software | Other | Total |
|---|---|---|---|---|---|
| Balance as of April 1, 2016 | ¥6,440 | ¥90,782 | ¥9,726 | ¥1,181 | ¥108,128 |
| Additions | — | 2,253 | 445 | 728 | 3,427 |
| Business combinations | 14,996 | 38,758 | — | 34 | 53,788 |
| Transfers | — | — | 904 | (904) | — |
| Disposals | — | (75) | (260) | (12) | (347) |
| Foreign currency translation differences | ¥1,334 | ¥4,030 | ¥(47) | ¥187 | ¥5,503 |
| Balance as of March 31, 2017 | 22,770 | 135,748 | 10,768 | 1,213 | 170,498 |
| Additions | — | 4,444 | 617 | 763 | 5,825 |
| Transfers | — | — | 477 | (477) | — |
| Disposals | — | — | (321) | (56) | (377) |
| Foreign currency translation differences | (474) | (1,562) | 17 | (108) | (2,128) |
| Balance as of March 31, 2018 | ¥22,295 | ¥138,630 | ¥11,558 | ¥1,335 | ¥173,819 |

Thousands of U.S. dollars

| | Goodwill | Intangible assets associated with products | Software | Other | Total |
|---|---|---|---|---|---|
| Balance as of March 31, 2017 | $214,323 | $1,277,744 | $101,352 | $11,420 | $1,604,839 |
| Additions | — | 41,834 | 5,812 | 7,185 | 54,832 |
| Transfers | — | — | 4,490 | (4,490) | — |
| Disposals | — | — | (3,021) | (525) | (3,547) |
| Foreign currency translation differences | (4,465) | (14,698) | 156 | (1,020) | (20,027) |
| Balance as of March 31, 2018 | $209,858 | $1,304,880 | $108,789 | $12,570 | $1,636,097 |

B. Accumulated Amortization and Accumulated Impairment Losses

Millions of yen

| | Goodwill | Intangible assets associated with products | Software | Other | Total |
|---|---|---|---|---|---|
| Balance as of April 1, 2016 | ¥— | ¥(16,452) | ¥(7,212) | ¥(784) | ¥(24,447) |
| Amortization | — | (6,412) | (941) | (5) | (7,358) |
| Impairment losses | — | — | (21) | (2) | (24) |
| Disposals | — | — | 257 | 5 | 262 |
| Foreign currency translation differences | — | (43) | 38 | 8 | 4 |
| Balance as of March 31, 2017 | — | (22,906) | (7,880) | (778) | (31,563) |
| Amortization | — | (6,740) | (1,123) | (5) | (7,868) |
| Impairment losses | — | (50) | (53) | — | (103) |
| Disposals | — | — | 299 | — | 299 |
| Foreign currency translation differences | — | (116) | (5) | 32 | (89) |
| Balance as of March 31, 2018 | ¥— | ¥(29,812) | ¥(8,761) | ¥(751) | ¥(39,324) |

Thousands of U.S. dollars

| | Goodwill | Intangible assets associated with products | Software | Other | Total |
|---|---|---|---|---|---|
| Balance as of March 31, 2017 | $— | $(215,605) | $(74,169) | $(7,322) | $(297,096) |
| Amortization | — | (63,438) | (10,570) | (44) | (74,063) |
| Impairment losses | — | (471) | (495) | — | (966) |
| Disposals | — | — | 2,818 | — | 2,818 |
| Foreign currency translation differences | — | (1,096) | (51) | 297 | (838) |
| Balance as of March 31, 2018 | $— | $(280,609) | $(82,467) | $(7,069) | $(370,145) |

C. Carrying Amount

Millions of yen

| | Goodwill | Intangible assets associated with products | Software | Other | Total |
|---|---|---|---|---|---|
| As of April 1, 2016 | ¥6,440 | ¥74,330 | ¥2,514 | ¥396 | ¥83,681 |
| As of March 31, 2017 | 22,770 | 112,842 | 2,888 | 435 | 138,935 |
| As of March 31, 2018 | ¥22,295 | ¥108,819 | ¥2,796 | ¥585 | ¥134,495 |

Thousands of U.S. dollars

| | Goodwill | Intangible assets associated with products | Software | Other | Total |
|---|---|---|---|---|---|
| As of March 31, 2018 | $209,858 | $1,024,271 | $26,321 | $5,502 | $1,265,952 |

Note: The table above has been retrospectively adjusted following the completion of the purchase price allocation for the acquisition of InnFocus, Inc.

**2) Impairment Losses**

In the fiscal year ended March 31, 2018, the Santen Group recorded impairment losses of ¥103 million ($966 thousand) for that period, along with ¥24 million for the period ended March 31, 2017. Impairment losses are recognized in other expenses in the consolidated statement of profit or loss and other comprehensive income.

The intangible assets for which impairment losses were recognized for the year ended March 31, 2017 were mainly "Software." The carrying amounts of these intangible assets were written down to the recoverable amounts due to the decline in expected profitability. Those recoverable amounts were measured at the value in use.

The intangible assets for which impairment losses were recognized for the year ended March 31, 2018 were mainly "Software" and "Intangible assets associated with products." The carrying amounts of these intangible assets were written down to the recoverable amounts due to the decline in expected profitability. Those recoverable amounts were measured at the value in use.

**3) Impairment Test for Goodwill**

In the fiscal year ended March 31, 2018, the Santen Group recorded goodwill of ¥22,295 million ($209,858 thousand) for that period, along with ¥22,770 million as of March 31, 2017. The goodwill was recognized as a result of the acquisitions of Santen S.A.S. and InnFocus, Inc.

Impairment testing of goodwill is performed annually. The recoverable amount in the impairment test for goodwill was measured using the market value of the share price of the Company. In the fiscal year ended March 31, 2018, the Santen Group did not recognize an impairment loss on goodwill, because the recoverable amount exceeded the carrying amount.

**4) Other Disclosures**

i. Amortization of intangible assets associated with products is recorded as amortization on intangible assets associated with products in the consolidated statement of profit or loss and other comprehensive income. Amortization associated with other intangible assets is included in cost of sales, selling, general and administrative expenses and research and development expenses in the consolidated statement of profit or loss and other comprehensive income.

ii. The Santen Group did not recognize any internally generated intangible assets as of March 31, 2018, and as of March 31 2017.

iii. Significant Intangible Assets

The significant intangible assets associated with products recognized in the consolidated statement of financial position were mainly composed of the patents, trademarks, domain names, and product marketing and distribution rights related to ophthalmology products acquired from Merck. The carrying amount of these intangible assets was ¥47,124 million ($443,560 thousand) as of March 31, 2018 and ¥50,740 million as of March 31, 2017. The remaining amortization period for these intangible assets is 7 to 13 years.

In addition, the Santen Group recorded the rights associated with DE-128 that were recognized in conjunction with the acquisition of InnFocus, Inc., the rights associated with DE-076B (generic name: ciclosporin, development name: Cyclokat) that were recognized in conjunction with the acquisition of Santen S.A.S., and the rights associated with DE-109 (sirolimus) that were acquired by contract from U.S.-based MacuSight, Inc. as intangible assets associated with products. The carrying amounts of these intangible assets were ¥40,980 million ($385,728 thousand), ¥5,607 million ($52,773 thousand) and ¥6,982 ($65,720 thousand) million as of March 31, 2018, respectively, and ¥43,275 million, ¥5,824 million and ¥6,420 million as of March 31, 2017, respectively. The remaining amortization period of intangible assets associated with products for DE-076B was 8 years. DE-128 and DE-109 are not yet being amortized because these intangible assets are not yet available for use.

iv. Commitments

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Research and development milestones | ¥32,762 | ¥25,487 | $239,900 |
| Sales target milestones | 36,394 | 31,631 | 297,728 |
| Total | ¥69,156 | ¥57,118 | $537,627 |

The amounts shown in the table above represent the maximum payments to be made when all milestones are achieved, and they are undiscounted and not risk adjusted. Since the achievement of the conditions for payment is highly uncertain, it is unlikely that they will all fall due and the amounts of the actual payments may vary considerably from those stated in the table.

