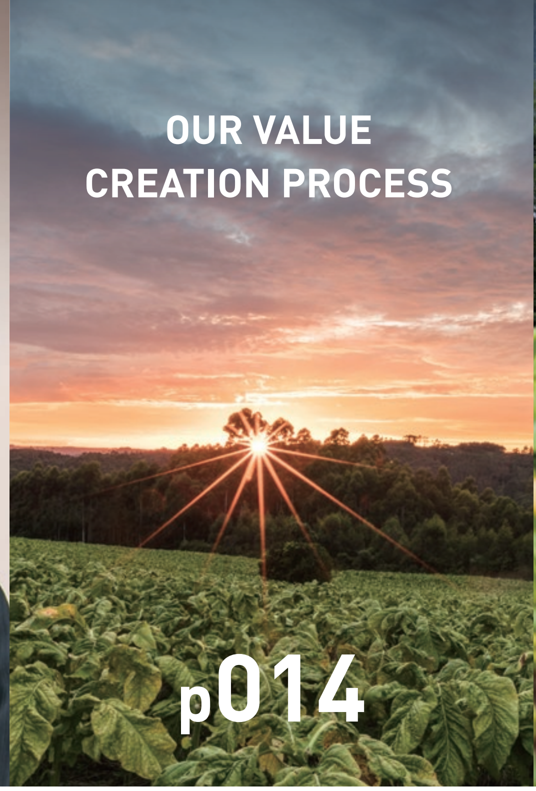
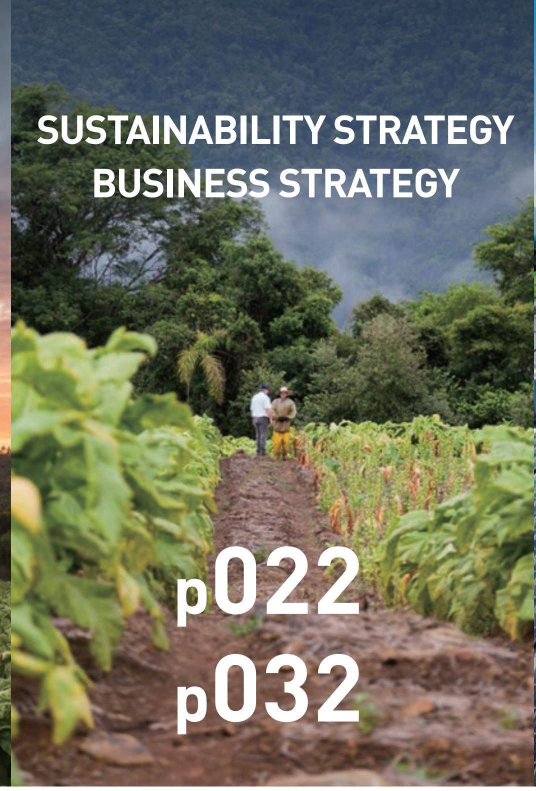
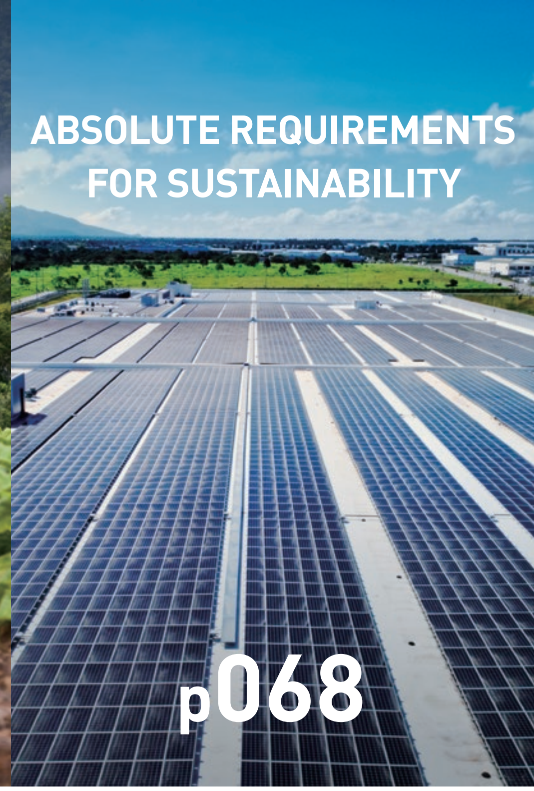
Japan Tobacco Inc.

Integrated Report 2019

Year ended December 31, 2019







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

Forward-looking statements

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

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

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

CORPORATE PROFILE

Foreword by the CEO

The JT Group is pleased to present its first Integrated Report to our stakeholders.

Our 4S model represents our commitment to serving our four stakeholder groups: our valued consumers, shareholders, employees and the wider society. We strive to fulfill our responsibilities towards our stakeholder groups by carefully considering their respective interests and exceeding their expectations wherever we can.

We are facing more volatile circumstances in our business environment, such as changes in consumer demands, the expansion of Reduced-Risk Products, stricter regulation on E-Vapor and tax increases in our markets. Not only do we need to take these circumstances into account, but must take into account how complex our society itself is becoming. These changes include more awareness on sustainability, innovation in IoT and connectivity, as well as changes in business models such as big data analysis and the subscription business model.

While we perceive these changes as clear opportunities, we must simultaneously be aware that timely adaptation is obligatory; otherwise, we may be eliminated from competition. In order for us to continue creating sustainable value, we understand it is crucial to provide a clearer, more convincing approach encompassing a broader, long-term perspective.

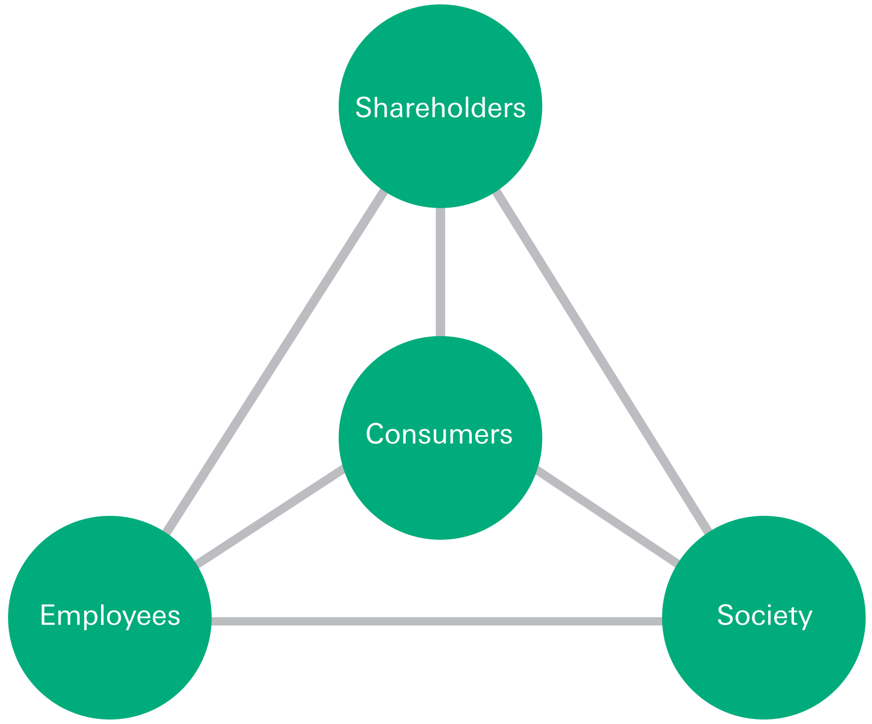
As tools to communicate with our stakeholders, we separately issued an Annual Report and a Sustainability Report until 2018. However, with increasing needs to communicate our business through a longer perspective with both financial and non-financial indicators, in 2019, we have decided to publish an Integrated Report. The JT Group is committed to transparency in providing our stakeholders with relevant information through this report. We trust that this report will help our stakeholders deepen their knowledge and understanding of our business.

M. Terabatake

Masamichi Terabatake
Representative Director and President, Chief Executive Officer

Our Management Principles: "The 4S model"

Our management principles pursue the 4S model. Under the 4S model, we strive to fulfill our responsibilities to our valued consumers, shareholders, employees and the wider society, carefully considering the respective interests of these four key stakeholder groups and exceeding their expectations wherever we can. We believe that pursuing this 4S model is the best approach to achieving sustainable profit growth over the mid- to long-term.



Editorial Policy

Period Covered
In principle, this report covers the period from January 1, 2019 to December 31, 2019, but also includes some information related to activities before and after this period.

Scope of Report
Japan Tobacco Inc. and consolidated subsidiaries

Published
March 2020

Referenced Guidelines
The International Integrated Reporting Council's "International Integrated Reporting Framework" was referred to in the writing of this report. In addition, the GRI Standards of the Global Reporting Initiative were referred to with regard to ESG information.

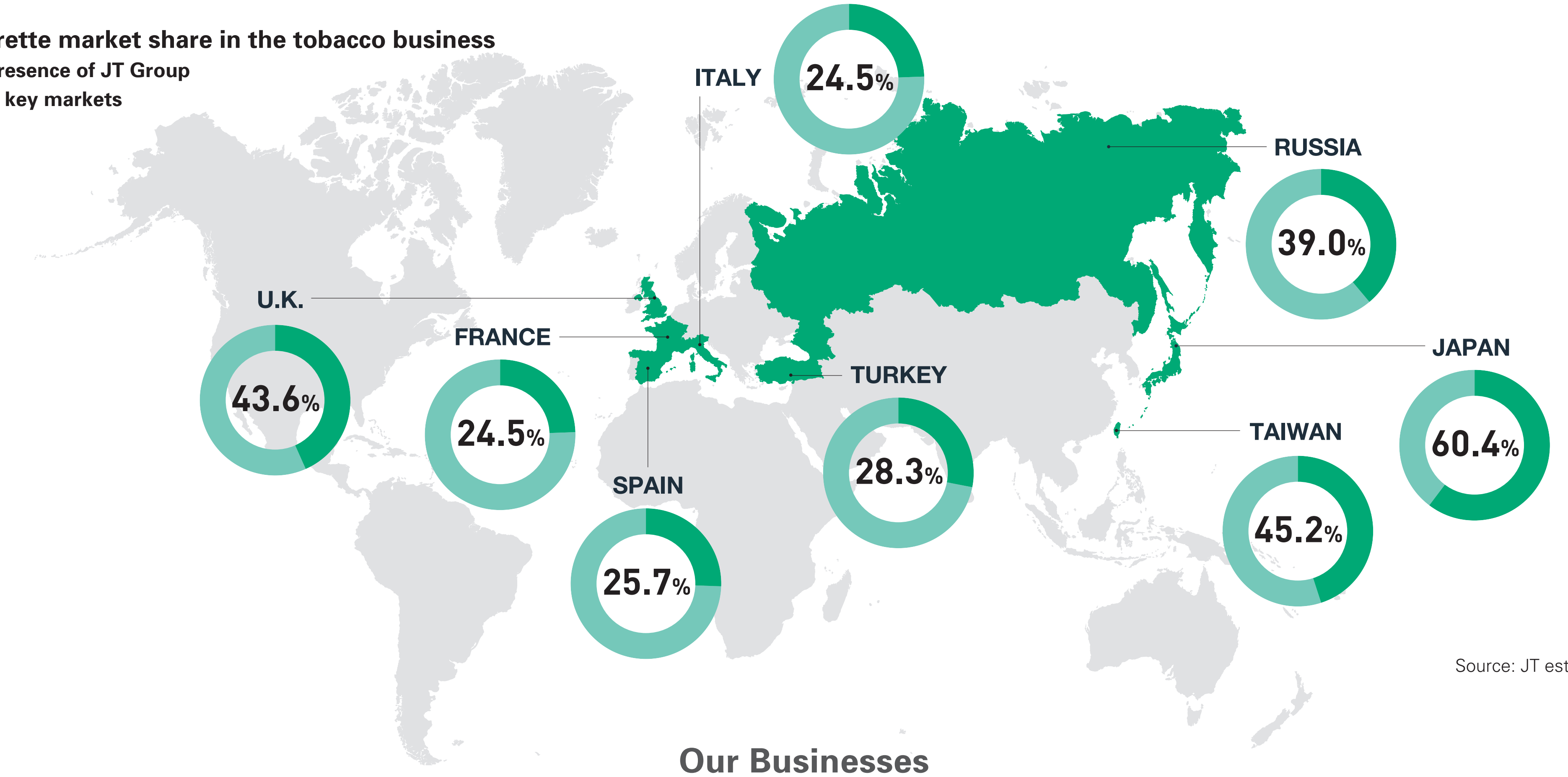
At a Glance

The JT Group is a leading global tobacco company operating in over 70 countries/regions. Our products are sold in over 130 countries/regions and our internationally recognized brands include Winston, Camel, MEVIUS and LD. Our pharmaceutical and processed food businesses complement the Group's profit growth and we are developing these businesses for sustainable growth. JT is listed on the Tokyo Stock Exchange. (JT ticker 2914)

Cigarette and Tobacco-Related Factories

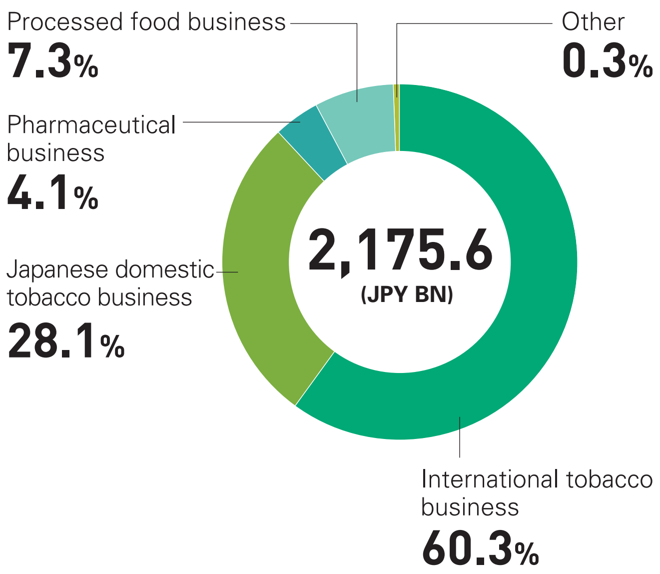
International	35
Japanese domestic	6
Total	**41**

Cigarette market share in the tobacco business
The presence of JT Group in our key markets

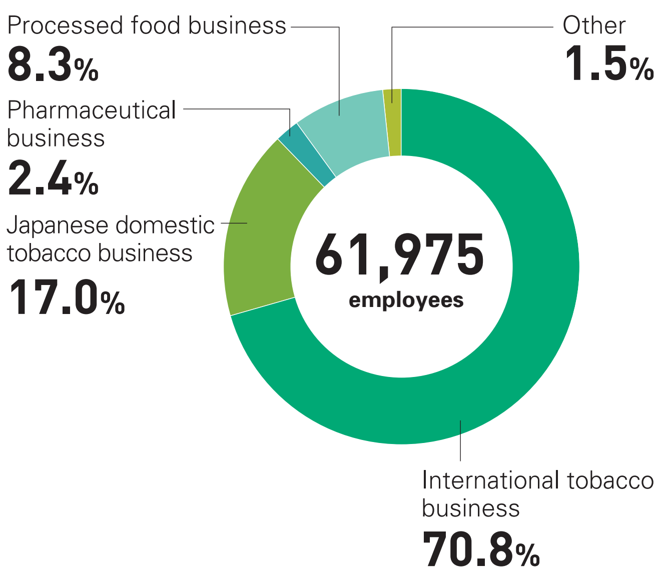


Source: JT estimate, IRI, Nielsen and Logista

Total Revenue
(2019)



Number of Employees
(As of December 31, 2019)



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

Our Businesses

International Tobacco Business

In the international tobacco business, we manufacture and offer conventional tobacco products, including cigarettes, cigars, pipe tobacco, smokeless tobacco, waterpipe tobacco and kretek as well as RRP.* Our key markets include France, Italy, Russia, Spain, Taiwan, Turkey and the U.K. Our international brand portfolio is very competitive and well-balanced, with strong equity brands across all relevant product categories and price segments. The portfolio includes leading brands in cigarettes and Fine Cut, such as Winston, Camel, MEVIUS and LD, as well as in RRP, such as Ploom and Logic.