## 17. Financial Assets (Non-current) and Other Financial Assets (Current)

### 1) Components

A. Non-current Assets

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Financial assets measured at amortized cost | | | |
| Other | ¥1,189 | ¥977 | $9,195 |
| Financial assets measured at fair value through other comprehensive income | | | |
| Stock | 28,615 | 34,713 | 326,738 |
| Financial assets measured at fair value through profit or loss | | | |
| Golf membership rights, etc. | 85 | 85 | 804 |
| Total | ¥29,889 | ¥35,775 | $336,736 |

B. Current Assets

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Financial assets measured at amortized cost | | | |
| Other | ¥333 | ¥472 | $4,446 |
| Total | ¥333 | ¥472 | $4,446 |

### 2) Financial Assets Measured at Fair Value through Other Comprehensive Income

Equities are held mainly for the purpose of strengthening business relationships with investees, and not for the purpose of obtaining gains through short-term trading. Accordingly, they are designated as financial assets measured at fair value through other comprehensive income.

A. Fair Value

The main components of financial assets measured at fair value through other comprehensive income and those fair values are as follows:

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| ONO PHARMACEUTICAL CO., LTD. | ¥11,951 | ¥17,083 | $160,793 |
| Eisai Co., Ltd. | 5,473 | 6,439 | 60,604 |
| Daiichi Sankyo Company, Ltd. | 3,949 | 3,703 | 34,851 |

B. Other

Dividend income related to financial assets measured at fair value through other comprehensive income held by the Company was ¥530 million ($4,988 thousand) as of March 31, 2018 and ¥411 million as of March 31, 2017.

Financial assets measured at fair value through other comprehensive income that were disposed of during the fiscal years ended March 31, 2018 and 2017 were as follows:

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Fair value at date of sale | ¥1,364 | ¥2,879 | $27,103 |
| Cumulative gains (losses) | 318 | 1,406 | 13,230 |
| Dividend income | 272 | 68 | 640 |

Notes:

1. These financial assets were sold for the purpose of liquidating certain assets held. Cumulative gains (net of tax) of ¥973 million ($9,161 thousand) in the fiscal year ended March 31, 2018 and ¥220 million in the fiscal year ended March 31, 2017 were reclassified from other components of equity to retained earnings.
2. Due to the acquisitions during the fiscal year ended March 31, 2017, financial instruments measured at fair value through other comprehensive income of ¥3,112 million were reclassified from financial assets to shares of subsidiaries. Cumulative gains of ¥2,161 million, net of tax, due to the reclassification in the fiscal year ended March 31, 2017 were reclassified from other components of equity to retained earnings. The fair value has been retrospectively adjusted following the completion of initial accounting procedures for business combinations, including the purchase price allocation for the acquisition of InnFocus, Inc.

## 18. Inventories

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Merchandise and finished goods | ¥23,205 | ¥25,160 | $236,818 |
| Work in process | 484 | 455 | 4,281 |
| Raw materials and supplies | 4,813 | 5,022 | 47,267 |
| Total | ¥28,502 | ¥30,636 | $288,366 |

## 19. Trade and Other Receivables

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Notes and accounts receivables | ¥68,829 | ¥76,318 | $718,354 |
| Allowance for doubtful receivables | (30) | (203) | (1,912) |
| Other | 2,171 | 2,539 | 23,902 |
| Total | ¥70,970 | ¥78,654 | $740,344 |

## 20. Equity and Other Equity Items

### 1) Share Capital and Treasury Shares

Stocks

| | 2017 | 2018 |
|---|---|---|
| Type of shares*1 | Ordinary shares | Ordinary shares |
| Number of authorized shares | 1,100,000,000 | 1,100,000,000 |
| Number of issued shares*2 | | |
| Beginning of year | 414,191,515 | 406,173,015 |
| Change during year*3 | (8,018,500) | 674,500 |
| End of year | 406,173,015 | 406,847,515 |
| Treasury shares | | |
| Beginning of year | 22,369 | 6,646 |
| Change during year*4 | (15,723) | 765 |
| End of year | 6,646 | 7,411 |

Notes:

1. The ordinary shares have no par value, and there are no restrictions on the rights of those shares.
2. The issued shares are fully paid.
3. The changes in the number of issued shares during the fiscal years were attributable to the issuance of new shares upon the exercise of subscription rights to shares and the cancellation of the treasury shares.
4. The change in the number of treasury shares during the fiscal year was due to the purchase of the shares(8,284,000 shares) and the cancellation of the shares(8,300,000 shares) based on the resolutions made by the Board of Directors on September 12, 2016 and December 14, 2016, respectively, and the fulfillment of the request to additionally purchase and sell such shares.

### 2) Capital Surplus

Capital surplus consists of additional paid-in capital not included in share capital upon the ordinary issuance of new shares and the issuance of new shares due to the exercise of subscription rights to shares, as well as other capital surplus.

### 3) Other Components of Equity

A. Remeasurements of Defined Benefit Plans

These are changes caused by remeasurements of defined benefit plans.

B. Net Gain or Loss on Financial Assets Measured at Fair Value through Other Comprehensive Income

This includes the cumulative amount of net changes in the fair value of financial assets measured at fair value through other comprehensive income until the recognition of the asset is cancelled or an impairment loss on the asset is booked.

C. Foreign Currency Translation Adjustments

These are exchange differences arising from the translation of the financial statements of foreign operations.

D. Subscription Rights to Shares

The Company has adopted a stock option plan based on subscription rights to shares. In accordance with rules set forth primarily by Article 361 and Article 238 of the Japanese Companies Act, the Company grants subscription rights to shares. The amount of subscription rights to shares recorded in other components of equity is based on the fair value thereof. In addition, the contractual conditions and other details of the subscription rights to shares are stated in Note 21 "Share-based Payments.”

### 4) Retained Earnings and Dividends

A. Retained Earnings

These are earnings recognized as profit or loss in or before the fiscal year ended March 31, 2018, and earnings reclassified from other comprehensive income.

B. Dividends

(i) Dividends paid

Year ended March 31, 2017

| Resolution date | Total dividends (Millions of yen) | Dividends per share (Yen) | Record date | Effective date |
|---|---|---|---|---|
| Annual General Meeting of Shareholders (June 24, 2016) | ¥5,384 | ¥13.00 | Mar. 31, 16 | Jun. 27, 16 |
| Board of Directors Meeting (November 2, 2016) | 5,366 | 13.00 | Sep. 30, 16 | Nov. 30, 16 |

Year ended March 31, 2018

| Resolution date | Total dividends (Millions of yen) | Total dividends (Thousands of U.S. dollars) | Dividends per share (Yen) | Dividends per share (U.S. dollars) | Record date | Effective date |
|---|---|---|---|---|---|---|
| Annual General Meeting of Shareholders (June 23, 2017) | ¥5,280 | $49,700 | ¥13.00 | $0.12 | Mar. 31, 17 | Jun. 26, 17 |
| Board of Directors Meeting (November 1, 2017) | 5,283 | 49,722 | 13.00 | $0.12 | Sep. 30, 17 | Nov. 30, 17 |

(ii). Dividends whose effective date is in the following fiscal year

Year ended March 31, 2017

| Resolution date | Total dividends (Millions of yen) | Dividends per share (Yen) | Record date | Effective date |
|---|---|---|---|---|
| Annual General Meeting of Shareholders (June 23, 2017) | ¥5,280 | ¥13.00 | Mar. 31, 17 | Jun. 26, 17 |

Year ended March 31, 2018

| Resolution date | Total dividends (Millions of yen) | Total dividends (Thousands of U.S. dollars) | Dividends per share (Yen) | Dividends per share (U.S. dollars) | Record date | Effective date |
|---|---|---|---|---|---|---|
| Annual General Meeting of Shareholders (June 26, 2018) | ¥5,289 | $49,783 | ¥13.00 | $0.12 | Mar. 31, 18 | Jun. 27, 18 |

## 21. Share-based Payments

**1) Contractual Conditions for Share Options**

A. Eligible Persons

Directors and Corporate Officers of the Company

B. Vesting Conditions

No provisions

C. Exercise Period for Share Options Granted

For 10 years from grant date

D. Settlement Method

Settled in shares

**2) Number and Weighted-average Exercise Price of Share Options**

| | 2017 | | 2018 | | |
|---|---|---|---|---|---|
| | Number of shares (Stocks) | Weighted average exercise price | Number of shares (stocks) | Weighted average exercise price | |
| | | (Yen) | | (Yen) | (U.S. dollars) |
| Balance at the beginning of the year | 2,311,800 | ¥503 | 2,113,300 | ¥461 | $4.34 |
| Granted | 120,500 | 1 | 141,100 | 1 | 0.01 |
| Exercised*1 | 281,500 | 600 | 674,500 | 610 | 5.74 |
| Expired | 37,500 | 543 | — | — | — |
| Balance at the end of the year | 2,113,300 | 461 | 1,579,900 | 356 | 3.35 |
| Balance of exercisable stock options, end of year | 1,678,500 | 580 | 1,176,500 | 478 | 4.50 |

Note: The weighted-average share price of stock options at the time of exercise was ¥1,748 ($16.45) in the fiscal year ended March 31, 2018 and ¥1,517 in the fiscal year ended March 31, 2017.