Global Flagship Brands

Winston CAMEL MEVIUS LD

RRP Brands

ploom logic.

Japanese Domestic Tobacco Business

The Japanese domestic tobacco business is headquartered in Tokyo, and manufactures and offers products for Japan, one of the biggest tobacco markets in the world, where JT has established substantial presence with its leading position. Its strong product portfolio includes Ploom TECH, Ploom TECH+ and Ploom S in the RRP category and the key brands of MEVIUS, Seven Stars, Natural American Spirit, Winston and Camel in the cigarette category.

Key Brands

MEVIUS SevenStars NATURAL AMERICAN SPIRIT Winston CAMEL

RRP Brands

ploom

Pharmaceutical Business

The pharmaceutical business focuses on the R&D, manufacturing and sale of prescription drugs, concentrating on three specific therapeutic areas: metabolic diseases; autoimmune/inflammatory diseases; and viral infection.

Processed Food Business

The processed food business primarily engages in key product categories that include frozen noodles, packed cooked rice and frozen baked bread, seasonings and bakery.

Message from the CEO

Masamichi Terabatake

Representative Director and President, Chief Executive Officer

> To remain the preferred choice of consumers, shareholders, employees and the wider society, we will continuously work to exceed their expectations through sustainable profit growth.

Our Management Principles: The "4S model"

Our management principles pursue the 4S model. Under the 4S model, we strive to fulfill our responsibilities to our valued consumers, shareholders, employees and the wider society, carefully considering the respective interests of these four key stakeholder groups and continuously working to exceed their expectations. We believe that pursuing this 4S model is the best approach to achieving sustainable profit growth over the mid- to long-term and increasing our corporate value. Doing this conveys benefits to the four stakeholder groups.

Over the years, the JT Group has continued growing by proactively dealing with operational challenges and by transforming with a long-term perspective, notwithstanding significant changes in its business environment, such as the peaking-out of the Japanese domestic tobacco market and the tightening of regulations. To mention a just few successes, we have achieved business expansion abroad through the large-scale acquisitions of RJR Nabisco Inc.'s non-U.S. business and the entire Gallaher Group Plc (U.K.), rebranded MILD SEVEN as MEVIUS and pursued geographic expansion into emerging markets.

It goes without saying that the business environment surrounding the JT Group is not becoming any more predictable, not to mention the growth of the RRP category. We are at an inflection point, ready to transform again. I will strive to ensure the Group's sustainable profit growth with the ambition of being the first to offer new value to our consumers in RRP.

The 4S model, which forms our management principles, remains the cornerstone for all our decision-making processes and activities.

In order to remain the preferred choice of consumers, shareholders, employees and the wider society, we will strive to fulfill our responsibilities, exceeding expectations wherever we can, through our sustainable profit growth.

Business Plan 2020

Under our three-year Business Plan 2020* starting in 2020, we remain committed to pursuing sustainable profit growth over the mid- to long-term. We will continue aiming to achieve mid to high single digit annual average growth of adjusted operating profit at constant FX over the mid- to long-term. This indicator of business performance excludes foreign exchange impacts, temporary effects and extraordinary factors.

In 2019, while the Japanese domestic tobacco business encountered a challenging operating environment, the international tobacco business maintained its strong momentum. As a result, adjusted operating profit at constant FX increased year-on-year driven by the growth of the tobacco business as a whole. In addition, we have strengthened our foundations to ensure that each business can sustain profit growth into the foreseeable future.

The key to the successful implementation of Business Plan 2020 is profit growth in the tobacco business, which remains the core and main driver of the Group's profit growth. We will further grow the tobacco business as a whole by thinking proactively, acting with speed and with a consumer-centric mindset.

It is necessary that we have strong commitment from the top management and faster decision making by reducing decision-making layers. That is why starting this year, I am serving as the head of the tobacco business, where I will take the overall lead.

In the Japanese domestic tobacco business, it goes without saying that generating profits in a stable and sustainable manner is key to growing the tobacco business in the future. While we expect the situation to remain difficult in the short-term, we continue to aim for profit generation by strengthening the top-line in both the RRP and cigarette categories.

With respect to the international tobacco business, we intend to continue delivering strong profit growth. In existing markets, our efforts will focus on enhancing brand equity to gain further market share and seizing pricing opportunities. Regarding geographic expansion, investments will drive organic growth while we leverage M&A opportunities when appropriate. Overall, we will continue to strengthen our profitable business base. In the RRP market, we intend to expand our presence. Meanwhile, although both the pharmaceutical and processed food businesses will continue to face a challenging business environment, we aim to complement the Group's profit growth by continuing to implement our strategies.

* Every year we publish a three-year rolling business plan, reflecting the challenges identified in our operating environment, which presents continuously changing uncertainties, in order to strengthen our competitiveness with agility.

Our Resource Allocation Policy and Shareholder Return Policy

Our resource allocation policy is based on the 4S model and prioritizes business investment leading to sustainable profit growth. Furthermore, we continue to prioritize investments towards the growth of the tobacco business.

We aim to enhance shareholder returns, considering profit growth over the mid- to long-term while we continue to secure a solid financial base. We also continue to prioritize stable and sustainable dividend per share growth while considering adjusted operating profit at constant FX—our primary indicator—along with profit reflecting currency impacts to determine the dividend per share.

Under these policies, the proposed dividend in 2020 is 154 yen, set at the same amount as it was in 2019. We will focus on continuing to ensure the stability of the dividend going forward.

Sustainability Strategy

For our Group to grow sustainably, it is vital for us to contribute to the sustainable development of our society through our business activities. As sustainability is at the heart of our management, we have set out a Group-wide sustainability strategy. We have also formulated a sustainability strategy for each of our businesses, bearing in mind the unique challenges they face.

Three absolute requirements of our Group-wide sustainability strategy are "respect for human rights," "an improved social and environmental impact," and "good governance and business standards." These are the foundations for a sustainable business. For our tobacco business, our core business, we have set four focus areas: "products and services," "people," "supply chain," and "regulatory environment and illegal trade." For these four focus areas, we have also established 11 specific targets and initiatives. By working towards the targets and promoting the initiatives, we will be supporting the United Nations' Sustainable Development Goals (SDGs).

In 2019, for the first time, we reported to our stakeholders on our progress toward the 11 specific targets for our tobacco business. Our pharmaceutical and processed food businesses both finished setting out their respective focus areas and targets, so we now have a sustainability strategy for all of our business segments. Going forward, we will continue to engage with our stakeholders and make concerted efforts to ensure that we can all grow together to secure a sustainable future.

Please refer to business targets for more details.

This Integrated Report provides an opportunity to discuss and share with shareholders, consumers, business partners and other stakeholders the key areas of focus in my capacity as CEO of the JT Group, the initiatives currently underway, our strategic direction as well as my management approach and the experiences that guide this approach.

Sowing Seeds for the Future

In the last Annual Report, I shared my first impressions upon returning to Japan as the new JT Group CEO after serving as deputy CEO of JTI. My main takeaway was simple: I did not see an operation that showed overall optimization. Instead, I saw an organization that was too rigid and fragmented, with each division tending toward narrower perspectives and internal optimization.

As this situation was clearly sub-optimal, I announced several measures in 2019, my second year in office, to loosen up the rigidity of the organization and enable swift decision making by streamlining the decision-making processes, relocating the headquarters in Japan and rethinking the working environment. Even our international tobacco business had several inefficiencies so we are transforming it as well. Further, I am taking a stronger leadership role in the tobacco business myself. While the impact from these measures will need some time to be recognized across the organization and become visible from the outside, rest assured that the JT Group is changing.

My personal belief has always been that a successful organization must adopt a mid- to long-term perspective. Any decision we take should start from an objective assessment of the current environment against the end goal we have defined. From there on, it is all about executing the plans.

This conviction was strengthened during my years working as Deputy CEO of JTI. When I joined our international tobacco business in 2013, it already represented the largest profit contributor of the JT Group. The acquisitions of RJRI in 1999 and the Gallaher Group in 2007 had transformed the JT Group into a global tobacco manufacturer with steady profit growth and strong cigarette brands regularly outperforming competition in many markets. From the outside, it seemed as though the strategic and operating models were working perfectly. However, at that point, I thought that the international tobacco business became short-term result oriented. This was concerning from a mid- to long-term perspective, as we were not prepared to deal with any earnings slowdown from key markets.

It is not to say that the international tobacco business did not have a mid- to long-term perspective. Back in RJR days, the operations were more focused on maximizing the profits by reducing necessary investments; however, after we acquired the business and decided to increase marketing investments to enhance brand equity, the entire organization was able to move to a more mid- to long-term growth mindset. Furthermore, JT's management principles described in the 4S model had gradually permeated the organization of the international tobacco business, also leading to more mid- to long-term growth mindset.

Although the international tobacco business had a long-term perspective, usually when business is growing steadily, people tend to minimize the importance of thinking with a longer-term perspective. I realized we continued to leverage the same winning strategies but that our actions did not necessarily fully embed the mid- to long-term outlook.

With the management team, we decided it was critical for the international tobacco business to increase the focus on the mid- to long-term in order to realize sustainable growth for the future. As Deputy CEO, I made sure to re-ingrain this mindset into the organization and change the overall direction of management. I ensured that our business planning and operations kept up with that mid- to long-term perspective. Further, I encouraged and supported employees to put this into practice, wherever and whenever I could. For example, when the international tobacco business needed to focus on strengthening its foundation in order to ensure future sustainable performance, I liaised with the management team in Japan to revisit the aggressive profit growth targets for that year. In a way, I thought of this as an investment towards the mid- to long-term and worked to gain the understanding of the parent company, JT, while ensuring the efforts undertaken were generating the expected returns.

My role was to seed for the future and encourage a meaningful business transformation. The effects of measures put in place back then can still be felt today. For example, an important turning point was the establishment of the global RRP organization in 2014. Another was the deployment of new focused investments in emerging regions, notably in the Middle East and South East Asia, which we defined as "markets that matter" where, in line with projected economic progression, we expected strong returns over the mid- to long-term. This new investment approach has become a cornerstone of the international tobacco business's strategy.

Revitalizing the Consumer-Centric Mindset

In 2019, we announced the implementation of a transformation of our international tobacco business. Transformation was something that came up when I was still Deputy CEO of the international tobacco business, as the management team was thinking about the business requirements to further enhance our competitiveness. Further acknowledged was that the consumer-centric approach was required in the mid- to long-term. The geographical expansion of the business had progressed rapidly, through two major M&A transactions. However, this rapid growth did not allow for an effective review of the allocation of roles between corporate functions, regions, markets and factories. As a result, the organization gradually became bloated. It became clear a transformation was mandatory to remove bureaucracy and increase the speed of decision-making. The aim of the international tobacco business's ongoing transformation is to streamline the organization and related operations, in order to create a stronger and more dynamic business model that can operate consistently with a consumer-centric approach.

Tobacco products, historically our key focus, have a limited room for innovation, so we have been optimizing by making adjustments for each market, individually. However, as the RRP category expands further, there will be instances where the established operating models for tobacco may not be relied upon. RRP is still in its early stages and the platforms themselves are evolving quickly; that is not conducive to market-specific optimization. Also from an effective use of Group-wide resources, product development for RRP should be consolidated globally. For these efforts to succeed, it will be important to continue competing with an entrepreneurial mindset without being anchored to previous successes. For example, an increasing number of venture companies have been disrupting various industries with unique methods that major corporations were not able to catch up in a timely manner. RRP gives me the impression of being a very similar situation. We must increase our speed and explore new business opportunities with a greater sense of urgency. So, does our company have enough risk-taking capabilities and the appropriate expertise? Unfortunately, it is probably correct to say that we do not have enough capabilities yet and therefore we have not been able to fully exploit the opportunities provided by the operating environmental changes.

In the Japanese domestic tobacco business, the prevailing top-down approach has hindered our ability to continue outperforming the competition in a business environment like RRP, where rapid changes are unavoidable. To address this situation, we are currently engaged in a paradigm shift, moving from a headquarter-led business to one driven by the frontline. Growth in the RRP category has slowed in Japan, and competitors have been trying to secure a captive consumer base. We need to capture a share by tapping the competitors' consumer base. For that to happen, we have been striving to upgrade the existing products as well as develop next generation products. In this process, we remind ourselves that we aim to be the first to deliver new value to our consumers. For example, regarding the development of Ploom S, the first Heated Tobacco device launched in Japan by JT, in line with our ethos as a Japanese manufacturer, we prioritized safety over cost and undertook development after deliberately lowering the power output of the battery. Unfortunately, such value was not entirely understood and appreciated by consumers. This was most likely attributable to the fact that we did not fully focus on the consumer's expectations. I feel that this remains an area of improvement for us.

My aim as the head of the tobacco business is to streamline the decision-making process. I think we need to empower our employees more, with an intention to encourage endeavors in unknown fields and new initiatives that employees will find necessary from earnest engagement with consumers. And, to ensure we ourselves change swiftly, we especially need quick decision-making and commitment by the top management. I am more determined than ever that I should promote this transformation myself.

Embracing New Ways of Working and Empowering the Frontline

In the last two years, I have visited many of our Japanese and international sites. As I heard from the people on the frontlines, I gained a clear understanding of the challenges faced by the entire JT Group.

For example, I found that our colleagues on the frontlines, regardless of their departments or locations, had some interesting ideas, but these ideas did not translate into action. In such cases, sometimes it was because the headquarters did not support the ideas due to a conservative approach to avoid failures. Other times, the proposals from the frontlines simply did not reach appropriate decision-makers who could have supported them. There are numerous instances of communication breakdowns, which I think is one of our problems. I have found this problem as especially true for the current headquarters building in Tokyo, even before I became Group CEO. It seemed like each floor was divided into small segments, both fostering and reinforcing an internally fragmented departmental mindset. This created a bottleneck for information sharing and work process as well as cross-functional communications.

Keenly aware of the risk that rigidity and fragmentation could create, I mulled over a solution that could harness the power of the frontlines and turn this situation around. This led to the decision to relocate the headquarters in 2020. By physically changing the environment, we are changing the way people communicate at the workplace, and ultimately changing the way people collaborate. We planned the layout of the new headquarters to create an environment where people can freely consult and discuss with various departments by expanding the floor space and making the seating arrangement effective for collaboration and communication. By facilitating collaboration and communication between departments, we can foster decision-making to maximize the power of the frontlines and support front line initiatives.

In the Japanese domestic tobacco business, we regrettably made two downward revisions to our RRP sales volume assumptions in 2019. While increasing profit in the short-term is difficult, 2020 is the first year in which we can fully compete with a portfolio of low-temperature and high-temperature heating products. We need to build an organization that can win the competition in the RRP market, and I want to focus our efforts on finding that path to success. It is not the right time to spend our efforts on remedies like fundamental restructuring, which may be effective but could have strong side effects. I believe that we should focus on revitalizing the organization first, in order for the frontlines to challenge themselves, after thinking through the consumer expectations, and then maximize the impact of those initiatives. For example, we are currently working to reform the sales force mindset, given its close proximity to consumers, so that the insights gathered on the field can be translated into actions in a timely manner. In 2020, we introduced a new evaluation system to encourage such new mindset throughout the sales force. The new system evaluates taking up new challenges, which had no direct ties to evaluations previously. As a result, the system now evaluates and rewards employees who develop new ways to engage with consumers.

Entrusting and Encouraging Our Frontline Strength

My belief in the power of the frontlines is rooted in experiences from my initial international assignment after the acquisition of Manchester Tobacco in 1992 and RJRI in 1999. While those experiences were tough, they enabled me to rapidly understand the importance of effectively fueling the motivation of the frontlines.

During my term at Manchester Tobacco, there were times when I had to disregard interesting proposals put forward by colleagues on the frontline because of the specific directions provided by the headquarters in Tokyo. Partly due to lack of experience, this kind of response did not help motivate my colleagues. I truly felt that when an individual or a team is really empowered to do something, their commitment, awareness and business impact increase exponentially.

During the integration of RJRI, I built on this experience. The acquisition of RJRI was an investment of unprecedented scale for JT at the time and was a project with the Company's destiny on the line. The headquarters in Japan carefully monitored progress to the point that it seemed likely to fall into micromanagement, with people asking things like, "How is this part getting along?," "Shouldn't we use a Japanese company as the supplier?," and "Wouldn't it be better to use this kind of Japanese method?" This style made me think that if we forced Japanese methods and headquarters directives on the acquired company, who had their own locally cultivated experience and expertise, we would end up destroying the value of the company. Based on my experience with Manchester Tobacco, I had strong reservations about the micromanagement approach and worked desperately to persuade the JT headquarters to change their stance. Thankfully, the top management at the time took my concerns seriously. They fully understood the danger and offered support, telling those at the JT headquarters to trust the locals and leave it up to them. When directives that seemed unlikely to contribute to business growth came from the departments at headquarters, I didn't outright refuse them, but I took my time to lay out the case in a way my counterparts could agree with and then put that into action proactively. As a result, we were able to adopt the methods that the people on the frontline thought were best, and thus maximize their power; I think this helped make the integration process go very smoothly.

One of our greatest strengths is the diverse workforce we can rely on. During the integration with RJRI, we could not have succeeded in a smooth integration without this diverse workforce. The diversity has increased further to date, and, in terms of nationalities, we have people from more than 100 countries. The concept of diversity and inclusion really resonates with me; the company's sustainable growth is connected to respecting not just people's nationality, gender and age, but also their experience, expertise and other differences in backgrounds and values. However, if we compare the JT Group to tobacco competitors simply in terms of scale, we are around half the size of the top two companies individually. We must think about how to use our limited resources most effectively and dynamically. More recently, with the aim of building an organization that can compete globally and optimally allocate resources across the Group, we are consolidating the R&D, Corporate Strategy and Business Development functions of JT and JTI. To ensure that our diverse workforce can leverage these strengths without any friction, we will continue to focus on improving the working environment and training personnel.

The Value We Offer to Consumers

Originally, we defined the JT Group Mission as to create, develop and nurture our brands to meet consumers' needs while understanding and respecting the diversity present in society. Our value creation process reconfirms that providing consumers with value unique to the JT Group is critical to seize growth opportunities over the mid- to long-term and to create a positive impact on the Company and society.

Social environment has been changing substantially, and it is inevitable that we will reach unexpected inflection points in various aspects of business, not just in the RRP category. To ensure we continue to create value without being disrupted by such a change, we should return to our fundamentals, which work for all our business activities; engaging with consumers. We can then re-define the "value unique to the JT Group" we are trying to deliver to consumers. At the same time, we ask ourselves, "What is the unique value that the JT Group can provide for all the stakeholders in the 4S model?" and, "How can we evolve and enhance such value?" We will continue to pursue the answers, and I believe that this pursuit will lead us to our long-term vision.

Our consumer-centric approach, a sincere engagement with the consumers above all, has permeated the Group in the form of our action principles, most notably the 4S model. This should be the starting point for all our actions. Take the tobacco business, for example. In our increasingly stressful modern society, we need to think deeply about what we, as a manufacturer, can produce that provides consumers with a moment to unwind and a moment of pleasure. Similarly, in the pharmaceutical business, we are striving to create original and innovative drugs for patients around the world in the shortest time possible. In the processed food business, we seek to provide safe and delicious food for consumers, with the hope that they choose our products for their loved ones. In any business, we should put consumers first and focus on that. By doing so, I believe that the value we create will become more sustainable.

In this Integrated Report, we lay out our value creation process. By positioning this process at our foundation while consistently evolving it, we will continue to refine and enhance the value unique to the JT Group that we can offer to all our stakeholders.

VALUE CREATION

Our History

The JT Group has achieved sustainable growth by globalizing and diversifying its businesses through both organic growth and M&A.

1970s and earlier

Origins of the modern Japanese tobacco industry

Japan Tobacco and Salt Public Corporation, under the authority of the Ministry of Finance, lays the foundation of Japan's tobacco industry.

1949 Japan Tobacco and Salt Public Corporation is founded.

1957 HOPE (10) is launched as Japan's first domestically produced filter cigarette.

1969 Seven Stars is launched as Japan's first domestically produced charcoal filter cigarette.

1977 MILD SEVEN is launched.

1980s

Privatizing and creating the business foundation

The public corporation privatizes under the name Japan Tobacco Inc., founding the tobacco, processed food and pharmaceutical businesses, which persist to this day.

1985 Japan Tobacco Inc. is established.

1985 The Business Development Division is established to promote new businesses. The division is later reorganized into the food and pharmaceutical businesses.

1988 JT is introduced as the Company's public communication name.

1990s

Growing to become the third largest global tobacco company through M&A

By acquiring RJR Nabisco Inc.'s non-U.S. tobacco business, JT secures the third position in terms of sales volume.

1992 JT acquires Manchester Tobacco Company Ltd. (U.K.).

1993 The Central Pharmaceutical Research Institute is established.

1998 JT acquires a majority stake in Torii Pharmaceutical Co., Ltd.

1999 JT acquires RJR Nabisco Inc.'s non-U.S. tobacco business, taking over the global brands of Winston and Camel.

1999 JT acquires Asahi Kasei Corporation's food business, including Asahi Foods and seven other subsidiaries.

2000s

Strengthening our position as a global tobacco company by accelerating our global expansion

By acquiring Gallaher Group Plc, JT secures a new market platform and diverse brands, further expanding the international tobacco business.

2005 JT acquires CRES Neva Ltd. (Russia).

2006 JT acquires AD Duvanska Industrija Senta (Serbia).

2007 JT acquires Gallaher Group Plc (U.K.), taking over the global brands of LD, Benson & Hedges and more.

2008 JT acquires a majority stake in Katokichi Co., Ltd. (currently TableMark Co., Ltd.) and Fuji Foods Corporation.

2010s

Providing new value by addressing the dynamic and diversifying needs of our consumers

JT strengthens the international tobacco business through geographical expansion driven by M&A and starts providing a wide range of product choices, including RRP.

2013 MILD SEVEN is renamed MEVIUS in Japan.

2014 JT acquires e-cigarette company, Zandera Ltd. (U.K.).

2015 JT acquires e-cigarette company, Logic (U.S.).

2016 JT acquires Natural American Spirit's non-U.S. tobacco business from Reynolds American Inc. (U.S.).

2016 T-Vapor product Ploom TECH is launched.

2016–2018 JT conducts tobacco business acquisitions, notably in the Philippines, Indonesia, Russia and Bangladesh.

2019 T-Vapor products, Ploom TECH+ and Ploom S, are launched.

Consolidated net income (Billions of yen)

500.0
400.0
300.0
200.0
100.0
0

1949 Japan Tobacco and Salt Public Corporation

1985 Japan Tobacco Inc.

The Three Strengths Underpinned by Our History and Accomplishments

A solid financial base

- Sustainable profit growth backed by a combination of organic growth and M&A
- Ability to generate stable cash flows underpinned by profit growth

Superior brand equity

- High brand equity through continuous investment in MEVIUS, our leading brand in Japan, as well as in Winston, Camel, LD and other global brands acquired through M&A
- Strong R&D and innovative product development capabilities

A diverse workforce

- A corporate culture that respects diversity and leverages it into the value creation process
- A Group that maximizes the synergies generated from diversity

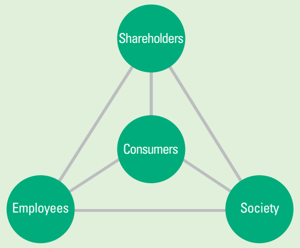
Our Value Creation Process

Our management principles pursue the 4S model. These principles guide our efforts to achieve our vision by enhancing corporate value and creating social value. We provide a wide range of products and services while leveraging our three strengths: a solid financial base, superior brand equity and a diverse workforce.

Our Management Principles

The 4S model

We strive to fulfill our responsibilities to our valued consumers, shareholders, employees and the wider society, carefully considering the respective interests of these four key stakeholder groups, continuously working to exceed their expectations.



Our Core Capital

Financial Capital

Sustainable profit growth and stable cash flows are backed by a combination of organic growth and M&A.

- Adjusted operating profit at constant FX .... **¥600.8 billion (+0.9% year-on-year change)**
- Total equity .... **¥2,743.6 billion**
- FCF .... **¥404.2 billion**

Intellectual Capital

Strong R&D Capabilities

We possess a diverse portfolio of competitive brands and robust brand equity rooted in our ability to deliver high-quality, innovative products.

- R&D expenditures .... **¥64.1 billion (Tobacco Science Research Center, Central Pharmaceutical Research Institute, etc.)**
- We own **three of the top 10 highest selling cigarette brands** in the world.

Human Capital

Our corporate culture respects diverse values and generates synergy from a diverse workforce.

- Number of employees **61,975**
- Employee nationalities .... **Over 100**
- Certified as a Top Employer in .... **63 locations**

Social and Relationship Capital

We have global business operations and a wide collaborative network spanning the value chain.

- Countries/regions where our products are sold .... **Over 130**
- Countries where we operate .... **Over 70**
- Directly contracted tobacco leaf growers and tobacco leaf merchants .... **Over 86,500**

Manufacturing Capital

Our optimal manufacturing system and facilities ensure superior quality and productivity supported by active capital investment.

- Capital expenditures .... **¥131.4 billion**
- Tobacco manufacturing bases .... **41 factories (29 countries)**
- Processed food manufacturing bases .... **31 factories (all factories have achieved FSSC 22000 certification)**

Natural Capital

The natural environment is vital to our sustainable growth.

- Stable climate conditions .... **Investment in renewable energy: Approx. US$21 million** (2016–2019)
- Abundant and quality water resources .... **10,448,035 m³ water** (2019) **intake volume; 95% of our factories have undergone water risk assessment**
- Healthy ecosystems for flora and fauna .... **Switch to renewable wood; Planted 7 million trees**

Our measures to reduce our environmental impact and the JT Group Environment Plan 2030 p72

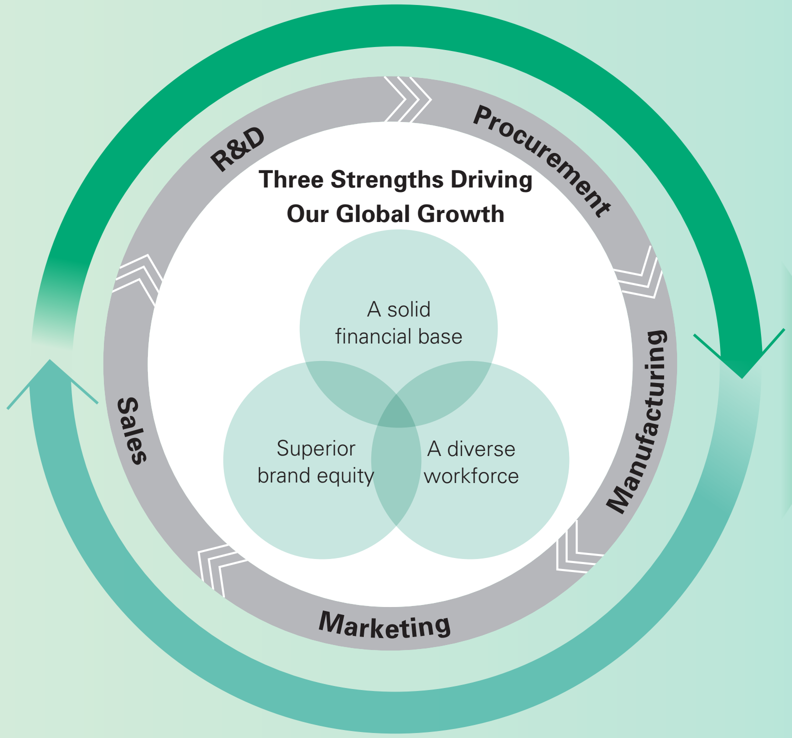
Our Business Activities and Growth Strategies

Business Strategy

Achieve quality top-line growth
Strengthen cost competitiveness
Enhance business foundation

Strategies by Segment

International Tobacco p42 Japanese Domestic Tobacco p46
Pharmaceuticals p50 Processed Food p52



Our Sustainability Strategy

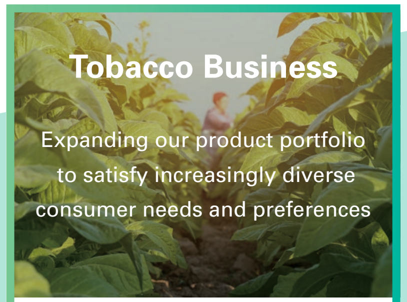
The JT Group's Three Absolute Requirements

Respect for human rights
An improved social and environmental impact
Good governance and business standards

Strategic Focus Areas for Sustainability

Tobacco p26 Pharmaceuticals p28 Processed Food p28

Our Products and Services



- **Cigarettes**
- **RRP**
  - **T-Vapor**
    - **Tobacco-Infused Vapor products**
    - **Heated Tobacco product**
  - **E-Vapor, etc.**

- **Three Key Therapeutic Areas**
  - **Metabolic diseases**
  - **Autoimmune/ inflammatory diseases**
  - **Viral infection**

- **Frozen and ambient foods**
- **Seasonings**
- **Bakery products**

The Value We Create

Corporate Value

Achieving consolidated profit targets

Mid to high single-digit annual average growth of adjusted operating profit at constant FX over the mid- to long-term

Enhancing shareholder returns in line with mid- to long-term profit growth

Social Value

Contributing to the sustainable development of society through our business activities

We contribute most significantly to the following nine SDGs by achieving specific targets in each business's focus areas, such as providing products and services that exceed consumer expectations, investing in our people and building a sustainable supply chain.

VISION

Continue to achieve global growth by providing diverse value unique to JT

Corporate governance and compliance support all of these processes p74

The external environment surrounding the JT Group p60

The Source of Our Competitiveness

Kiyohide Hirowatari
Executive Vice President

We will continue to sustainably create value by ensuring our business will leverage the three strengths that make global growth possible.

Overview of Our Core Strengths

Our vision is to achieve global growth by providing value unique to JT through pursuing the 4S model, which embodies its management principles.

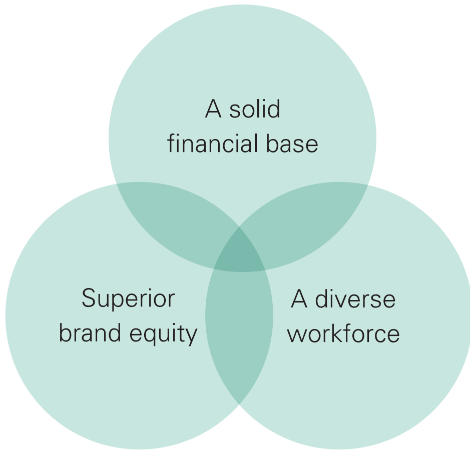
To realize this vision, we conduct business while leveraging the strengths we have cultivated throughout our history and through our accomplishments: a solid financial base, superior brand equity and a diverse workforce. These are also the source of our competitiveness. In addition, we create social value that contributes to the sustainable development of society and enhances our corporate value by offering various products and services to meet the needs of consumers and society.

Foundation of Our Strengths

The JT Group was established in 1985 upon the privatization of Japan Tobacco and Salt Public Corporation. Shortly thereafter, the Japanese market was opened to foreign tobacco manufacturers. Their aggressive actions, in addition to a tobacco tax hike, dramatically changed the operating environment. To top it off, the total demand for tobacco in Japan started to decline. The peak of demand was in the latter half of the 1990s, with a subsequent decline due to a fall in the adult population and an increase in health concerns associated with smoking. This created an increasingly severe business environment.