**3) Range and Weighted-average Remaining Contractual Life of Share Options at the Fiscal Year-End**

The exercise price of share options ranged from ¥1 ($0.01) to ¥663 ($6.24) as of March 31, 2018 and ¥1 to ¥663 as of March 31, 2017. The weighted-average remaining life was 5.3 years as of March 31, 2018 and 5.1 years as of March 31, 2017.

**4) Fair Value and Fair Value Measurement Method of Share Options Granted During the Year**

A. Measurement method

Black-Scholes model

B. Fair Value and Primary Base Assumptions and Measurement Method

| | 2017 | 2018 |
|---|---|---|
| Resolution date | August 2, 2016 | August 1, 2017 |
| Expected volatility*1 (%) | 29.4 | 30.0 |
| Option life (years) | 6.5 | 6.5 |
| Expected dividend yield (%) | 1.92 | 1.52 |
| Risk-free interest rate (%) | (0.205) | (0.105) |

| | Yen | | U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Fair value | ¥1,148.21 | ¥1,544.09 | $14.53 |
| Weighted-average share price | 1,302 | 1,706 | 16.06 |
| Exercise price | 1 | 1 | 0.01 |

Note: The expected volatility is estimated by calculating the volatility of the share price at the end of each month relative to the end of the previous month, and determining the annualized standard deviation of the volatility for the previous 6.5 years.

**5) Expenses Recognized in Consolidated Statement of Profit or Loss**

Expenses related to share-based payments were ¥218 million ($2,051 thousand) in the fiscal year ended March 31, 2018, and ¥138 million in the fiscal year ended March 31, 2017.

## 22. Financial Liabilities (Non-current) and Other Financial Liabilities (Current)

### 1) Components

A. Components of Non-current Liabilities

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Long-term loans payables (excluding the current portion of long-term loans payable) | ¥7,598 | ¥3,500 | $32,944 |
| Long-term accounts payable - other | 18,669 | 17,679 | 166,410 |
| Other | 21 | 64 | 607 |
| Total | ¥26,288 | ¥21,244 | $199,961 |

B. Components of Current Liabilities

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Current portion of long-term loans payable | ¥9,331 | ¥4,098 | $38,573 |
| Other payables | 6,208 | 7,268 | 68,411 |
| Other | 2,110 | 3,038 | 28,591 |
| Total | ¥17,649 | ¥14,404 | $135,576 |

## 23. Post-employment Benefits

### 1) Outline of Post-employment Benefit Plans

In order to provide for post-employment benefits for employees, the Company and its consolidated subsidiaries have adopted funded and unfunded defined benefit plans and defined contribution plans.

With defined benefit corporate pension plans (all constitute funded plans), a lump-sum payment and pension will be provided according to wage and service length. However, the Company and some of its consolidated subsidiaries have introduced cash balance plans to defined benefit corporate pension plans.

A retirement benefit trust has been set up for some defined benefit corporate pension plans. With post-employment lump-sum payment plans (unfunded, but some are funded as a result of setting up a retirement benefit trust), a lump-sum payment is provided as a post-employment benefit according to wage and service length.

**2) Defined Benefit Plans**

A. Net Defined Benefit Liabilities

Millions of yen

| | Defined benefit obligations | Fair value of plan assets | Net defined benefit liabilities |
|---|---|---|---|
| Balance as of April 1, 2016 | ¥20,394 | ¥(17,837) | ¥2,556 |
| Current service cost | 1,261 | – | 1,261 |
| Interest (income) expense | 79 | (70) | 8 |
| Remeasurements of the net defined benefit liabilities | | | |
| Return on plan assets excluding amounts included in interest income on plan assets | – | (273) | (273) |
| Actuarial gains and losses arising from changes in demographic assumptions | (6) | – | (6) |
| Actuarial gains and losses arising from changes in financial assumptions | (251) | – | (251) |
| Experience adjustments | 91 | – | 91 |
| Total remeasurements of the net defined benefit liabilities | (165) | (273) | (438) |
| Foreign currency translation differences | (55) | 25 | (30) |
| Employer contributions to plan | – | (974) | (974) |
| Benefits paid by plan | (822) | 339 | (483) |
| Other | 192 | (192) | – |
| Balance as of March 31, 2017 | ¥20,882 | ¥(18,982) | ¥1,900 |
| Current service cost | 1,290 | – | 1,290 |
| Interest (income) expense | 98 | (92) | 6 |
| Remeasurements of the net defined benefit liabilities | | | |
| Return on plan assets excluding amounts included in interest income on plan assets | – | (546) | (546) |
| Actuarial gains and losses arising from changes in demographic assumptions | (1) | – | (1) |
| Actuarial gains and losses arising from changes in financial assumptions | 148 | – | 148 |
| Experience adjustments | (25) | – | (25) |
| Total remeasurements of the net defined benefit liabilities | 122 | (546) | (424) |
| Foreign currency translation differences | 34 | (27) | 7 |
| Employer contributions to plan | – | (502) | (502) |
| Benefits paid by plan | (880) | 406 | (473) |
| Other | 179 | (179) | – |
| Balance as of March 31, 2018 | ¥21,725 | ¥(19,921) | ¥1,804 |

Thousands of U.S. dollars

| | Defined benefit obligations | Fair value of plan assets | Net defined benefit liabilities |
|---|---|---|---|
| Balance as of March 31, 2017 | $196,551 | $(178,667) | $17,884 |
| Current service cost | 12,143 | — | 12,143 |
| Interest (income) expense | 927 | (866) | 60 |
| Remeasurements of the net defined benefit liabilities | | | |
| Return on plan assets excluding amounts included in interest income on plan assets | — | (5,141) | (5,141) |
| Actuarial gains and losses arising from changes in demographic assumptions | (8) | — | (8) |
| Actuarial gains and losses arising from changes in financial assumptions | 1,393 | — | 1,393 |
| Experience adjustments | (238) | — | (238) |
| Total remeasurements of the net defined benefit liabilities | 1,147 | (5,141) | (3,994) |
| Foreign currency translation differences | 320 | (252) | 68 |
| Employer contributions to plan | — | (4,725) | (4,725) |
| Benefits paid by plan | (8,279) | 3,826 | (4,453) |
| Other | 1,680 | (1,680) | — |
| Balance as of March 31, 2018 | $204,490 | $(187,507) | $16,983 |

B. Components of Plan Assets

| | | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|---|
| | Presence of quoted market prices in active markets | 2017 | 2018 | 2018 |
| Equities | Yes | ¥5,505 | ¥4,663 | $43,896 |
| Bonds | Yes | 9,567 | 10,249 | 96,471 |
| General accounts of life insurance companies | No | 1,725 | 1,732 | 16,304 |
| Other | No | 2,184 | 3,276 | 30,837 |
| Total | | ¥18,982 | ¥19,921 | $187,507 |

Plan assets are invested with the aim of securing the required overall returns over the long term with an acceptable risk exposure, in order to ensure the payment of pensions and other benefits in the future. To achieve this goal, the Santen Group selects assets that are suitable for investment along with determining the optimal combination of assets for the future based on consideration of the expected rate of return, risk and other factors. In addition, the composition of the assets is revised as necessary.

C. Actuarial Assumptions

| | 2017 | 2018 |
|---|---|---|
| Discount rate (%) | 0.51 | 0.45 |

D. Sensitivity Analysis

A 0.5% change in significant actuarial assumption would affect the present value of defined benefit obligations by the amounts shown below:

| | Millions of yen | | | | Thousands of U.S. dollars | |
|---|---|---|---|---|---|---|
| | 2017 | | 2018 | | 2018 | |
| | 0.5% Increase | 0.5% Decrease | 0.5% Increase | 0.5% Decrease | 0.5% Increase | 0.5% Decrease |
| Discount rate (%) | (1,187) | 1,307 | (1,184) | 1,301 | (11,145) | 12,247 |

Note: In this analysis, the other variables are assumed to be fixed.