Perceiving these market changes as opportunities for growth, we strengthened our marketing capabilities and cost competitiveness in the Japanese domestic tobacco business; expanded our business portfolio by entering the pharmaceutical and processed food businesses; and worked to further expand globally. Through these efforts, we strove to reinforce our business foundation to ensure sustainable growth. Specifically, with the acquisition of RJR Nabisco Inc.'s non-U.S. tobacco business in 1999 and Gallaher Group Plc in 2007, we formed the foundation of our current overseas expansion and gained new market platforms; a wide variety of brands; and a diverse workforce that enabled the growth of these businesses. As a result, the international tobacco business became a profit growth driver alongside our Japanese domestic tobacco business, which had long been the core of profit generation. This enabled us to establish a financial foundation capable of generating stable cash flows.

Our Strengths



Our Strengths at Present

The JT Group currently sells products in over 130 countries/regions and continues to steadily grow as a global tobacco company.

Backed by our solid financial base, we proactively make business investments and focus on geographic expansion in emerging markets, while promoting RRP, which is our future-focused growth driver. In addition, our GFBs (Winston, Camel, MEVIUS and LD) and other superior brands make great contributions to our sustainable growth, while we continuously enhance their brand equity.

Furthermore, we are striving to maximize Group-wide management synergies by instilling a common philosophy of fully leveraging our diverse workforce, which represents over 100 different nationalities and promoting collaboration within this diverse workforce. We are keenly aware that all the Company's actions and achievements are born from our workforce. We are working to promote greater diversity, including in work styles and are strengthening our support for the development of each and every employee. For details, please refer to the next page.

Our Future Strengths

We are aware that due to global economic trends, foreign exchange rate risks and international geopolitical risks, there has been a steady increase in uncertainty surrounding our business environment.

To maintain our growth amid such a challenging environment, we must adapt to the various market trends and address our consumers' diversifying needs. We also need to reform our ways of thinking to effect change without being confined to our past successes. By fostering this mindset in each employee and supporting their ambitions, we will continue to accelerate our transformation into a company that initiates change and drives evolution. We regard this rapidly changing business environment as an opportunity for further growth. We will continue our sustainable value creation by managing our global business appropriately and with integrity, while better leveraging the three strengths we've cultivated to date.

Investing in People

Our sustainability journey is dependent on the skills and spirit of our employees and people in the communities impacted by our business. We will create positive impacts through our business.

The JT Group Human Resources Management Philosophy

We believe that highly skilled and talented people form the foundation of a company's success and contribute to real sustainable growth. In light of this, the JT Group proactively takes steps to secure long-term engagement and employee satisfaction.

Attracting and Developing Talent

Today's business environment is challenging and requires all of our employees to work together and acquire advanced skills. Various programs take place globally and locally and we constantly invest in our employees to ensure they flourish in their careers.

For example, in 2018 and 2019, our international tobacco business ran a customized leadership development program called "LIGHT UP" in partnership with INSEAD business school. A total of 32 employees from around the globe were selected to participate in this program.

Reflecting our commitment to talent development, we often recruit existing employees to fill open positions. In 2019, 93.7% of employees were internally promoted.

Another priority for us is ensuring that we are chosen by the best talent – particularly from Generation Z,* as this group represents a growing proportion of our new hires and their unique skills will help drive innovation in the JT Group.

Consequently, our international tobacco business launched the first global internship competition "Make It Bright" in 2019. The program reached nine million students globally and more than 5,000 registered. Finalists from 17 countries pitched their ideas for our business and the winning team from Ukraine will receive a six-month paid global internship in 2020.

* Representatives of Generation Z aged 18+, born between the mid-1990s and 2001.

Diversity and Inclusion

Establishing a diverse and inclusive workplace is a top priority for us, as we would like all of our employees to enjoy their work and the opportunities this brings to perform to the best of their abilities.

We also believe that diversity and inclusion create a rich mix of viewpoints and perspectives, which can inspire new ideas, offer solutions to complex issues and drive our business forward.

We welcomed a new Vice President of Diversity and Inclusion in February 2019 in our international tobacco business; and established a new strategy consisting of three pillars: Gender Equality, New Ways of Working and LGBT+ Inclusion. A Diversity and Inclusion Advisory Council at Board level in our international tobacco business demonstrates senior management's support for this inclusive and forward-looking approach. Senior leadership have taken a special training on identifying the obstacles preventing talented women from advancing their careers. Another project to address this was a reciprocal mentoring program that matched JTI top management with more junior employees (including women, men and LGBT+ employees). The aim was to enhance the top management's understanding of some of the challenges facing female employees, while providing the junior employees with a valuable career mentoring opportunity.

Other key initiatives and achievements in 2019:

- Workshops on LGBT+ Inclusion in Asia-Pacific and Europe with the Vice President of Diversity and Inclusion and various experts.
- Our international tobacco business introduced a new policy, allowing employees to work remotely four days a month.
- JT has been certified as a childcare-supporting company (in Japanese) by the Japanese Ministry of Health, Labor and Welfare and achieved the highest-ranking Gold status in the PRIDE index for the fourth consecutive year.

Employee Engagement

To evaluate the effectiveness of our programs, determine the level of employee engagement and identify areas for improvement, we carry out an Employee Engagement Survey every three years* across the Group.

Moreover, other surveys are conducted at a local or departmental level, so that we can always be mindful of employees' concerns and quickly implement relevant measures. For instance, in 2019, we introduced a new scheme in Japan, allowing departments to carry out surveys at any time. A variety of options are available under the new scheme, including a three-minute survey for gathering rapid feedback.

* Before 2019, our Japanese operations conducted the survey every year.

	Aspirational Goal	Target	Progress
Employer of Choice	We will be the employer of choice by investing in people.	We will be a certified employer of choice every year in at least 60 locations by focusing on talent management, rewards, and empowerment.	We were certified as a Top Employer in 63 locations, an increase of 5 locations from the prior year. We were also awarded with local certifications in 8 locations.

The JT Group Community Investment

We believe that we can contribute to the sustainable growth of societies by helping to make communities more inclusive and resilient.

	Aspirational Goal	Target	Progress
Community Investment	We will be the employer of choice by investing in people.	Between 2015 and 2030 we will invest US$600 million to help make communities inclusive and resilient, with our employees contributing 300,000 volunteering hours.	Between 2015 and 2019, we invested US$300 million in our communities and employees volunteered 119,349 hours on company time.

Learn more about our community investment activities on page 71.

Tobacco Business Sustainability Four Strategic Focus Areas

- Investing in People
- Exceeding Expectations with Products and Services - RRP
- Building Sustainable Supply Chains
- Regulatory Environment and Illegal Trade

Note: "Investing in People" is also a strategic focus area for our pharmaceutical and processed food businesses.

The JT Group Health and Safety

Our Approach

Our employees have the right to be protected from work-related injuries and illnesses, and it is our responsibility to provide a safe and healthy work environment. We align our health and safety standards with OHSAS 18001 and always meet or exceed legal requirements.

When our standards are stricter than local laws, we require our local offices to comply with our standards. The scope of our standards extends beyond our employees, covering contractors and visitors to our operations.

Three Pillars of Safety

Our safety programs are based on three fundamental pillars: safe workplaces, safety competence and a Group-wide culture where the safety of our people always comes first. The highest risks across the JT Group are driving vehicles, riding motorcycles and working with machinery, as well as slips, trips and falls.

To mitigate these risks and prevent injuries, we conduct risk assessments throughout the whole supply chain. This helps us to identify hazards, implement appropriate measures and protect our employees. We also focus on raising awareness among employees and thoroughly embedding our safety culture in our day-to-day operations.

In some countries where infrastructure is poor and traffic weakly regulated, our people are more at risk of being involved in road traffic accidents. Given the number of mergers and acquisitions in our international tobacco business, addressing this challenge is critical to protecting our employees, contractors and local communities and ensuring our business continuity.

We have been implementing a motorcycle safety program in countries with a high vehicle accident rate (Zambia, Malawi and Tanzania) since 2016, and we have since achieved a 50% reduction in work-related injuries. Furthermore, in 2019 we rolled out a new driver safety policy and implementation guidelines across our international tobacco business, requiring all local offices to conduct a risk assessment to identify high-risk drivers and to send periodic progress reports and action plans to our headquarters in Geneva. Given the growing number of female employees, the policy now also includes maternity protection. In the next three years, 30,000 employees will take a driver training course.

Towards a Better Workplace

We care deeply about employee well-being because we want our employees to feel motivated every day. We run a variety of well-being programs across the Group, such as ergonomic assessments and ensuring general occupational hygiene.

To design these programs, we gather well-being data from our local offices. In 2018, we expanded our data scope by introducing new rules requiring all local offices to report their occupational health cases to our headquarters. This will allow us to understand our global risks and develop a consistent approach to them while strengthening existing protection measures.

Local managers are responsible for investigating reported issues and identifying the causes. If the issues are attributed to the work or workplace, we take appropriate measures immediately to protect employees' well-being and prevent recurrences.

In Japan, we focus on mental health and preventing lifestyle-related diseases such as diabetes and we encourage employees to attend stress management sessions and individual consultations with doctors. These programs have had a positive impact on employee productivity and the absenteeism rate in Japan, which has recently been below 1%.

We are pleased to announce that JT was named as a "White 500" company for the fourth year running. This award is presented by Japan's Ministry of Economy, Trade and Industry. It recognizes large enterprises that are making outstanding progress towards better well-being among their employees.

Our Health and Safety Performance as a Group

		2015	2016	2017	2018	**2019**
No. of Fatalities	Employees	1	2	0	1	1
	Contractors	1	1 (only JTI)	2	0	0
Lost Time Injury Rate (per 200,000 working hours)	Employees	0.34	0.39	0.37	0.24	0.24
Occupational Illness Rate*1 (per million working hours)	Employees	0	0	0.08	0.02	0.01
Other Important KPIs						
% of Cigarette and Tobacco-Related Factories Certified to OHSAS 18001		78.9%	77.8%	74.4%	76.9%	79.5%
Number of Vehicle Accidents*2		1,122	1,151	66	85	71
Vehicle Accident Frequency Rate*2 (excludes property damage, accidents per million kilometers)		4.84	3.87	0.23	0.21	0.16

Notes: This year, we recalculated all the historical data. Concretely, we removed some data from newly acquired business considering the fact that newly acquired business needs 18 months to integrate the JT Group Health and Safety Standards.
We revised our KPIs this year and we no longer report the number of lost time incidents, and the lost time incidents rate.
We regret that one employee and two people in our communities died as a result of work accidents in 2019. We try to learn from every accident and remain committed to achieving zero fatalities.

*1 Data scope: 2015: only JT, 2016 and 2017: JT and Japanese domestic Group companies, from 2018: The entire JT Group. Learn more about our data scopes at JT.com.

*2 The numbers of vehicle accidents and the vehicle accident frequency rates in 2015 and 2016 contain property damages because the data is not available in our international tobacco business. The data in 2015 covers only our international tobacco business and from 2016, we cover JT and JTI.

Health and Safety Performance in Our Tobacco Business

	Aspirational Goal	Target	Progress
Zero Injuries	We will be the employer of choice by investing in people.	In line with our vision of zero workplace injuries, we will reduce injury rates by 25% by 2023 and 50% by 2030. (Baseline year: 2015).	Recordable injury rate* declined 31.2% from 0.72 in 2015 to 0.49 in 2019.

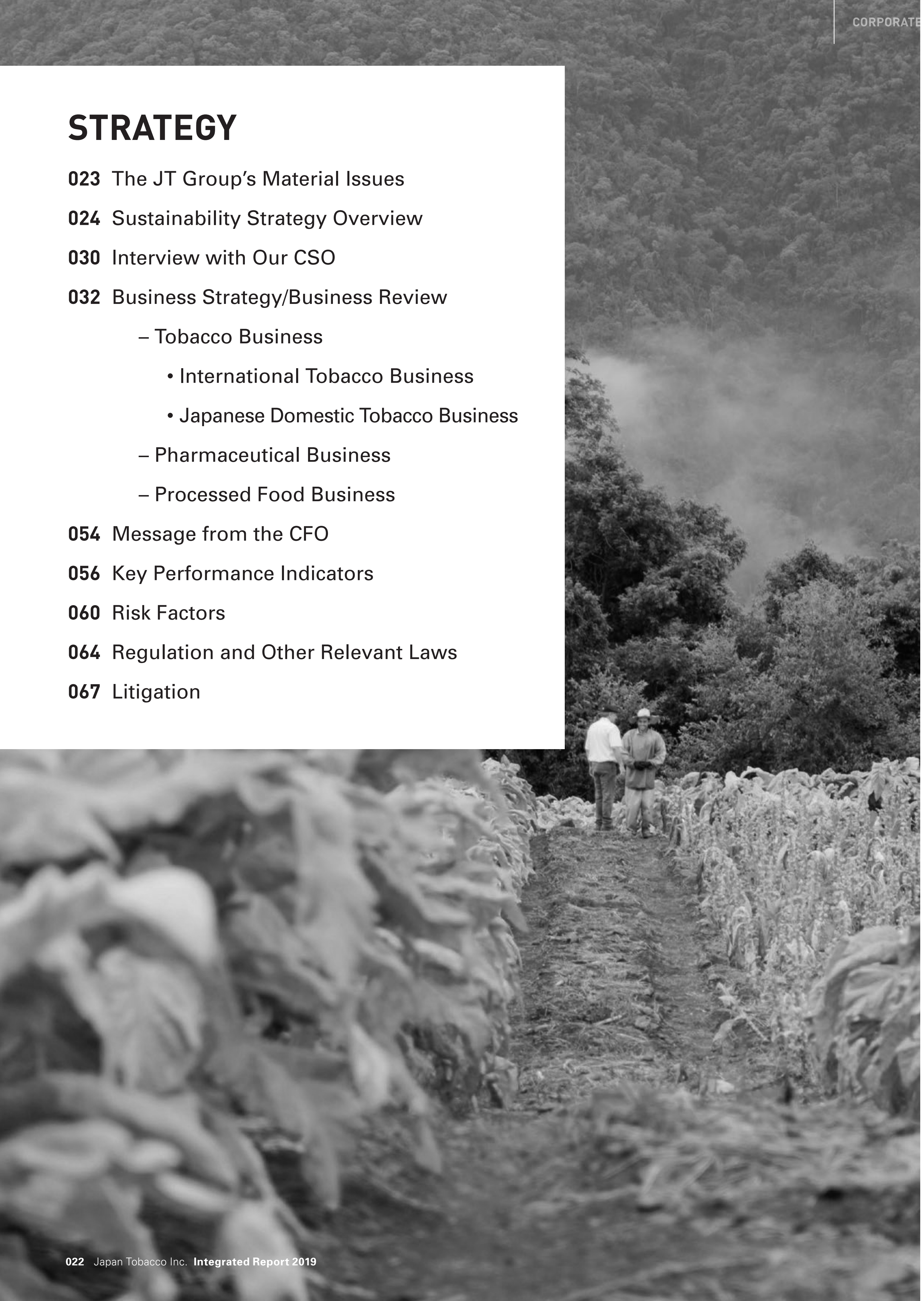
* Recordable injury rate = Recordable injuries/200,000 hours worked. Some data from newly acquired business have been excluded, as newly acquired business needs 18 months to integrate the JT Group Health and Safety Standards.

		2015	2016	2017	2018	**2019**
Recordable Injury Rate (per 200,000 working hours)	Employees	0.72	0.64	0.67	0.50	0.49

Learn more about our health and safety performance at JT.com.

Tobacco Business Sustainability Four Strategic Focus Areas
- Investing in People
- Exceeding Expectations with Products and Services - RRP
- Building Sustainable Supply Chains
- Regulatory Environment and Illegal Trade

Note: "Investing in People" is also a strategic focus area for our pharmaceutical and processed food businesses.