E. Impact of the Defined Benefit Plan on Future Cash Flows

The estimated contribution amount for the fiscal year ended March 31, 2018 was ¥502 million ($4,725 thousand).

The weighted-average duration of the defined benefit obligation for the fiscal year ended March 31, 2018 is 13.1 years (for the fiscal year ended March 31, 2017, 13.5 years).

**3) Defined Contribution Plan**

The amounts recorded as costs in connection with defined contribution plans were ¥1,105 ($10,400 thousand) million in the fiscal year ended March 31, 2018 and ¥943 million in the fiscal year ended March 31, 2017.

## 24. Provisions

### (1) Statements of Changes in Provisions

Millions of yen

| | Asset retirement obligations (Note A) | Provision for restructuring (Note B) | Provision for paid absence (Note C) | Other | Total | Breakdown on consolidated statement of financial position | |
|---|---|---|---|---|---|---|---|
| | | | | | | Non-current | Current |
| Balance as of April 1, 2017 | ¥232 | ¥659 | ¥1,154 | ¥752 | ¥2,797 | ¥1,426 | ¥1,372 |
| Additional provision made in the period | 2 | — | 780 | 779 | 1,560 | — | — |
| Amounts used during the period | 2 | — | 825 | 487 | 1,314 | — | — |
| Unused amounts reversed during the period | — | 2 | — | 282 | 283 | — | — |
| The increase during the period in the discounted amount arising from the passage of time | 3 | — | 2 | — | 5 | — | — |
| Foreign currency translation differences | — | 59 | 33 | 19 | 110 | — | — |
| Balance as of March 31, 2018 | ¥235 | ¥716 | ¥1,143 | ¥781 | ¥2,875 | ¥1,367 | ¥1,508 |

Thousands of U.S. dollars

| | Asset retirement obligations (Note A) | Provision for restructuring (Note B) | Provision for paid absence (Note C) | Other | Total | Breakdown on consolidated statement of financial position | |
|---|---|---|---|---|---|---|---|
| | | | | | | Non-current | Current |
| Balance as of April 1, 2017 | $2,182 | $6,201 | $10,863 | $7,083 | $26,330 | $13,419 | $12,910 |
| Additional provision made in the period | 19 | － | 7,339 | 7,329 | 14,686 | － | － |
| Amounts used during the period | 16 | － | 7,769 | 4,581 | 12,367 | － | － |
| Unused amounts reversed during the period | － | 16 | － | 2,652 | 2,668 | － | － |
| The increase during the period in the discounted amount arising from the passage of time | 28 | － | 15 | － | 43 | － | － |
| Foreign currency translation differences | － | 555 | 308 | 176 | 1,040 | － | － |
| Balance as of March 31, 2018 | $2,212 | $6,741 | $10,756 | $7,355 | $27,064 | $12,868 | $14,196 |

Note A

Asset retirement obligations are recorded to provide for the removal of hazardous substances from plant equipment and other facilities and the fulfillment of obligations to restore leased buildings and other facilities to their original state. To this end, the amount expected to be payable in the future is discounted according to the expected period of use based on estimates and other information obtained from construction contractors.

The Santen Group predicts that the timing of the outflow of economic benefits will primarily be after over one year has passed from each fiscal year-end,but the timing will be affected by future business plans.

Note B

The provision for restructuring provides for expenditures to be incurred in the course of implementing business restructuring measures. It is provided for in the estimated amount of the related expenses. Furthermore, the Santen Group predicts that the timing of the outflow of economic benefits will primarily be after over one year has passed from each fiscal year-end, but the timing will be affected by future business plans.

Note C

The provision for paid absence recognizes a liability for the unused portion of paid absence granted to employees based on the paid absence system. The Santen Group predicts that the timing of the outflow of economic benefits will primarily be after over one year has passed from each fiscal year-end.

**25. Trade and Other Payables**

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Trade accounts payable | ¥16,570 | ¥20,575 | $193,665 |
| Erectronically recorded monetary liabilities | 1,313 | 1,896 | 17,842 |
| Other payables | 6,054 | 7,272 | 68,452 |
| Total | ¥23,937 | ¥29,743 | $279,959 |

**26. Cash and Cash Equivalents**

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Cash on hand and balances with banks | ¥53,297 | ¥69,283 | $652,137 |
| Time deposits over three months | ― | ― | ― |
| Total cash and cash equivalents in consolidated statement of financial position | 53,297 | 69,283 | 652,137 |
| Bank overdrafts | (1,015) | ― | ― |
| Cash and cash equivalents in consolidated statement of cash flows | ¥52,282 | ¥69,283 | $652,137 |

**27. Payments for Acquisition of Subsidiary**

Each Major Classes of Assets Acquired and Liabilities Assumed of Companies That Became Newly Consolidated Subsidiary in the Year Ended March 31, 2017

Major classes of assets acquired and liabilities assumed due to the acquisition of share of InnFocus, Inc. and the related consideration transferred and payments made during the year ended March 31, 2017 were as follows:

| | Millions of yen |
|---|---|
| Intangible assets | ¥38,758 |
| Other non-current assets | 46 |
| Goodwill | 14,996 |
| Current assets | 2,586 |
| Deferred tax liabilities | (13,690) |
| Current liabilities | (111) |
| Other | 6 |
| Cost of shares | ¥42,592 |
| Fair value of the previously held equity interest | (4,071) |
| Contingent consideration | (16,903) |
| Other payables | (47) |
| Cash and cash equivalents | (2,507) |
| Net：Payments for acquisition of subsidiary | ¥19,064 |

The table above has been retrospectively adjusted following the completion of the purchase price allocation for the acquisition of InnFocus, Inc

### 28. Financial Instruments

#### 1) Capital Management

The Santen Group considers the equity attributable to owners of the company ratio and profit ratio to equity attributable to owners of the company to be important management indicators. The Group monitors these indicators closely, and conducts purchases of treasury stock on the market and new share issuances as necessary. In doing so, the Group aims to maintain the trust of investors, creditors, and the markets and sustain a strong capital base to support continued development of its business into the future.

#### 2) Classification of Financial Assets and Financial Liabilities

Financial assets and financial liabilities are classified as follows:

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Financial assets | | | |
| Financial assets measured at fair value through other comprehensive income | | | |
| Stock | ¥28,615 | ¥34,713 | $326,738 |
| Financial assets measured at fair value through profit or loss | | | |
| Golf membership rights, etc. | 85 | 85 | 804 |
| Financial assets measured at amortized cost | | | |
| Other financial assets | 1,521 | 1,449 | 13,641 |
| Trade and other receivables | 70,970 | 78,654 | 740,344 |
| Cash and cash equivalents | 53,297 | 69,283 | 652,137 |
| Total financial assets | ¥154,489 | ¥184,184 | $1,733,664 |
| Financial liabilities | | | |
| Financial liabilities measured at fair value through profit or loss | | | |
| Contingent consideration | 18,669 | 17,679 | 166,410 |
| Financial liabilities measured at amortized cost | | | |
| Other financial liabilities | 25,268 | 17,968 | 169,127 |
| Trade and other payables | 23,937 | 29,743 | 279,959 |
| Total financial liabilities | ¥67,875 | ¥65,390 | $615,495 |

**3) Outline of Financial Risk Management**

The risks arising from financial instruments held by the Santen Group are as follows:

**A. Credit Risk**

1) Outline

Credit risk is the risk of financial loss borne by the Santen Group if a customer or a counterparty to a financial instrument is unable to meet its contractual obligations. The main sources of credit risk are customer receivables and investments.

i. Trade and other receivables

The Santen Group performs due date and credit limit controls in accordance with its credit management rules and periodicallyassesses the financial reliability of each customer taking into account the customer's financial position and other factors.

The percentage of the Santen Group's business conducted with the top 10 wholesalers in Japan reached 65% of consolidated revenue in the fiscal year ended March 31, 2018, compared with 65% in the fiscal year ended March 31, 2017. If the Santen Group's wholesale partners experience bankruptcy leading to credit losses, its business performance might be adversely affected.

ii. Financial assets and other financial assets

The Santen Group purchases bonds issued only by issuers that have high credit ratings.