STRATEGY

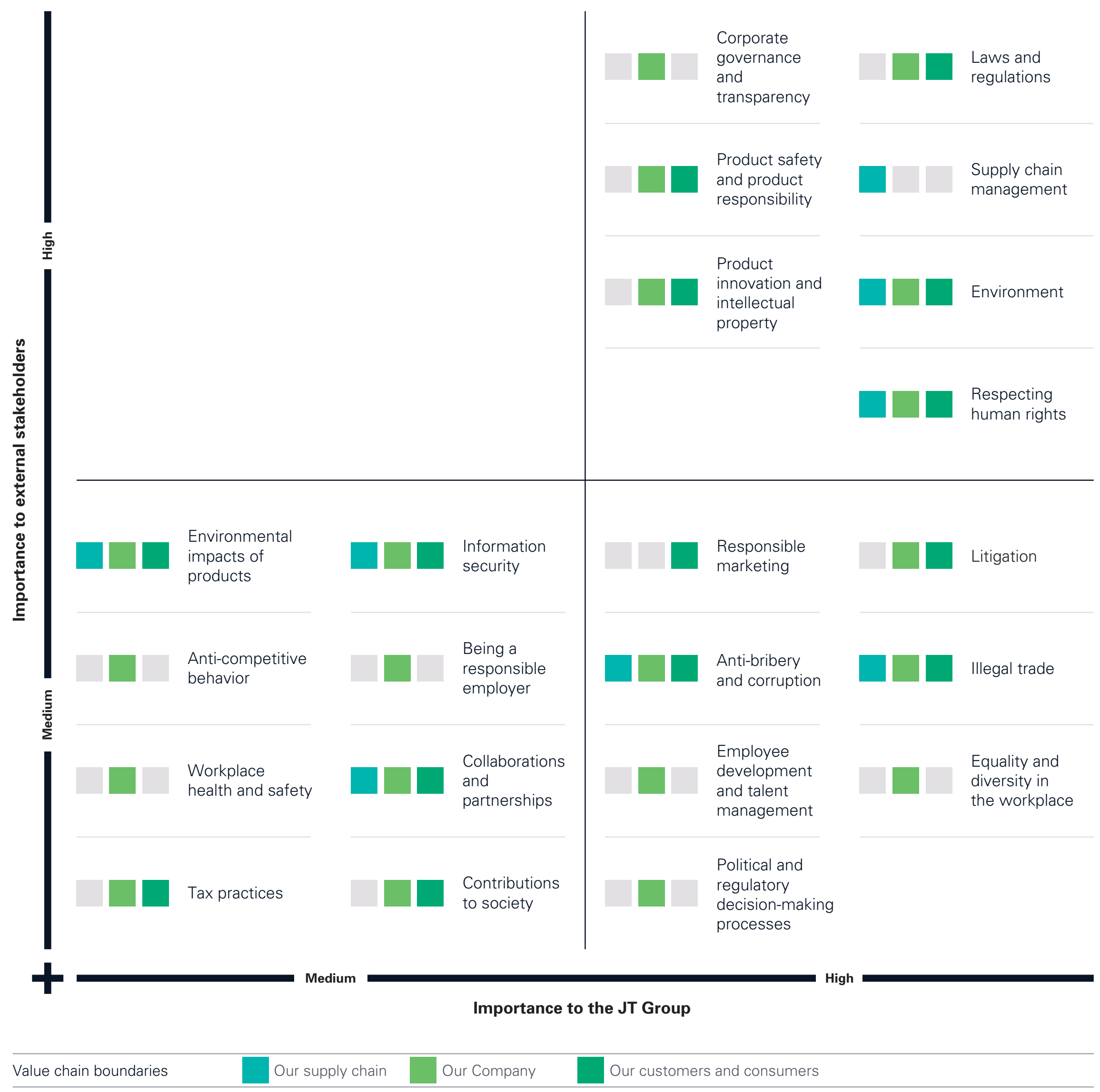
The JT Group's Material Issues

To help the JT Group to grow and to build a sustainable future as a member of the society in which we operate, we have identified a list of high-priority material issues. Our materiality is based on the JT Group's management principle, the 4S model. In 2015, we performed a materiality assessment covering the entire Group for the first time, selecting material issues with a medium or high level of importance for the JT Group and for our external stakeholders.

To identify our material issues, we began with a media and peer review, which generated a list of sustainability topics relevant to the Group. In addition to interviews with employees, our CEO and other members of top management, we also held interviews with 17 external stakeholders, including suppliers, investors, labor unions, NGOs and industry associations. Our top management then approved the results of the materiality assessment during a special workshop.

This process resulted in a final list of 22 material issues. We then divided these into two categories according to their level of importance to the JT Group and our external stakeholders: medium or high.

The JT Group's Materiality



Since our first materiality assessment, we have noted increasing public concern about the environment. We share this concern and have therefore repositioned "Environment" from Medium-Medium to High-High in the above matrix. We will continue to build on our effort to reduce our environmental impact on the planet.

Please refer to pages 72-73 for more details.

Looking ahead, we plan to carry out periodic materiality assessments to ensure that our priorities are up-to-date and consistent with the current needs.

Sustainability Strategy Overview

The JT Group's sustainability strategy is formulated based on the 4S model, our management principles, and encompasses our materiality analyses. It encourages us to look beyond our usual planning cycle period and think about the longevity of our business, the future of our planet and the society we live in. The foundations of our sustainability strategy, which apply across the Group, are our "three absolute requirements for sustainability."

The JT Group's Three Absolute Requirements for Sustainability

Respect for human rights

We are committed to respecting human rights across our global operations and value chains, as expressed in the JT Group Human Rights Policy.

p70

An improved social and environmental impact

We are committed to protecting the environment and making a positive difference wherever we operate.

p71-73

Good governance and business standards

We are committed to promoting transparent, fair and timely decision making that carefully considers the respective interests of consumers, shareholders, employees and the wider society.

p74-89

Tobacco Business Sustainability Strategy

We have identified priority areas for each business segment. The tobacco business, our core business, has selected the following four focus areas with its aspirational goals. In addition, we have set **11 specific targets**.

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

Pharmaceutical Business Sustainability Strategy

Throughout 2019, our pharmaceutical business held numerous discussions on sustainability and set out three focus areas. The mission of our pharmaceutical business is to create innovative, original drugs to support patients in the shortest time possible. In view of this mission, we have selected **"products and services"** and **"product safety and responsibility"** as our focus areas. As talent development of our employees is essential to first-in-class drug discovery, we have also selected **"people"** as our focus area. In total, we have set **five specific targets** for these pharmaceutical business focus areas.

Focus Areas	Aspirational Goals
Products and Services	**We will create innovative, original drugs to support patients in the shortest time possible.**
People	**We will strive to nurture talent development which enables us to create first-in-class (FIC) drugs.**
Product Safety and Responsibility	**We will strictly comply with all relevant laws, regulations, and industry standards in order to deliver safe drugs to patients.**

Processed Food Business Sustainability Strategy

Our mission in the processed food business is to deliver safe, high-quality products to consumers. One of the focus areas that we have selected is **"products and services."** We aim to continuously deliver products with commitment to quality and technology, in line with consumer needs. In the processed food business also, we will place emphasis on **"people."** We will strive to ensure workplace safety and invest in our people. Our third focus area is the **"supply chain."** We will continue to deliver safe products to our consumers by working on reducing social and environmental impacts, to ensure that our supply chain is sustainable over the mid- to long-term. In total, there are **eight targets** set for the focus areas in the processed food business.

Focus Areas	Aspirational Goals
Products and Services	**We will continue to provide high-quality, technology-driven products in response to our customer's needs, to satisfaction and trust.**
People	**We will ensure workplace safety for our employees, while continuously investing in people who can contribute to enhancing corporate value.**
Supply Chain	**We will reduce social and environmental impacts and continue to deliver safe products to consumers.**

Contribution to the SDGs

The JT Group supports the Sustainable Development Goals (SDGs) adopted by the United Nations. Through our business activities, the JT Group will contribute to the SDGs related to our business and its environment. We have mapped related SDGs against our initiatives for sustainable business and identified the nine SDGs to which our business can best contribute.

Please refer to pages 26-29 for more details.

Sustainability Strategy of Tobacco Business

4 Strategic Focus Areas	Aspirational Goals	Targets*1	Progress*2	SDGs		
Products and Services	**We will be a total tobacco company offering consumers an even greater choice of products by focusing on quality, innovation, and reduced-risk potential.**	**Reduced-Risk Products** Reduced-Risk Products (RRP) offer real benefits to consumers and society. Our responsibility as a manufacturer is to continuously develop and launch RRP that meet consumer expectations and to provide information on them. We will lead in providing the widest range of consumer choice in the RRP category.	At the end of 2019, our Reduced-Risk Product portfolio was present in 28 countries, with a choice of three tobacco vapor offerings (T-Vapor) and five types of e-cigarettes (E-Vapor).	3		p36
People	**We will be the employer of choice by investing in people.**	**Zero Injuries** In line with our vision of zero workplace injuries, we will reduce injury rates by 25% by 2023 and 50% by 2030. (Baseline year: 2015).	Recordable injury rate*3 declined 31.2% from 0.72 in 2015 to 0.49 in 2019.	8		p18
		Community Investment Between 2015 and 2030 we will invest US$600 million to help make communities inclusive and resilient, with our employees contributing 300,000 volunteering hours.	Since 2015, we have invested US$300 million in our communities and employees volunteered 119,349 hours on company time.	10, 11, 15		
		Employer of Choice We will be a certified employer of choice every year in at least 60 locations by focusing on talent management, rewards, and empowerment.	We were certified as a Top Employer in 63 locations, an increase of 5 locations from the prior year. We were also awarded with local certifications in 8 locations.	8		
Supply Chain	**We will reduce environmental and social risks, and enable transparent and responsible practices across our supply chain.**	**Greenhouse Gas Emissions** We will reduce greenhouse gas emissions from our own operations by 35% and from our direct leaf supply chain by 40%, between 2015 and 2030.	Since 2015, we have reduced greenhouse gas emissions from our own operations by 17.4%. Greenhouse gas emissions from our direct leaf supply chain increased by 17.9%.*4	13	17	p38
		Water and Waste We will reduce water withdrawal by 15% and waste by 20%, in relation to our own operations, between 2015 and 2030.	Since 2015, we have reduced water withdrawal by 9.7% and waste by 6.3%, in relations to our own operations.	12		
		Forestry We will replace all wood from natural forests used in the tobacco curing process of our directly contracted growers with renewable fuel sources by 2030.	Based on our 2019 sustainable tree planting activities in Tanzania, Zambia and Brazil, we estimate that we are on a path to achieve 59% renewable wood sourcing by 2026.	12, 15		
		Agricultural Labor Practices We will implement our Agricultural Labor Practices (ALP) program in all sourcing countries by 2025.	In 2019, 81% of our supplying entities reported against ALP. [58%*5 of our directly contracted growers and 98% of our leaf merchants were covered by ALP; leaf merchants data come from reporting entities only and excluding India and China.] 74% of our volumes were covered by ALP.	8		
		Supplier Screening We will screen all key suppliers against environmental, social, and governance criteria by 2023.	At the end of 2019, 67% of our key suppliers were screened against ESG criteria.*6	8		
Regulatory Environment and Illegal Trade	**We will ensure the Company is included in policymaking leading to fair and balanced regulation, and enhance our cooperation with governments to combat illegal trade.**	**Engagement** We will always protect our ability to participate in public policy debate with the aim to achieve balanced regulation that meets societal concern and supports business growth.	During 2019, we engaged openly and transparently in public policy debate and made our views known to regulators, NGOs and other relevant stakeholders in the countries where we operate.	16		p41
		Illegal Trade We will engage in dialogue with law enforcement agencies, with the goal to exchange intelligence regarding illegal tobacco products, in order to support the reduction of illegal tobacco products.	In 2019, our Anti-Illicit Trade team provided 1,129 intelligence reports to law enforcement agencies, and advised 2,687 law enforcement officers on counterfeit recognition.	16		p40

*1 The above are targets for our tobacco business, except for Community Investment which is a Group-wide target.
*2 Progress shown above are 2019 results.
*3 Recordable injury rate = Recordable injuries/200,000 hours worked. Some data from newly acquired business have been excluded, as newly acquired business needs 18 months to integrate the JT Group Health and Safety Standards.
*4 The main reason for the increase in GHG emissions from our direct leaf supply chain is the increased volume sourced from Zambia and Tanzania, both of which use wood for curing that currently is predominantly non-renewable. We expect that the impact of initiatives to reduce leaf-related emissions will be seen from 2022 onwards, with curing barn upgrades and the increase in proportion of renewable wood used for curing in Zambia and Tanzania.
*5 The decrease from 96% in 2018 to 58% in 2019 is due to new acquisitions.
*6 Results for our international tobacco business.

Sustainability Strategy of Pharmaceutical Business

Strategic Focus Areas	Aspirational Goals	Targets	SDGs	
Products and Services	**We will create innovative, original drugs to support patients in the shortest time possible.**	**Engaging in R&D Activities** We will continue our efforts and investments into research and development activities of innovative drugs in specific therapeutic areas.	3 GOOD HEALTH AND WELL-BEING	
People	**We will strive to nurture talent development which enables us to create first-in-class (FIC) drugs.**	**Fostering Ethical Awareness** In order to develop talent and foster employees' ethical awareness and sense of responsibility towards saving patients, we will continue to learn more about patients' needs by engaging in dialogue with medical experts through our internal educational activity "For the Patients Project."	8 DECENT WORK AND ECONOMIC GROWTH	
		Community Investment*¹ Between 2015 and 2030 we will invest US$600 million to help make communities inclusive and resilient, with our employees contributing 300,000 volunteering hours.	10 REDUCED INEQUALITIES, 11 SUSTAINABLE CITIES AND COMMUNITIES, 15 LIFE ON LAND	17 PARTNERSHIPS FOR THE GOALS
Product Safety and Responsibility	**We will strictly comply with all relevant laws, regulations, and industry standards in order to deliver safe drugs to patients.**	**Responsible Promotion of Drugs** We will conduct, among others, regular training programs for our medical representatives in order to provide medical professionals with appropriate information on pharmaceutical products.	12 RESPONSIBLE CONSUMPTION AND PRODUCTION	
		Greenhouse Gas Emissions We will reduce greenhouse gas emissions from our own operations by 31%, between 2015 and 2030.	13 CLIMATE ACTION	

Sustainability Strategy of Processed Food Business

Strategic Focus Areas	Aspirational Goals	Targets	SDGs	
Products and Services	**We will continue to provide high-quality, technology-driven products in response to our customer's needs, to satisfaction and trust.**	**Improvement of Quality of Life** We will develop and provide high-value-added products with a focus on "health," "convenience," and "diversity," in response to diverse consumer needs.	3 GOOD HEALTH AND WELL-BEING	
People	**We will ensure workplace safety for our employees, while continuously investing in people who can contribute to enhancing corporate value.**	**Enhance Job Satisfaction** We will further improve job satisfaction by promoting talent development in a secure and motivating workplace.	8 DECENT WORK AND ECONOMIC GROWTH	
		Zero Injuries In line with our vision of zero workplace injuries, we will reduce injury rates by 25% by 2025 and 50% by 2030. (Baseline year: 2018)	8 DECENT WORK AND ECONOMIC GROWTH	
		Community Investment*¹ Between 2015 and 2030 we will invest US$600 million to help make communities inclusive and resilient, with our employees contributing 300,000 volunteering hours.	10 REDUCED INEQUALITIES, 11 SUSTAINABLE CITIES AND COMMUNITIES, 15 LIFE ON LAND	17 PARTNERSHIPS FOR THE GOALS
Supply Chain	**We will reduce social and environmental impacts and continue to deliver safe products to consumers.**	**Foster a Safe and Reliable Corporate Brand** We will promote food safety management in compliance with global food safety standards to develop food safety. We will also enhance the way we communicate with customers so that they retain trust in our food quality.	12 RESPONSIBLE CONSUMPTION AND PRODUCTION	
		Promote Use of Environmentally Friendly Packaging Materials We will promote the use of renewable plant-based resources and reduce our use of non-renewable resources, to reduce the environmental impact of our products.	12 RESPONSIBLE CONSUMPTION AND PRODUCTION, 13 CLIMATE ACTION, 15 LIFE ON LAND	
		Waste We will reduce the amount of waste associated with our Japanese domestic offices by an average of 1% per year. (Intensity target*²).	12 RESPONSIBLE CONSUMPTION AND PRODUCTION	
		Greenhouse Gas Emissions We will reduce greenhouse gas emissions from our own operations by 28%, between 2015 and 2030.	13 CLIMATE ACTION	

*¹ Target for Community Investment is a Group-wide target.
*² Amount of waste generation / Amount of production.

Interview with Our CSO

Kazuhito Yamashita
Director and Senior Vice President
Chief Sustainability Officer, Compliance and General Affairs

Q. Tell us about your role as the Chief Sustainability Officer (CSO).

Contributing to the sustainable development of society is essential for the JT Group to achieve sustainable growth and to meet the needs of our four key stakeholder groups under our 4S model. As a director of the company and CSO, it is my role to look to the future and pursue sustainability management across our Group. With a mid- to long-term perspective, we aim to achieve sustainable growth for the society in which we operate and for the JT Group, so that we can respond to the expectations of our stakeholders.

Q. How do you pursue sustainability management in your organization?

In 2015, we identified 22 material issues relevant to the JT Group and our stakeholders to achieve sustainable growth. In 2016, our Corporate Governance Policy stipulated that "the Board of Directors, based on the understanding that measures towards domestic and foreign issues on sustainability are an essential part of risk management, shall receive reports as necessary through Members of the Board in charge of sustainability and proactively work on such issues, such as by holding discussions." As the policy demonstrates, pursuing sustainability is at the heart of what we do and it is one of the key management issues for the Group.

In 2019, to build on our past sustainability initiatives and continue evolving, we re-organized our organizational structure and established a sustainability management division at JT headquarters and appointed a Senior Vice President for sustainability. We also set out a sustainability strategy encompassing the whole Group. We are now supporting Group businesses to implement their respective sustainability strategies. By doing so, we are engaged in environmental management, risk management, supply chain management, initiatives for respecting human rights and community investment on a day-to-day basis.

Q. Tell us about your sustainability issues and challenges.

The three absolute requirements for the Group are **"respect for human rights," "an improved social and environmental impact"** and **"good governance and business standards."**

The JT Group operates in more than 130 countries/regions. In some of these markets, human rights are at risk – and **respect for human rights** is a crucial aspect of the Group's sustainability. We set out the JT Group Human Rights Policy in 2016. Since then, have been training our employees on human rights through regular e-learning courses. We perform human rights due diligence for our operations globally. We work to ensure that human rights are respected not only within our own Group, but also throughout our value chain.

As we all are increasingly concerned about the effects of climate change, corporations are working on **improving environmental impact**. We have set out the JT Group Environment Plan 2030 to address these issues within our Group and throughout our value chain. We are working on reducing GHG emissions, shifting to renewable energy, managing water risks, conserving forest resources and further reducing the environmental impact of waste.

To **improve our social impact**, we prioritize three areas: "reducing inequalities," "improving community resilience in disaster-prone areas" and "protecting the environment." What we would like to see is inclusiveness both in society as a whole and indeed in all the communities we operate in. We also provide employees with opportunities for volunteering so that they can proactively contribute to local communities.

Corporate governance is one of the most important management issues. Governance is a mechanism for ensuring that transparent, fair, prompt and resolute decision making is carried out in line with the 4S model, our management principles. Going forward, we will keep our governance under review for continuous improvement to ensure it is fit for the purpose.

Q. Can you tell us about the sustainability strategy for each of your businesses?

Each business has set out its own "focus areas," with specific targets. Back in 2018, our tobacco business had four focus areas and a total of **11 targets**. By pursuing such targets, we believe we can support and contribute to achieving the United Nations' Sustainable Development Goals. I'm pleased to say this is the first time we are reporting on progress toward achieving the 11 targets of our tobacco business.

During 2019, our pharmaceutical and processed food businesses set out their own sustainability strategies, focus areas and **targets**. Our sustainability strategy for the entire Group is now in place.

Q. Can you give us some insights into the sustainability strategy for your tobacco business?

E-cigarettes and tobacco vapor products are gaining popularity as alternatives to traditional combustible products. With the surge of a new category of Reduced-Risk Products (RRP), the tobacco industry is undergoing major change. We have selected **Products and Services** as one of our focus areas. Understanding what consumers are looking for is essential. We would like to offer our customers an even greater choice of products by focusing on quality, innovation and reduced risk potential.

For the Group to achieve sustainable growth, the skills and commitment of our employees are vital. The communities we operate in, and the people who live in them, are important stakeholders. For this reason, we focus on investing in **People** and our tobacco, pharmaceutical and processed food businesses have each chosen this topic as one of their focus areas.

Supply chain management is a top priority for our business. Leaf tobacco is the most important raw material for us, so its stable and sustainable procurement is crucial to supply chain management. We will continue to implement Agricultural Labor Practices (ALP), our core program for managing the leaf tobacco supply chain and responding to societal issues.

The tobacco industry is highly regulated. The restrictions imposed through **regulation** are increasing every year and it is an area of concern to our stakeholders. We will protect our ability to participate in public policy debates and continue to engage in dialogue. **Illegal trade** not only undermines our business, but it can cause serious harm to our consumers and society. We will continue to engage with law enforcement agencies, exchanging intelligence about illegal tobacco products to help reduce illegal trade.

Q. How are you raising awareness of sustainability within the Group?

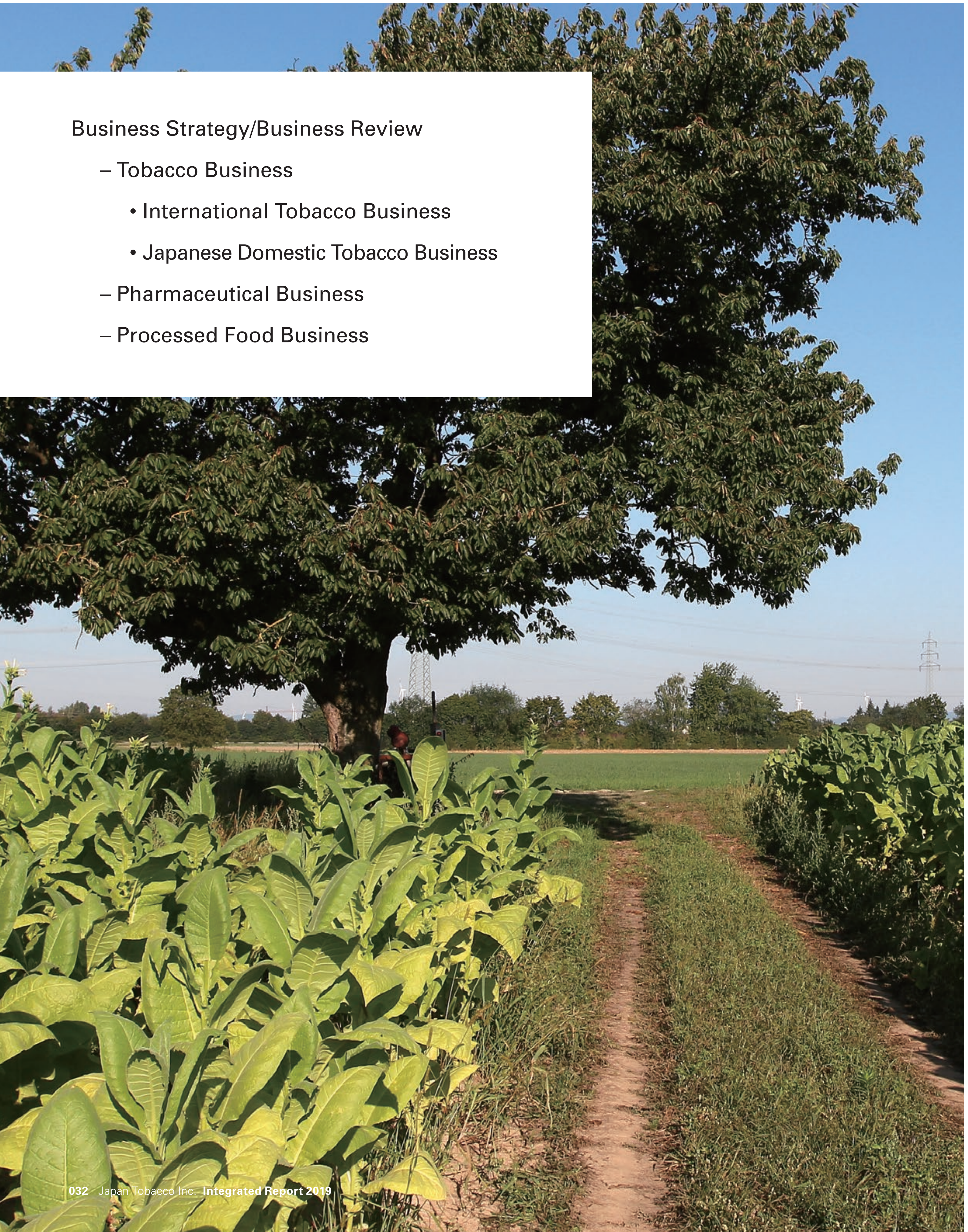
We are working to raise each and every employee's awareness of sustainability through a variety of initiatives. These include communications from top management to employees, seminars on ESG (environmental, social and governance) issues, workshops to enhance employees' understanding of the United Nations' Sustainable Development Goals and briefings at our operational sites.

In our international tobacco business, our Sustainability Awards celebrate outstanding sustainability projects undertaken by our own employees. Through these initiatives, we encourage our employees to think about and act on sustainability.

Q. Tell us about your aspirations for the future.

As we work day in, day out to grow our business, my dream is for everyone in our Group to think about sustainability and to feel that they are contributing to improving the society we are all part of. I believe this is the direction we should be heading in – I hope I can be proactive in leading the way.

Business Strategy/Business Review



Tobacco Business

The tobacco business remains our core and is expected to continue driving our sustainable profit growth.

The Tobacco Business Strategy

Tobacco business: Our core business and the Group's profit growth driver

– Mid to high single digit profit growth for the mid- to long-term

- Japanese Domestic Tobacco
  – Strengthen top-line in both RRP and cigarettes
- International Tobacco
  – Sustainable profit growth in existing markets
  – Geographic expansion through M&A and organic initiatives
  – Steady progression in RRP

The tobacco business has been focusing on sustainable profit growth, consistently playing a pivotal role in JT Group's profit growth. Its role continues to be of paramount importance for the achievement of mid to high single-digit adjusted operating profit growth at constant currency, which is our main target. In light of the evolving operating environment, we have been enhancing our focus on the sustainability of the profit growth generated by the tobacco business. Additionally, in order to strengthen and speed up the decision-making process, we have streamlined the management structure, as demonstrated by our Group CEO, Masamichi Terabatake, directly heading the tobacco business.

We believe that the consumer-centric mindset is key to achieving our business targets and, therefore, we continue to foster this mindset across the organization. By constantly reviewing and adapting our mindset and investment initiatives, we will continue to strengthen our business operations in both cigarettes and RRP. In particular, RRP is relatively a new business, where we cannot rely solely on the strategies deployed successfully in cigarettes. In order to overcome the intense competition in this important category, we are optimizing resource allocations across the Group; enhancing collaboration between domestic and international divisions and maximizing synergies and growth opportunities on a global basis. Following the consolidation of the R&D functions in 2019, we have significantly streamlined corporate strategy, business development and RRP reporting lines in 2020. We are also working towards integrating the quality assurance functions, whose role will be to ensure product safety and reliability. In the three-year time set for the Business Plan 2020, cigarettes will continue to play a major role in delivering mid to high single digit profit growth in the overall tobacco business.

In the Japanese domestic tobacco business, we have a strong and wide product portfolio in cigarettes, primarily comprised of the key brands of MEVIUS, Seven Stars, Winston, Natural American Spirit and Camel, as well as in RRP comprised of Ploom TECH and Ploom TECH+ representing the low-temperature heating category and Ploom S representing the high-temperature category. Generating stable and sustainable profit growth through fully utilizing these strong equity brands in both cigarettes and RRP is the key to the tobacco business growth. While increasing profit in Japan in the short-term is challenging, we aim to return to profit growth by strengthening our top-line initiatives in both cigarettes and RRP. Please refer to the "Japanese domestic tobacco business" for further details.

In the international tobacco business, we seek to continue strong bottom-line growth through a clear strategic agenda centered on sustainable profit growth in existing markets; geographic expansion through M&A and organic initiatives; and steady progression in RRP. In existing markets, we will focus on maximizing the equity of our Global Flagship Brands (Winston, Camel, MEVIUS and LD) in order to fuel our market share momentum and seize pricing opportunities. Concerning geographic expansion, we will focus our organic investments on further strengthening our talent base, brand portfolio and business infrastructure. At the same time, we will remain alert to valuable M&A opportunities in markets that matter. In RRP, Logic is strengthening its presence in the E-Vapor segment, fueled by the ongoing progression of Compact in many geographies. As part of our continuous development process, we will also commercialize a Heated Tobacco product in selected international markets this year. The device will be endorsed by Ploom, while related consumables will be branded according to market and consumer preferences. Please refer to the "international tobacco business" for further details.

This section is intended only to explain the business operations of the JT Group, not to promote sales of tobacco or vaping products or encourage smoking or vaping among consumers.

Tobacco Industry

The Tobacco Industry is evolving and there are many types of tobacco products available in this marketplace today. Cigarettes remain the most popular choice for consumers, while Fine Cut, cigars, pipe tobacco, smokeless tobacco, waterpipe tobacco and kretek continue to draw consumers' interest.

In addition, the RRP category has become increasingly popular. In particular, the "E-Vapor" market size has been expanding at a fast rate, notably in the U.S. and across Europe. The products vaporize liquid solutions, often containing nicotine, and the generated vapor is then inhaled by the user.

As E-Vapor products do not use tobacco leaf, they have not usually been regulated or taxed as tobacco containing products. However, regulation and taxation of the products have changed in some countries in accordance with the expansion of this category.

Another type of RRP, referred to as "T-Vapor" or "Tobacco Vapor," has been growing steadily, particularly in Japan. These products are taxed and regulated as tobacco products in principle because they use tobacco leaves. We expect further innovation and product offerings will drive growth in T-Vapor, especially as market players take keen interest in this new category.

In addition to these two types, the growth of smokeless tobacco has accelerated in markets with a long history of these products, particularly in Europe and the U.S. With smokeless tobacco, users can enjoy the characteristic tobacco taste and flavor directly through their nose or mouth.

Approximately 5.3 trillion cigarettes*[1] are consumed annually around the world, reaching global sales of approximately US$700 billion.*[1] China is by far the largest market, accounting for over 40% of global consumption, but is almost exclusively operated by a state monopoly. Indonesia, the U.S., Russia and Japan are the following four largest markets.*[1]

In general, the market dynamics of cigarettes are distinctively different between mature and emerging markets.

In mature markets, industry volume tends to decline and these movements can reflect various factors, such as limited economic growth, tax increases, tightening regulations and demographic changes among others. In addition, down-trading is prevalent in these markets, as limited growth of disposable income inclines consumers to seek more value in comparatively affordable tobacco products.

In emerging markets, on the other hand, total consumption tends to be more resilient, driven by population growth and economic development, particularly across the Middle East and Africa. As personal disposable income generally increases year-on-year, consumers look for quality and trade up to products in a higher price range.

Overall, the global industry volume*[1] of cigarettes has been decreasing in recent years, although at a sustainable pace. However, more importantly, we expect industry value to continue growing in the 2020-2022 period, with price increases more than compensating for the volume contraction. These trends – decline in volume and increase in value – are expected to continue in the upcoming three years. On the other hand, the RRP industry will grow further as we anticipate its global*[2] net sales value to reach approximately US$40 billion in 2022.

Excluding the Chinese monopoly, there are four major global tobacco players: Philip Morris International Inc., British American Tobacco Plc., Japan Tobacco Inc. and Imperial Brands Plc. In terms of RRP, besides these four companies, JUUL Labs, Inc. (E-Vapor) and Swedish Match AB (smokeless tobacco) also have a meaningful presence.