2) Credit exposure

The maximum amount of exposure to credit risks for financial assets is the carrying amount after considering impairment in the consolidated statement of financial position.

3) Aging analysis

The analysis of the aging of trade and other receivables that were not impaired as of the end of the reporting period is as follows:

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Not past due | ¥70,103 | ¥78,190 | $735,980 |
| Past due | | | |
| 30 days or less | 532 | 369 | 3,476 |
| Over 30 days but within 90 days | 101 | 126 | 1,184 |
| Over 90 days | 263 | 172 | 1,617 |
| Total past due | 897 | 667 | 6,276 |
| Allowance for doubtful receivables | (30) | (203) | (1,912) |
| Total trade and other receivables | ¥70,970 | 78,654 | $740,344 |

**B. Liquidity Risk**

1) Outline

Liquidity risk is the risk that the Santen Group will encounter difficulty in fulfilling obligations related to the financial liabilities it must settle using cash or other financial assets. The main sources of liquidity risk are trade payables and loans payable.

The Santen Group manages liquidity risk primarily by monitoring monthly cash flows.

2) Maturity analysis

The contractual maturities of financial liabilities are as follows.

Year ended March 31, 2017 (as of March 31, 2017)

Millions of yen

| | Carrying amount | Contractual cash flows | Within 1 year | Between 1 year and 2 years | Between 2 years and 3 years | Between 3 years and 4 years | Between 4 years and 5 years | Over 5 years |
|---|---|---|---|---|---|---|---|---|
| Trade and other payables | ¥23,937 | ¥23,937 | ¥23,937 | ¥— | ¥— | ¥— | ¥— | ¥— |
| Other financial liabilities | | | | | | | | |
| Loans payable | 16,929 | 16,964 | 9,355 | 4,105 | 503 | 3,001 | — | — |
| Other payables | 6,208 | 6,208 | 6,208 | — | — | — | — | — |
| Other | 2,131 | 2,131 | 2,111 | 11 | 4 | 4 | 1 | 1 |
| Total | ¥49,206 | ¥49,241 | ¥41,612 | ¥4,116 | ¥506 | ¥3,005 | ¥1 | ¥1 |

Note: The table above does not include contingent consideration arising from business combinations. Details on contingent consideration are disclosed in Note 33 "Business Combination."

Year ended March 31, 2018 (as of March 31, 2018)

Millions of yen

| | Carrying amount | Contractual cash flows | Within 1 year | Between 1 year and 2 years | Between 2 years and 3 years | Between 3 years and 4 years | Between 4 years and 5 years | Over 5 years |
|---|---|---|---|---|---|---|---|---|
| Trade and other payables | ¥29,743 | ¥29,743 | ¥29,743 | ¥— | ¥— | ¥— | ¥— | ¥— |
| Other financial liabilities | | | | | | | | |
| Loans payable | 7,598 | 7,609 | 4,105 | 503 | 3,001 | — | — | — |
| Other payables | 7,268 | 7,268 | 7,268 | — | — | — | — | — |
| Other | 3,102 | 3,102 | 3,038 | 59 | 3 | 1 | 1 | 0 |
| Total | ¥47,711 | ¥47,722 | ¥44,154 | ¥562 | ¥3,004 | ¥1 | ¥1 | ¥0 |

Thousands of U.S. dollars

| | Carrying amount | Contractual cash flows | Within 1 year | Between 1 year and 2 years | Between 2 years and 3 years | Between 3 years and 4 years | Between 4 years and 5 years | Over 5 years |
|---|---|---|---|---|---|---|---|---|
| Trade and other payables | $279,959 | $279,959 | $279,959 | $— | $— | $— | $— | $— |
| Other financial liabilities | | | | | | | | |
| Loans payable | 71,517 | 71,621 | 38,639 | 4,735 | 28,247 | — | — | — |
| Other payables | 68,411 | 68,411 | 68,411 | — | — | — | — | — |
| Other | 29,198 | 29,198 | 28,595 | 552 | 32 | 8 | 8 | 1 |
| Total | $449,086 | $449,187 | $415,604 | $5,287 | $28,279 | $8 | $8 | $1 |

Note: The table above does not include contingent consideration arising from the business combination. Details on contingent consideration are disclosed in Note 33 "Business Combination."

**C.Market Risk**

1) Outline

The risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises foreign currency risk, interest rate risk and other price risks.

The Santen Group responds to currency risk by adjusting the balance of outstanding foreign currency denominated financial assets and liabilities in the same currency.

With no floating interest rate financial instruments in its portfolio, the Santen Group has judged that it has no exposure to significant interest rate risk.

Other price risks primarily have an impact on stocks of companies with which the Company has business relationships. The Company periodically reviews the fair market values of these stocks and reports on them at the Company's Board of Directors meeting.

2) Foreign currency risk

i. Foreign currency risk exposure

The following is a summary of the quantitative currency risk exposure data provided to the Santen Group's management based on its risk management policy:

Thousand of each curency

| | 2017 | | 2018 | |
|---|---|---|---|---|
| | EURO | U.S. dollar | EURO | U.S. dollar |
| Trade and other receivables | €457 | $10,976 | €3,192 | $14,113 |
| Trade and other payables | (1,287) | (5,121) | (508) | (21,341) |
| Financial liabilities | — | (166,410) | — | (166,410) |
| Net exposure amount | €(829) | $(160,555) | €2,684 | $(173,638) |

ii. Sensitivity analysis of foreign currency risk

The tables below show the increase (decrease) in profit or loss for the year that would result from the yen's depreciation against the Euro or U.S. dollar at the rates indicated below at the fiscal year-end.

This analysis is based on foreign exchange rate variables that the Santen Group believes to be reasonably possible as of the fiscal year-end. The analysis assumes that all other variables (particularly interest rates) are held constant. It was conducted on the same basis as the analysis for the year ended March 31, 2017. The yen's appreciation at the same rate would have the opposite effect, in the same amount, on profit (loss) for the year.

This analysis does not include the effects of translating financial instruments denominated in the functional currency, as well as the income and expenses and assets and liabilities of foreign operations, into Japanese yen.

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| | Profit (loss) | Profit (loss) | Profit (loss) |
| EURO (5% appreciation) | ¥5 | ¥(18) | $(165) |
| U.S. dollar (5% appreciation) | 901 | 922 | 8,682 |

Note: The above negative amounts represent the negative impact on profit before tax in the event of a 5% appreciation in the Japanese yen.

**3) Fair Value of Financial Instruments**

A. Fair Value and Carrying Amount

The carrying amount and fair value of financial instruments are shown below. Financial instruments measured at fair value, and financial instruments whose carrying amounts and fair values are a reasonable approximation, are not included in the following table.

| | Millions of yen | | | | Thousands of U.S. dollars | |
|---|---|---|---|---|---|---|
| | 2017 | | 2018 | | 2018 | |
| | Carrying amount | Fair value | Carrying amount | Fair value | Carrying amount | Fair value |
| Loans payable | ¥16,929 | ¥16,856 | ¥7,598 | ¥7,552 | $71,517 | $71,082 |

Note: The fair value of loans payable is categorized as Level 2.

B. Approaches and Valuation Techniques Applied to Measure Fair Value

The valuation techniques for measuring the fair value of financial instruments are as follows:

i. Loans payable

Loans payable with floating interest rates have fair values that approximate their carrying amounts because market interest rates are reflected in a short period. The fair value of loans payable with fixed interest rates are measured by the total sum of the principal and interest discounted by the interest rates that would apply if similar borrowings were conducted anew.

ii. Contingent consideration

The fair value of contingent consideration arising from the business combination mainly comprises the milestone payment based on progress with the development of MicroShunt and sales performance. The fair value of this contingent consideration is calculated with consideration for the time value of money.

C. Fair Value Hierarchy

The following table is an analysis of financial instruments carried at fair value by valuation method.

The levels of the fair value hierarchy are defined as follows:

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities

Level 2: Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e., as a price) or indirectly (i.e., derived from price)

Level 3: Inputs for the asset or liability that are not based on observable market data (unobservable inputs)

The measurement of fair value is undertaken in accordance with the Santen Group's valuation policies and procedures. Fair value is measured using the valuation model that most appropriately reflects the individual characteristics, features and risks of the financial instruments.

Any significant transfers of the financial instruments between levels are evaluated at each period end.