*[1] According to 2018 data
*[2] Excludes China

Regulations

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

Recent regulations are focusing more on the product itself. Plain packaging, or a branding ban, has been introduced in some markets and furthermore, regulators are becoming more aggressive by restricting ingredients and emissions, in accordance with the guidelines proposed by the Framework Convention on Tobacco Control. In Europe, all EU member states have already implemented the new Tobacco Products Directive in 2017, which adopted extended health warnings, minimum requirements for a packaging unit or restrictions on the use of additives among others. These moves to commoditize tobacco products will undermine fair competition among tobacco manufacturers that are trying to meet increasingly diverse consumer preferences. Even worse, they could result in an undesired increase in illicit trade, as commoditized products with less uniqueness are easier to counterfeit and more difficult to detect when smuggled.

Regarding RRP, a few countries such as the U.S. and parts of Europe have recently established new standards and frameworks used in terms of scientifically evaluating the claims of reduced risks that come with using these products. In order to gain official approval from these governments, major global tobacco manufacturers have intensified their activities in developing these reduced-risk claims. With regards to the regulatory progress in this RRP category, specified regulations are implemented in some markets, namely the prohibition of sales in the U.S. of flavored E-Vapor products, which was implemented in February 2020, or in other countries the implementation of the same level of regulations as conventional tobacco products. However, global implementation of RRP product regulations has not yet been observed, and the attitude towards regulations still differs from one market to another. Please refer to "Regulation and Other Relevant Laws" for more details.

Taxation

Tobacco products are subject to excise or similar taxes in most countries as governments seek to secure their revenue or promote public health. During 2019, excise taxes (including for RRP) were raised in various markets, including France, Romania, Russia and Turkey.

In general, tax increases are passed onto the retail prices. Therefore, repeated tax increases in a short period of time or substantial tax increases, could lead to a decline in industry volume and trigger an increase in illicit trade, which could in turn affect our business.

Tobacco Business Sustainability Strategy - Four Focus Areas

Exceeding Expectations with Products and Services - RRP

As alternatives to traditional combustible products, e-cigarettes (E-Vapor) and tobacco vapor products (T-Vapor) are gaining popularity with consumers around the world. Our industry is changing but our commitment to consumer choice remains.

We are always listening and reacting to the changing tastes of adult smokers and vapers around the world. We develop, test and bring to market new and innovative forms of RRP and offer real benefits to consumers, society and our business.

Between 2018 and 2020, we are investing 100 billion yen in RRP, to further develop our supply chain and expand our research and development capabilities.

Our Product Portfolio

JT Science: An online resource for all

Our mission is to inform, educate and collaborate with all those interested in learning about the science behind RRP - from consumers to scientists and the regulatory community. We strive for an open, balanced and fair environment where factual scientific data and assessments are shared in a transparent way.

Learn more about our research at JT Science.

RRP Supply Chain

We have established a dedicated supply chain for our RRP, building strong supplier partnerships that support business expansion and meet the demands of our increasingly sophisticated portfolio.

In 2018, we opened an e-liquid (E-Vapor) production facility on the premises of our manufacturing site in Gostkow, Poland. We then further boosted our in-house production in 2019, bringing into service a new Ploom product plant in the same location. These new facilities will enable us to keep up with the demand for e-liquids containing nicotine, tobacco capsules and tobacco sticks in expanding markets across the world.

Responsible Recycling and Disposal Schemes

We take our responsibility for the environment very seriously and provide consumers with advice and support to help them conveniently and safely recycle or dispose our products at the end of their useful life.

Ploom Return Scheme in Japan

In some parts of Japan, we have introduced recycling boxes at shops selling Ploom so that consumers can return their used devices, capsules and cartridges conveniently.

This program was a significant extension of a 2017-2018 pilot scheme, in which we sent out recycling boxes to more than 250,000 people. In 2019, we started collecting used Ploom devices in addition to used capsules and cartridges.

Key achievements in 2019
Recycling boxes introduced in around 300 shops

Logic Return Scheme in Switzerland

Online customers can order a Logic recycling box, made from FSC-certified paper,* to collect their used pods. They can then send these boxes to us free of charge for recycling.

We also set up “pod points” in shops selling Logic products across Switzerland, giving consumers the option to return their used products in person.

Key achievements: March-December 2019
3,600+ individual recycling boxes ordered
440+ recycling boxes returned

	Aspirational Goal	Target	Progress
RRP	We will be a total tobacco company, offering consumers an even greater choice of quality, products by focusing on quality, innovation, and reduced-risk potential.	We will lead in providing the widest range of consumer choice in the RRP category.	At the end of 2019, our RRP portfolio was present in 28 countries, with a choice of three tobacco vapor offerings (T-Vapor) and five types of e-cigarettes (E-Vapor).

* Paper products that meet the Forest Stewardship Council standards

Building Sustainable Supply Chains

Maintaining a well-managed supply chain is essential for the sustainability of our business. To ensure the highest levels of sustainability and integrity across the supply chain, we work in close cooperation with all our suppliers.

Agricultural Labor Practices

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

As part of our continuous improvement approach, the ALP program allows us and our suppliers to identify potential labor challenges on tobacco farms and help improve growers' labor practices. Being an integral part of the Supply Chain Due Diligence process, it also contributes to the social aspect of grower communities and supports sustainable agriculture overall. Whether we source tobacco directly from growers or through tobacco leaf merchants, our contracted suppliers are committed to implementing ALP.

	Aspirational Goal	Target		Progress
Agricultural Labor Practices	We will reduce environmental and social risks, and enable transparent and responsible practices across our supply chain.	We will implement our ALP program in all sourcing countries by 2025.	100% of our supplying entities to report on ALP	In 2019, 81% of our supplying entities reported against ALP. [58% of our directly contracted growers and 98% of our leaf merchants were covered by ALP; leaf merchants data come from reporting entities only and excluding India and China.*]
			100% of tobacco leaf volumes to be covered by ALP	74% of our volumes were covered by ALP.

Learn more about our historical data at JT.com.

* The decrease from 96% in 2018 to 58% in 2019 is due to new acquisitions.

Supplier Screening

Our supplier screening process, applied in our international tobacco business, allows us to understand potential risks related to compliance, human rights, the environment and health and safety. In 2019, we continued to strengthen and automate the process by integrating a continuous key supplier monitoring service. In the Japanese market, suppliers of non-tobacco materials and other products and services are subject to screening against the JT Group Supplier Standards, with key suppliers being monitored regularly though surveys.

	Aspirational Goal	Target	Progress
Supplier Screening	We will reduce environmental and social risks, and enable transparent and responsible practices across our supply chain.	We will screen all key suppliers against environmental, social, and governance criteria by 2023.	At the end of 2019, 67% of our key suppliers were screened against ESG criteria in our international tobacco business.

ARISE

Our flagship program ARISE – Achieving Reduction of Child Labor in Support of Education – has been committed to tackling child labor in our tobacco growing communities since 2011. In 2019, ARISE placed 6,186 children into formal education, building on the impact of previous years. The program is forging real sustainable change by implementing robust solutions to prevent child labor.

In 2019, we focused on mapping out new communities to scale up ARISE, building on community capacities to ensure the sustainability of the program and digitizing our Child Labor Monitoring System using blockchain technology.

We will continue to work collaboratively with growers, communities, business leaders and governments to create solutions that address the root causes of child labor, while always keeping the child's right to quality education at the heart of what we do.

Elaine McKay
Social Programs Director, JT International S.A.

Reducing Our Environmental Impact in the Tobacco Value Chain

Regarding our targets on "Greenhouse gas emissions," "Water and waste" and "Forestry," visit Environment and our operations. Learn more about our programs and initiatives in our international tobacco business at "We're serious about protecting the environment."

Regulatory Environment and Illegal Trade

Experts estimate that over 10% of all cigarettes sold globally (excluding China) are illicit, with approximately US$45 billion in global tax revenue lost each year. This illegal trade fuels human trafficking, organized crime and terror groups. It causes harm to consumers, as uncontrolled products circumvent regulations and quality controls, and undermines legitimate tobacco businesses. Tackling illegal trade is a top priority for us, and our Anti-Illicit Trade team is recognized as the industry leader in combating this problem.

Tackling Illegal Trade

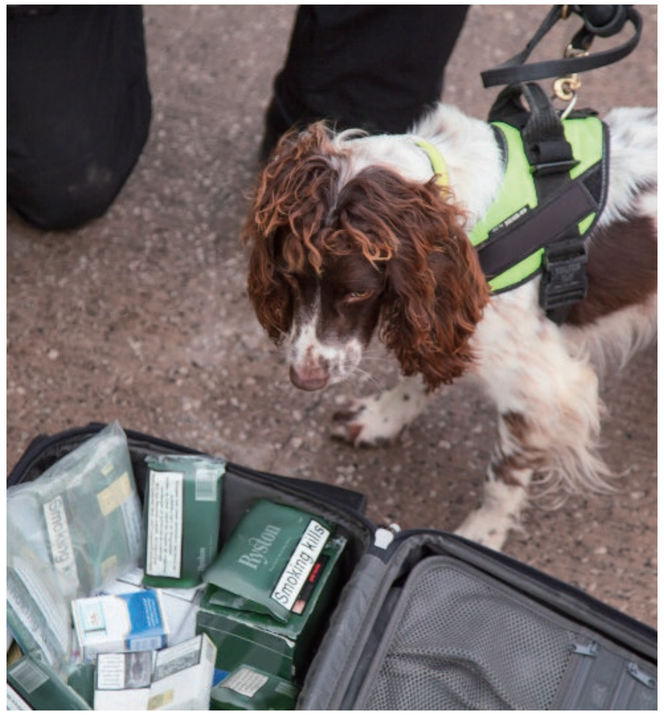
Our global Anti-Illicit Trade team investigates the illegal tobacco trade and protects consumers and society, as well as our business and reputation, from criminal elements.

The team works with our markets to secure our supply chain and assists law enforcement in removing illegal tobacco from the marketplace. It maintains a robust dialogue with governments and law enforcement agencies on the threat of illegal tobacco through public-private partnerships and provides counterfeit awareness programs for law enforcement, globally.

The team protects the JT Group's business and reputation, supporting our long-term, sustainable future.

In 2019, our Anti-Illicit Trade team provided 1,129 intelligence reports to law enforcement agencies, leading to seize more than 3.2 billion illegal cigarettes. Based on our information, law enforcement raided more than 70 counterfeit tobacco factories and storage locations.

As a direct result of our work to tackle illegal trade, and based on seizure statistics, notified seizures of counterfeit products in the EU have remained consistently high over the past four years (approximately 90% of products seized are counterfeit). During the same period, notified seizures of our own genuine products in the EU have decreased by nearly 50%, thanks to our markets' efforts in securing our supply chain, with the support of the Anti-Illicit Trade team. Both the EU and the U.K.'s HM Revenue and Customs recognized us as an industry leader in the fight against illicit trade.



In tackling illegal trade, the JT Group complies with all laws and regulations while fulfilling its obligations under the European Union Cooperation Agreement, signed in 2007.

This means supplying tobacco products only in volumes that correspond with the legitimate demand of the intended market of retail sale. Our Anti-Illicit Trade Research team has developed a global methodology to assist market authorities in taking a consistent and accurate approach to annual legitimate market demand (LMD) calculations. Our markets perform these in conjunction with their annual plan, creating a proactive supply chain control mechanism to make sure that planned sales volumes are in line with LMD, and ensuring our compliance.

Compliance also means the implementation and operation of our Track and Trace program, which helps us to track the movements of products along the supply chain, supporting our supply chain analysis. The program has been an important element of our compliance policy for more than a decade firstly as a self-regulation measure and later to meet legal requirements in a growing number of jurisdictions.

In addition to the United Arab Emirates, Saudi Arabia and Russia, the first regional system applicable in all member states of the EU went live on May 20, 2019. Despite the challenging timelines involved in implementing this complex system, we complied with the regulations as of entry into force, with minimal disruption in the countries in which we operate.

Learn more about our approach to tackling illegal trade at JT.com.

	Aspirational Goal	Target	Progress
Illegal Trade	We will ensure the Company is included in policymaking leading to fair and balanced regulation, and enhance our cooperation with governments to combat illegal trade.	We will engage in dialogue with law enforcement agencies, with the goal to exchange intelligence regarding illegal tobacco products, in order to support the reduction of illegal tobacco products.	In 2019, our Anti-Illicit Trade team provided 1,129 intelligence reports to law enforcement agencies, and advised 2,687 law enforcement officers on counterfeit recognition.

Optimizing the Regulatory Environment

During 2019, we engaged openly and transparently in public policy debate and made our views known to regulators, NGOs and other relevant stakeholders in the countries where we operate.

We responded to public consultations on regulatory issues of concern to society and business, such as plain packaging, RRP and retail display bans, among many others.

We also participated in public discussions around good governance, anti-illegal trade, better regulation, transparency and sustainability.

	Aspirational Goal	Target	Progress
Engagement	We will ensure the Company is included in policymaking leading to fair and balanced regulation, and enhance our cooperation with governments to combat illegal trade.	We will always protect our ability to participate in public policy debate with the aim to achieve balanced regulation that meets societal concern and supports business growth.	During 2019, we engaged openly and transparently in public policy debate and made our views known to regulators, NGOs and other relevant stakeholders in the countries where we operate.

Learn more about our views on regulation and the latest regulatory developments in the industry at JT.com.

Business Review

International Tobacco Business

Results for the fiscal year ended December 31, 2019

Total volume increased 4.3%, driven by acquisitions in Bangladesh and Russia. Excluding acquisitions, total volume performance was resilient due to the accelerated growth of our Global Flagship Brands (+4.0%). Currency-neutral core revenue grew 9.3%, led by robust price/mix gains and positive volume contribution. Adjusted operating profit was up 10.7%, at constant currency, driven by the strong top-line performance. On a reported basis, core revenue increased 1.5% while adjusted operating profit was down 10.5%, reflecting currency headwinds.

Key Highlights

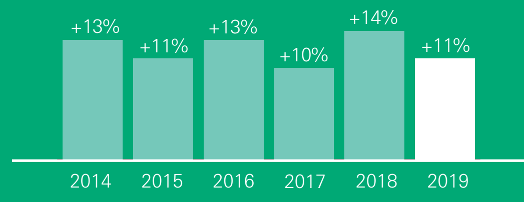
Total Shipment Volume
445.8 (BnU)
+4.3%
Year-on-Year Change

GFB Shipment Volume
277.0 (BnU)
+4.0%
Year-on-Year Change

Core Revenue
11,496 (USD MM)
+1.5%
Year-on-Year Change

Adjusted Operating Profit
3,126 (USD MM)
-10.5%
Year-on-Year Change

Adjusted Operating Profit Growth at Constant FX*



* Excluding 2017 one-time loss

I anticipate another strong year for JTI in 2020. We continue to believe in the robustness and resilience of the conventional products model, while stepping up our efforts in RRP to satisfy changing consumer needs.

Eddy Pirard
Chief Executive Officer, JT International S.A.

2019 Performance

Overview

2019 was an excellent year for JTI across all key performance indicators.

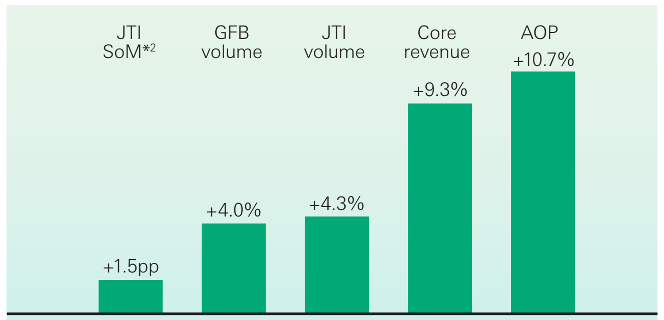
The successful integration of the acquired businesses in Bangladesh and Russia enabled us to grow strongly versus prior year, achieving a total volume increase above 4%. Excluding acquisitions, our volume declined less than 1%, as market share gains continued, driven by all Global Flagship Brands.

Our investments in strategic acquisitions and organic expansion have enabled JTI to accelerate share of market and share of value growth, recording an outstanding increase across its top-30 markets.

Price/mix contribution continued to be strong and above JTI's 5-year average, demonstrating once again the robustness and sustainability of our growth model. The robust price/mix contribution, combined with an expanded volume base, resulted in currency-neutral core revenue and adjusted operating profit growth of 9.3% and 10.7%, respectively.