Year ended March 31, 2017

| | Millions of yen | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| Assets | | | | |
| Financial assets measured at fair value through other comprehensive income | | | | |
| Stocks | ¥27,822 | ¥— | ¥793 | ¥28,615 |
| Financial assets measured at fair value through profit or loss | | | | |
| Golf membership rights, etc. | — | 20 | 66 | 85 |
| Liabilities | | | | |
| Financial liabilities measured at fair value through profit or loss | | | | |
| Contingent consideration | — | — | 18,669 | 18,669 |

Notes:

1. There were no significant transfers of financial instruments between Level1 and Level2.
2. The table above has been retrospectively adjusted following the completion of the purchase price allocation for the acquisition of InnFocus, Inc.

Year ended March 31, 2018

| | Millions of yen | | | | Thousands of U.S. dollars | | | |
|---|---|---|---|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total | Level 1 | Level 2 | Level 3 | Total |
| Assets | | | | | | | | |
| Financial assets measured at fair value through other comprehensive income | | | | | | | | |
| Stocks | ¥33,427 | ¥— | ¥1,285 | ¥34,713 | $314,638 | $— | $12,100 | $326,738 |
| Financial assets measured at fair value through profit or loss | | | | | | | | |
| Golf membership rights, etc. | — | 20 | 66 | 85 | — | 187 | 617 | 804 |
| Liabilities | | | | | | | | |
| Financial liabilities measured at fair value through profit or loss | | | | | | | | |
| Contingent consideration | — | — | 17,679 | 17,679 | — | — | 166,410 | 166,410 |

Note: There were no significant transfers of financial instruments between levels of the fair value hierarchy.

The change in carrying values associated with Level 3 financial instruments using significant unobservable inputs.

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Balance, beginning of year | ¥2,348 | ¥859 | $8,083 |
| Purchases | 359 | 539 | 5,073 |
| Other comprehensive income | 1,200 | (27) | (255) |
| Sales | (188) | — | — |
| Transfers from Level 3 | (2,858) | — | — |
| Other | (2) | (20) | (185) |
| Balance, end of year | ¥859 | ¥1,351 | $12,717 |

Notes:

1. Securities categorized into Level 3 are measured using the market values of comparable companies, valuation models based on net assets of investees, and other valuation approaches.
2. Transfers from Level 3 were made due to the listing of financial instruments held by the Company and the acquisition of a subsidiary.
3. The table above does not include contingent consideration arising from the business combination. Details on contingent consideration are disclosed in Note 33 "Business Combination."

## 29. Operating Leases

### (1) The Total of Future Minimum Lease Payments under Non-cancellable Operating Leases

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Not later than 1 year | ¥1,835 | ¥1,801 | $16,954 |
| Later than 1 year and not later than 5 years | 1,781 | 2,440 | 22,963 |
| Later than 5 years | 913 | 480 | 4,521 |
| Total | ¥4,529 | ¥4,721 | $44,438 |

### (2) Lease Payments Recognized as Expenses

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Lease payments | ¥2,387 | ¥2,337 | $21,995 |

**30. Subsidiaries**

**Structure of the Santen Group**

| Name | Location | Main business | Percentage of voting equity | |
|---|---|---|---|---|
| | | | 2017 | 2018 |
| Claire Co., Ltd. | Japan | Cleaning services | 100.0 | 100.0 |
| Santen Business Services Co., Ltd. | Japan | Indirect support services | 100.0 | 100.0 |
| Santen Eye Care Co., Ltd. | Japan | Manufacturing and sales of prescription pharmaceuticals | 100.0 | 100.0 |
| Santen Holdings U.S. Inc. | U.S.A. | Regional headquarters and management of North American subsidiaries | 100.0 | 100.0 |
| Santen Inc. | U.S.A. | Clinical development of prescription pharmaceuticals and related business development | 100.0<br>(100.0) | 100.0<br>(100.0) |
| Advanced Vision Science, Inc. | U.S.A. | Development, manufacturing and sales of medical devices | 100.0<br>(100.0) | 100.0<br>(100.0) |
| Phacor Inc. | U.S.A. | - | 100.0<br>(100.0) | 100.0<br>(100.0) |
| InnFocus, Inc. | U.S.A. | Development and manufacturing of glaucoma devices | 100.0 | 100.0 |
| Santen Ventures, Inc. | U.S.A. | Investment in startup companies | — | 100.0<br>(100.0) |
| Santen Holdings EU B.V. | Netherlands | Financing headquarters for EMEA business | 100.0 | 100.0 |
| Santen Oy | Finland | Manufacturing, sales, contract manufacturing, and clinical development of prescription pharmaceuticals | 100.0<br>(100.0) | 100.0<br>(100.0) |
| Santen S.A.S. | France | Clinical development and sales of prescription pharmaceuticals | 100.0<br>(100.0) | 100.0<br>(100.0) |
| Santen GmbH | Germany | Sales of prescription pharmaceuticals and related business development | 100.0<br>(100.0) | 100.0<br>(100.0) |
| SantenPharma AB | Sweden | Sales support for prescription pharmaceuticals | 100.0<br>(100.0) | 100.0<br>(100.0) |

| Name | Location | Main business | Percentage of voting equity | |
|---|---|---|---|---|
| | | | 2017 | 2018 |
| Santen SA | Switzerland | EMEA regional headquarters and management, and manufacturing and sales of prescription pharmaceuticals | 100.0<br>(100.0) | 100.0<br>(100.0) |
| Santen Italy S.r.l. | Italy | Sales of prescription pharmaceuticals | 100.0<br>(100.0) | 100.0<br>(100.0) |
| Santen UK Limited | UK | Sales of prescription pharmaceuticals | 100.0<br>(100.0) | 100.0<br>(100.0) |
| Santen Pharmaceutical Spain, S.L. | Spain | Sales of prescription pharmaceuticals | 100.0<br>(100.0) | 100.0<br>(100.0) |
| SANTEN LIMITED LIABILITY COMPANY | Russia | Sales support for prescription pharmaceuticals | 100.0<br>(100.0) | 100.0<br>(100.0) |
| Santen Pharmaceutical (China) Co., Ltd. | China | Manufacturing, sales and clinical development of prescription pharmaceuticals | 100.0 | 100.0 |
| Santen Pharmaceutical Sales and Marketing (Suzhou) Co., Ltd. | China | Sales of prescription pharmaceuticals | 100.0<br>(100.0) | 100.0<br>(100.0) |
| Chongqing Santen Kerui Pharmaceutical Co., Ltd. | China | Manufacturing and sales of prescription pharmaceuticals | 49.0<br>(49.0) | 49.0<br>(49.0) |
| Santen Pharmaceutical Korea Co., Ltd. | Korea | Sales and clinical development of prescription pharmaceuticals | 100.0 | 100.0 |
| Taiwan Santen Pharmaceutical Co., Ltd. | Taiwan | Sales of pharmaceuticals | 100.0 | 100.0 |
| Santen India Private Limited | India | Market research and clinical development of pharmaceuticals | 100.0<br>(0.1) | 100.0<br>(0.1) |
| Santen Pharmaceutical Asia Pte. Ltd. | Singapore | Regional headquarters and management of subsidiaries in the ASEAN region and manufacturing and sales of prescription pharmaceuticals | 100.0 | 100.0 |
| SANTEN (THAILAND) CO., LTD. | Thailand | Sales of prescription pharmaceuticals | 100.0<br>(100.0) | 100.0<br>(100.0) |
| SANTEN PHARMA MALAYSIA SDN. BHD. | Malaysia | Sales of prescription pharmaceuticals | 100.0<br>(100.0) | 100.0<br>(100.0) |

| Name | Location | Main business | Percentage of voting equity | |
|---|---|---|---|---|
| | | | 2017 | 2018 |
| SANTEN PHILIPPINES INC. | Philippines | Sales of prescription pharmaceuticals | 100.0 (100.0) | 100.0 (100.0) |
| SANTEN PHARMACEUTICAL (HONG KONG) LIMITED | China | Sales of prescription pharmaceuticals | 100.0 (100.0) | 100.0 (100.0) |

Notes:

1. Numbers included in parentheses at "Percentage of voting equity" represent the ratio of the equity through indirect ownership to the total voting equity.
2. The percentage of voting equity with Chongqing Santen Kerui Pharmaceutical Co., Ltd. represents the ratio of the contribution. Chongqing Santen Kerui Pharmaceutical Co., Ltd. became a consolidated subsidiary since Santen Pharmaceutical (China) Co., Ltd. has a majority of the voting rights.
3. Santen Ventures, Inc. has been newly established and included in the scope of consolidation from the fiscal year ended March 31, 2018.
4. Santen Switzerland SA changed its name to Santen SA in the fiscal year ended March 31, 2018.

## 31. Related Parties

### 1) Related Party Transactions

Year ended March 31, 2017 (April 1, 2016 to March 31, 2017)
There were no transactions to report.

Year ended March 31, 2018 (April 1, 2017 to March 31, 2018)
There were no transactions to report.

### 2) Compensation for Key Management Personnel

The key management personnel of the Company refers to all of its directors, including outside directors.

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Compensation | ¥179 | ¥156 | $1,466 |
| Share-based payments | 37 | 110 | 1,038 |
| Total | ¥216 | ¥266 | $2,504 |

## 32. Contingencies
### (1) Contingent Liabilities

A. Guarantees

The Company has provided guarantees to financial institutions covering employee loans.

These are not recognized as liabilities in the consolidated statement of financial position because the possibility of loss from contingent liabilities was remote.

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Employees (loan guarantees) | ¥30 | ¥23 | $213 |

## 33. Business Combination

1) Business Combination

For the year ended March 31, 2017

Acquisition of InnFocus, Inc.

A. Outline of the Buisiness Combinations

i. The name and a description of the acquiree

Company name: InnFocus, Inc.

Main business: Development and provision of next generation products for glaucoma surgey

ii. The primary reasons for the business combination

InnFocus, Inc. is developing the MicroShunt implant to lower and sustain intraocular pressure (IOP) for the treatment of primary open-angle glaucoma (mild to severe stage disease). The MicroShunt has shown significant and sustainable lowering of IOP when used alone or in combination with cataract surgery in clinical trials outside of the U.S. Late stage clinical studies are underway in the U.S. and Europe in advance of PMA (Pre-Market Approval) application to the U.S. Food and Drug Administration (FDA) planned in the near future. The MicroShunt has received CE Mark in Europe.

With this acquisition, the Company will strengthen its glaucoma pipeline and stay at the forefront of innovation in ophthalmology. This agreement is in line with the Company's long-term vision to become a "Specialized Pharmaceutical Company with a Global Presence." The Company is excited about the MicroShunt as a new and effective treatment option that should significantly improve patient outcomes.

iii. Acquisition date

August 19, 2016 (U.S. time)

iv. Acquisition method

The Company acquired all of the voting equity interests of InnFocus, Inc. for consideration in cash.

And it stated by contract of milestone payment based on the progress of development for the MicroShunt and sales performance.

v. The percentage of voting equity interests acquired

Percentage of voting equity owned before acquisition: 9.56%

Percentage of voting rights additionaly acquired : 90.44%

Percentage of voting equity after acquisition :100.00%

B. The Fair Values of Assets Acquired, Liabilities Assumed and Purchase Condideration Transferred as at the Date of the Acquistion

With regard to this business combination, the Santen Group had previously reported provisional amounts because the purchase price allocation had not been completed. However, the purchase price allocation was completed in the fiscal year ended March 31, 2018 The components of the fair values of assets acquired, liabilities assumed and purchase consideration transferred as at the date of the acquisition were as follows.

Millions of yen

| | Amounts |
|---|---|
| Intangible assets | ¥38,758 |
| Other non-current assets | 46 |
| Other current assets | 79 |
| Cash and cash equivalents | 2,507 |
| Deferred tax liabilities | (13,690) |
| Current liabilities | (111) |
| Other | 6 |
| Goodwill (note) | 14,996 |
| Total | ¥42,592 |
| Cash (including other payables) | 21,618 |
| Contingent consideration | 16,903 |
| Fair value of the held equity interest previously | 4,071 |
| Total consideration for transferred | ¥42,592 |

Note: The content of goodwill mainly resulted from a reasonable estimate of the expected future profitability. The goodwill can not be recorded as deductible for tax purposes.

In the fiscal year ended March 31, 2018, the Santen Group retrospectively adjusted the initial provisional amounts, following the completion of the purchase price allocation. As of the date of the acquisition, the main adjustments were increases of ¥38,758 million in intangible assets, ¥16,903 million in contingent consideration, and ¥13,690 million in deferred tax liabilities, along with a reduction of ¥6,386 million in goodwill.

In the consolidated statement of profit or loss and other comprehensive income for the fiscal year ended March 31, 2017, net profit for the year was reduced by ¥1,330 million, mainly due to exchange differences on contingent consideration.

In addition, the Santen Group retrospectively adjusted the consolidated statement of financial position as of March 31, 2017, following the completion of the above mentioned purchase price allocation. The main adjustments were increases of ¥43,275 million in intangible assets, ¥18,669 million in contingent consideration, and ¥15,366 million in deferred tax liabilities, along with a reduction of ¥7,147 million in goodwill.

Acquisiton-related costs are included in ¥562 million in "Selling, general and administrative expenses."

C. The Impact on the Companies' Business Results

Business results of InnFocus, Inc. for the post-acquisition period, which were recognized in the consolidated statement of profit or loss and other comprehensive income for the year ended March 31, 2017 were as follows

Millions of yen

| | |
|---|---|
| Revenue | ¥— |
| Profit before tax | (1,151) |

The impact on the Santen Groups' business results for the period ended March 31, 2017 of assuming the acquisition date had been as of the beginning of the annual reporting period was as follows (out of scope of audit).

| | Millions of yen |
|---|---|
| Revenue | ¥— |
| Profit before tax | (848) |

For the year ended March 31, 2018
There are no business conbination to report.

2) Contingent consideration

The fair value of contingent consideration arising from the business combination mainly comprises the milestone payment based on progress with the development of MicroShunt and sales performance. The estimated amount which the Company could be required to pay as contingent consideration is $409 million, without consideration for the time value of money.
The fair value hierarchy level of the contingent consideration is Level 3.
Of the changes in the fair values related to contingent consideration, the components based on changes in the time value of money are recorded as "Finance expenses," while the components based on changes in factors other than the time value of money are recorded as "Other income" or "Other expenses."

A. Changes

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| Opening balance | ¥— | ¥18,669 | $175,729 |
| Increase due to business combinations | 16,903 | — | — |
| Changes in fair value during the fiscal year (unrealized) | (197) | — | — |
| Settlement amount during the fiscal year | — | — | — |
| Exchange differences | 1,963 | (990) | (9,320) |
| Closing balance | ¥18,669 | ¥17,679 | $166,410 |

B. Scheduled payments by maturity

| | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|
| | 2017 | 2018 | 2018 |
| One year or less | ¥— | ¥1,730 | $16,279 |
| One to five years | 12,886 | 12,779 | 120,285 |
| More than five years | 8,726 | 5,477 | 51,551 |

C. Sensitivity analysis
If the significant assumptions that affect the fair value of contingent consideration were to change, the fair value of contingent consideration would be impacted as follows:

| | | Millions of yen | | Thousands of U.S. dollars |
|---|---|---|---|---|
| | | 2017 | 2018 | 2018 |
| Discount rate | 1.0% increase | ¥(812) | ¥(480) | $(4,522) |
| | 1.0% decrease | 710 | 577 | 5,426 |

## 34. Subsequent Events

Introducing a new stock-linked remuneration program

At a meeting of its Board of Directors held on May 9, 2018, the Company decided to introduce a new stock-linked remuneration program (the "Program"). Furthermore, the introduction of the Program was approved at the 106th annual general meeting of shareholders held on June 26, 2018.

**1) Purpose of the Program**

The purpose of the Program is to encourage the Company's Directors excluding Outside Directors (the "Target Directors"), to engage in realizing the Company's vision and strategy with vigor and to promote further sharing of value with shareholders from the perspective of enhancing the stock-linked remuneration program's functions and effectiveness by clarifying the message conveyed by the Program so that it contributes to the Company's continuous growth and improvement of corporate value on a medium-to long-term basis.

**2) Outline of the Program**

The Program consists of a "performance share unit system (performance-linked stock remuneration system)," a type of remuneration that is linked to the rate of achievement numerical targets during a certain performance evaluation period, and a "restricted stock-linked remuneration system," a stock-linked remuneration with transfer restrictions that are lifted by satisfying conditions, such as holding of the position of Target Director continuously for a certain period of time.

A. The "performance share unit system"

The "performance share unit system" is a performance-linked stock remuneration program in which numerical targets such as the Company's business performance are predetermined for the performance evaluation period, which consists of several consecutive fiscal years (decided by the Company between three and five years) of the Company's medium-term management plan and which pays the remuneration amount related to the number of Company shares issued according to the rate of achievement of the numerical targets and cash to secure funds for tax payment purposes as remuneration for the performance evaluation period.

We set the total amount of remuneration paid during the performance evaluation with period at equal to or less than 100 million yen per year multiplied by the number of years of each performance evaluation period, the upper limit of the number of shares provided at equal to or less than 100 thousand shares per year multiplied by the number of years of each performance evaluation period, and the total amount of cash for tax payment purposes paid during the performance evaluation period at equal to or less than 100 thousand shares per year multiplied by the number of years of each performance evaluation period, which is then multiplied by the share price at the time of issuance.

B. The "restricted stock-linked remuneration system,"

In the "restricted stock-linked remuneration system," Target Directors pay all of the monetary remuneration claims paid by the Company based on the Program as investment assets in kind and receive issuance or disposition of common shares of the Company. The issuance or disposition of the Company's common shares (the "Company Shares") pursuant to the "restricted stock-linked remuneration system" is conditional on the conclusion of a restricted stock allotment agreement that includes the details of (i)~(iii) below between the Company and the Target Director that is scheduled to be provided with the restricted stock-linked remuneration.

(i) No Company Shares may be transferred to a third party, pledged or otherwise disposed of in any manner whatsoever over a certain period.
(ii) The Company shall acquire the Company Shares without consideration if a certain event occurs.
(iii) The restriction on transfer shall be lifted at the time the restriction period expires on condition that the Target Director holds the position of Director, Corporate Officer, Corporate Auditor, employee or equivalent hereof continuously during the transfer restriction period. However, reasonable adjustments shall be made for resignations prior to the expiration of the transfer restriction period for justifiable reasons prescribed by the Company.

We set the total amount of remuneration paid in one fiscal year under the "restricted stock-linked remuneration system" at equal to or less than 100 million yen per year, and the upper limit of the number of shares provided at equal to or less than 100 thousand shares per year.

**3) Others**

The Company plans to introduce a performance share unit system and a restricted stock-linked remuneration system or another restricted stock unit system (for delivery of Company shares or other after a certain period of time) proposal to Corporate Officers in and outside Japan who do not concurrently serve as Directors of the Company.

After the Program is introduced, the previous stock options for stock-linked remuneration will be abolished and subscription rights to new shares will not be granted to Directors and Corporate Officers as stock options in the future.

Internal Control Report

**1 Framework of Internal Control Over Financial Reporting**

We, as Chairman and CEO of Santen Pharmaceutical Co., Ltd. (the Company) and CFO of the Company, are responsible for the design and operation of internal controls over financial reporting ("ICOFR") and for establishing and maintaining an ICOFR based on the framework of ICOFR in Japan in accordance with "On the Setting of the Standards and Practice Standards for Management Assessment and Audit concerning Internal Control Over Financial Reporting (Business Accounting Council (Council Opinions), February 15, 2007)."

Internal control aims at achieving the objectives to a reasonable extent with the organized and integrated function of individual component as a whole. Therefore ICOFR does not provide an absolute assurance for preventing and detecting all errors to consolidated financial statements.

**2 Assessment Scope, Timing and Procedures**

Basis of Presenting Internal Control Report

The report on ICOFR of the consolidated financial statements of the Company ("Internal Control Report") is prepared on the basis of generally accepted assessment standards of internal control over financial reporting in Japan ("Assessment Standards") and is compiled from the Internal Control Report prepared by the Company as required by the Financial Instruments and Exchange Law of Japan ("Law").

The Assessment Standards require management to assess ICOFR, which consists of the internal controls over the consolidated financial statements included in the Annual Securities Report filed under the Law and the internal control over disclosure information and others included in the Annual Securities Report that materially affects the reliability of the financial statements.

The scope of management's assessment of ICOFR in this annual report is different from the scope required by the Assessment Standards. Management assessment of ICOFR in this annual report covers the ICOFR with respect to the accompanying consolidated financial statements only. In addition, the accompanying consolidated financial statements are reclassified and modified from the consolidated financial statements prepared for the purpose of the Law. Supplementary information is also added to the consolidated financial statements. The process of making reclassifications and modifications and the addition of certain information is for the convenience of readers outside Japan. Management voluntarily includes the process in its assessment of ICOFR, even though it is outside the scope of the Assessment Standards.

Scope of Assessment

Management's assessment of ICOFR was conducted as of March 31, 2018 in accordance with the Assessment Standards.

In evaluating internal controls, management first assessed internal controls that have a material impact on overall consolidated financial reporting ("company-level controls") and, based on the results, selected business process to be assessed. For assessment of process level controls management analyzed the selected business processes, identified a key control that would have a material impact on the reliability of financial reporting, and assessed effectiveness of internal controls through assessing design and operation of the key controls.

Management assessed the effectiveness of the ICOFR applicable for the Company and its subsidiaries, to extent necessary in light of their degree of impact on the reliability of financial reporting. Management determined materiality for reliability of financial reporting in light of their degree of quantitative and qualitative impact on financial reporting. From the results of the company-level controls assessment of the Company and two subsidiaries, management determined a reasonable scope for process level controls to be assessed.

Management selected the Company as the significant business unit for assessing process level controls, as its revenue was more than 2/3 of the previous fiscal year's consolidated revenue. The process related to revenue, account receivables and inventories from the Company was selected for process level control assessment as they have significant relation to the business objectives of the Company. Apart from selected significant business units, including other business units, processes whose accounts were determined to have a high risk of misstatement and involves significant use of management estimate and projection, and processes whose businesses or operations included high risk transactions were additionally selected for controls assessment.

**3 Results of assessment**

Based on our assessment procedures noted above, we concluded the Company's internal control over financial reporting was effective as of March 31, 2018.

**4 Supplementary information**

No subsequent events have arisen that has caused to materially effect our evaluation of the effectiveness on the internal control over financial reporting as of March 31, 2018.

**5 Other**

Nothing to report.

Akira Kurokawa
Chairman & CEO

Kazuo Koshiji
CFO

August 3, 2018

# Independent Auditor's Report

To the Board of Directors of Santen Pharmaceutical Co., Ltd.:

We have audited the accompanying consolidated financial statements of Santen Pharmaceutical Co., Ltd. and its consolidated subsidiaries, which comprise the consolidated statement of profit or loss and other comprehensive income, statement of financial position, statement of changes in equity and statement of cash flows for the year then ended March 31, 2018 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 International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

**Auditor's Responsibility**

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, 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 Santen Pharmaceutical Co., Ltd. and its consolidated subsidiaries as at March 31, 2018, and their financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.

**Convenience Translation**

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended March 31, 2018 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 2 to the consolidated financial statements.

**Report on the Internal Control Report**

We also have audited the accompanying report on internal control over financial reporting of the consolidated financial statements of Santen Pharmaceutical Co., Ltd. as at March 31, 2018 (“Internal Control Report”).

**Management’s Responsibility for the Internal Control Report**

Management is responsible for the design and operation of internal control over financial reporting and the preparation and fair presentation of the internal control report in conformity with assessment standards for internal control over financial reporting generally accepted in Japan. Internal control over financial reporting may not completely prevent or detect financial statement misstatements.

**Auditor’s Responsibility**

Our responsibility is to express an opinion on the internal control report based on our internal control audit. We conducted our internal control audit in accordance with auditing standards for internal control over financial reporting 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 Internal Control Report is free from material misstatement.

An internal control audit involves performing procedures to obtain audit evidence about the assessment of internal control over financial reporting in the Internal Control Report. The procedures selected depend on the auditor’s judgement, including significance of effect on the reliability of financial reporting. Also, an internal control audit includes evaluating the appropriateness of the scope, procedures and result of the assessment determined and presented by management, and the overall internal control report presentation. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

**Opinion**

In our opinion, the Internal Control Report, in which Santen Pharmaceutical Co., Ltd. states that internal control over financial reporting was effective as at March 31, 2018, presents fairly, in all material respects, the assessment of internal control over financial reporting in conformity with assessment standards for internal control over financial reporting generally accepted in Japan.

KPMG AZSA LLC

August 3, 2018
Osaka, Japan