Importantly, 2019 marked the ninth consecutive year in which JTI achieved double-digit earnings growth at constant currency (excluding one-time factor in 2017), while also increasing investment levels.

2019 Performance*[1]



*[1] 2019 variance vs. prior year. Core revenue and adjusted operating profit (AOP) at constant currency
*[2] Based on JTI's top-30 markets (cigarettes + Fine Cut)

Our top- and bottom-line performance remained strong when excluding acquisitions and inventory movements, highlighting the strength of our talented people and the competitiveness of our brands.

top EMPLOYER GLOBAL 2020
CERTIFIED EXCELLENCE IN EMPLOYEE CONDITIONS

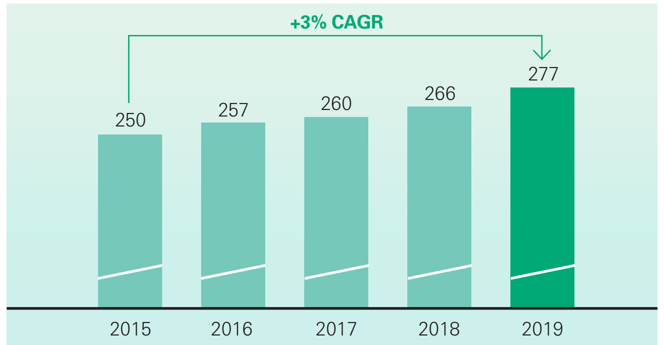
In addition, throughout the year we continued to pursue selected opportunities in RRP, notably with the expansion of Logic Compact in E-Vapor and the introduction of Nordic Spirit in nicotine pouches.

Global Flagship Brands

Global Flagship Brands grew volume for the fifth consecutive year, reaching 277 billion units. This represents a 4% increase versus 2018 and a compounded annual growth rate of 3% since 2015.

This achievement is remarkable if we consider that, over the same period, tobacco industry volume has declined around 4% per year in our top-30 markets.

GFB Volume Evolution 2015-2019 (BnU)



All four Global Flagship Brands increased volume in 2019, supported by a consistent investment strategy aimed at strengthening their equity, portfolio and geographic reach.

Winston's shipment volume growth exceeded 3%, breaking volume or share records in more than 25 markets, including Brazil, Germany, the Philippines, Romania and Turkey.

Camel grew more than 5%, achieving double-digit volume increase in 23 markets and setting share records in 11, such as France, Indonesia, Poland, Spain and Thailand.

LD, with a 6% volume increase, grew for the third consecutive year and was our fastest growing tobacco brand in 2019. LD broke volume records in 15 markets, including Canada, Taiwan and the U.S.

MEVIUS returned to growth, increasing approximately 1% versus 2018, primarily driven by the positive performance in Cambodia, Mongolia and Myanmar.

Price/Mix

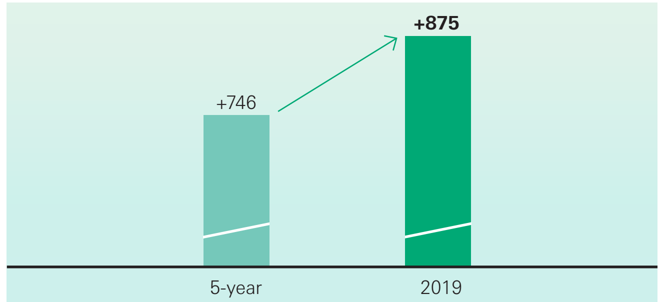
The strong equity of our brands in both cigarettes and Fine Cut, nurtured by focused investment, continued to play a pivotal role in enhancing JTI's pricing power.

Strong pricing was, once again, the key driver of our financial performance in 2019.

Including continued price and portfolio investments to strengthen our competitiveness and business agility, we recorded a total price/mix variance of US$875 million in 2019.

Importantly, price/mix was above our five-year average, demonstrating the continued resilience of the tobacco pricing model.

JTI Price/Mix Variance (USD MM)



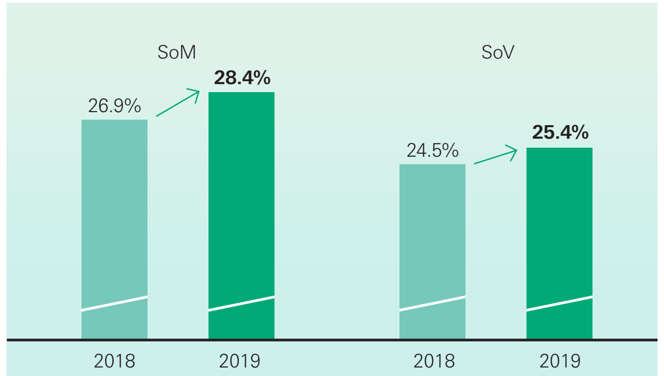
As a result of the investment efforts to expand and diversify our geographic footprint, pricing gains generated across our key markets, notably France, Russia, Turkey and the U.K., were complemented by an increasingly robust contribution from other markets, such as Germany, Iran and the Philippines.

Furthermore, emerging markets in Africa, Asia and the Middle East have gradually increased their price/mix relevance, reinforcing our confidence in the sustainability and flexibility of our growth model.

Share of Market

The solid performance of our Global Flagship Brands also enabled JTI to achieve significant share of market and share of value gains across its top-30 markets.

JTI Share in Top-30 Markets



Of a particular note was the progression recorded in Europe, where we enhanced our presence in both cigarettes and Fine Cut.

The continued share growth was primarily driven by our consumer-centric approach, strategically positioning our brands across key product categories and price segments.

Key Market of the U.K.

2019 was an excellent year for JTI in the U.K. market. We grew share across all product categories, breaking records through commercial initiatives aimed at injecting innovation, strengthening retail presence as well as ensuring price competitiveness.

We also expanded our presence in RRP, with Logic consolidating its leading position, supported by the growth of Compact in closed tanks.

Key Market of Russia

Our 2019 performance in Russia was robust. Share of market remained at 39%, underpinned by Global Flagship Brands and the improving momentum of the local heritage brands acquired with Donskoy Tabak.

Global Flagship Brands continued to gain share, exceeding the 25% threshold.

The resilient performance of Winston, still by far the first choice of Russian consumers, was complemented by the strong growth of LD.

All these achievements were realized while continuing to seize pricing opportunities, which remained strong despite the downtrading and volume contraction impacting the overall industry.

Reduced-Risk Products

Our seeding process in RRP continued at a sustained pace. Logic Compact, our most successful E-Vapor offering to date, was launched in additional 24 markets, which represents a significant increase versus the initial plan.

Leveraging consumer insights, commercial learnings and new capabilities acquired in recent years, we also started exploring opportunities in new categories.

In nicotine pouches, we launched Nordic Spirit in seven European markets with encouraging results.

Importantly, in the first half of 2020, we will introduce a Heated Tobacco product in Russia.

The device will be branded Ploom while related consumables will be endorsed by Winston, the number one tobacco brand in the market.

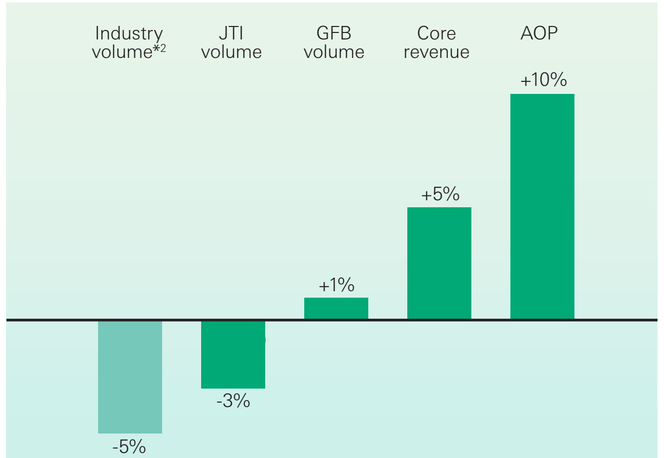
2020 Outlook

The 2020 outlook for the International Tobacco Business is built on robust assumptions. We will continue growing our share of market, significantly outperforming the tobacco industry volume trend in our top-30 markets.

Global Flagship Brands will play a key role in fueling share of market growth, as related volumes are anticipated to increase for the sixth consecutive year.

The pricing environment in conventional products remains robust. Price/mix variance is expected to be positive and to drive another year of strong core revenue and adjusted operating profit growth, at constant currency.

2020 Guidance*1



*1 2020 variance vs. prior year. Core revenue and AOP at constant currency
*2 Based on JTI's top-30 markets (cigarettes + Fine Cut)

We expect to achieve double-digit adjusted operating profit growth while continuing to invest in our people, brands and infrastructures.

We will ensure an adequate prioritization of resources throughout the business, supporting the growth of our conventional portfolio in markets that matter and stepping up our efforts in RRP.

The Transformation initiatives kicked-off in 2019 are gradually advancing, with the purpose of removing impediments to growth and building on our strengths, including new capabilities within the organization such as Global Business Service centers, Digital and Agile Teams.

These initiatives will significantly strengthen our business foundations, paving the way for more years of sustainable growth.

Business Review

Japanese Domestic Tobacco Business

Results for the fiscal year ended December 31, 2019

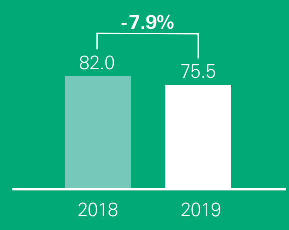
Core revenue declined 2.3%, as cigarette pricing gains were more than offset by the decline in cigarette sales volume and decrease in RRP related revenue. Adjusted operating profit decreased 10.4%, mainly due to an impairment loss and the top-line decline.

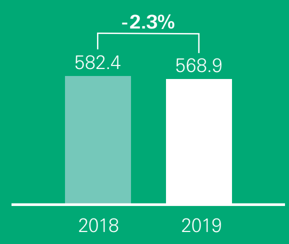
Key Highlights

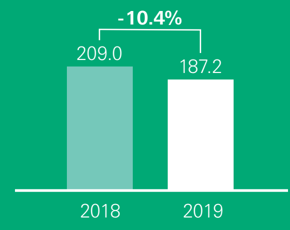
JT Cigarette Sales Volume
75.5 (BnU)
-7.9%
Year-on-Year Change

Core Revenue
568.9 (JPY BN)
-2.3%
Year-on-Year Change

Adjusted Operating Profit
187.2 (JPY BN)
-10.4%
Year-on-Year Change







In the Japanese domestic tobacco business, we continue to aim for profit generation by strengthening the top-line for both cigarettes and RRP. In cigarettes, we aim to recover share by leveraging our brand loyalty and expanding our product portfolio. For RRP, we will strive to build competitive advantage by further investing in R&D and marketing.

Junichi Fukuchi
Chief Executive Officer of Japanese Tobacco Business, Tobacco Business Planning, Tobacco Business

2019 Performance

In the Japanese domestic tobacco business, after the launch of Ploom TECH, we have launched 2 new RRP devices nationwide: Ploom TECH+ in June 2019, in the low-temperature heating category, and Ploom S in August 2019, in the high-temperature heating category. With these three devices set in place, 2019 was a year of realization, where we were able to find areas of improvement in RRP through continuous communication with our consumers. For cigarettes, we have taken measures to strengthen our product portfolio, including the introduction of little cigar products, in order to meet the consumers' changing needs.

Total Tobacco Industry Volume

The total tobacco industry volume* decreased about 4% year-on-year mainly due to a natural decline trend and the impact of price revision in October 2018.

Cigarette industry volume* decreased 6.3% year-on-year due to the decline in industry volume and expansion in the RRP category. Out of the entire tobacco industry volume, overall RRP market size* in Japan is estimated at approximately 23% (shipment basis).

* Source: JT estimate. Cigarette industry volume and cigarette share of market include little cigars which are classified as cigars as per the Tobacco Business Act in Japan as well as conventional cigarettes.

Volume and Financial

Core revenue decreased 2.3% to 568.9 billion yen, as cigarette pricing gains in the January-September period were more than offset by declines in cigarette sales volume and RRP-related revenue.

Adjusted operating profit decreased 10.4% to 187.2 billion yen, mainly due to an impairment of capsule manufacturing machines for low-temperature heating products and the top-line decline.

- JT cigarette sales volume decreased 7.9% year-on-year to 75.5 billion units due to the cigarette industry volume decline as well as our market share loss.
- JT RRP sales volume increased by 0.5 billion to 3.3 billion cigarette equivalent units.

Share Performance

For RMC, our share declined due to the intensified competition in the value segment.

- JT cigarette category share: 60.4% (1.0 percentage point decline from 2018)

For RRP, our share increased throughout the year, following the expansion of our RRP portfolio.

- JT RRP category share: approximately 9% (in convenience stores, roughly a 2 percentage point increase from 2018)

Industry Overview

We predict that the total tobacco industry volume will steadily decline at a low single-digit rate despite the planned full enforcement of the new indoor smoking regulation in April 2020. We expect the RRP industry volume to grow moderately compared to the rapid expansion in the previous year, bringing our share to over 25% of the total tobacco industry. As competition for share in this market intensifies, we expect that our competitors will continue to increase investments in this category in Japan. For cigarettes, the competition in the value segment, including little cigars, has been intensifying following the down-trading trend since the price revision in October 2018. Considering the tax hikes in line to take place in 2020 and 2021, we expect this down-trading trend to continue and the value segment to expand. In the midst of delisting our former third-class products and competitors continuously producing value segment cigarettes, we launched little cigar products in 2019 as a measure to prevent consumers from transferring out to our competitors.

This section is intended only to explain the business operations of the JT Group, not to promote sales of tobacco or vaping products or encourage smoking or vaping among consumers.

Strategy

In the RRP category, we aim to establish and maintain a competitive advantage in both high- and low-temperature heating categories by capturing shares from competitors in the high-temperature heating category, while continuing to develop the low-temperature heating category. As the areas of improvement made clear in 2019, we continuously work on the development of the devices, expansion of refill line-up and production of digital infrastructure for future diverse marketing. We will also strengthen our investment towards R&D, marketing and sales for our future growth, while continuously reducing costs in 2020.

We consider the cigarette category will remain an important profit generator going forward. While we expect cigarette demand to decline due to the planned tobacco tax hikes in 2020 and 2021, we will utilize appropriate pricing to maintain our profitability. We aim to recover our share by taking initiative throughout our product portfolio, mainly by maintaining our share of the premium+ and prestige segment products in addition to the launch of value segment products, which are to tackle down-trading.

2020 Outlook

The key to the growth of the tobacco business in the future is to generate profits in a sustainable manner in the Japanese domestic tobacco business. While we expect the short-term turnaround of the business to be challenging, we will continue to aim for profit generation by strengthening the top-line for both RRP and cigarettes.

Core revenue is expected to decrease by 5.1%, as the decrease in cigarette sales volume and the decline in RRP related revenue will more than offset the cigarette pricing gains and increase in RRP sales volume. Adjusted operating profit will decrease 9.2% due to the decrease in core revenue while we continue to increase the necessary investments. Despite the difficulty in terms of profitability, we recognize 2020 as a year for rebuilding the business foundation towards sustainable profit growth in the mid- to long-term.

This section is intended only to explain the business operations of the JT Group,
not to promote sales of tobacco or vaping products or encourage smoking or vaping among consumers.

Our Brand Portfolio

Our T-Vapor Products

Our Ploom brand offers our customers the choice to select the best product that meets their diverse preferences and lifestyles. Ploom S, our Heated Tobacco product, offers a superior taste of tobacco leaves; Ploom TECH, one of our Tobacco-Infused Vapor product, offers a variety of flavors; and Ploom TECH+, the other Tobacco-Infused Vapor product, offers a rich and powerful tobacco vapor.

Our Core Brands

In our Japanese market, we offer more than 15 brands in various product categories, including cigarettes, T-Vapor and little cigars. Some of these brands include MEVIUS, a market leader for more than 40 years; Seven Stars, which has been generating the highest revenue for 12 consecutive years;* Natural American Spirit; Winston; and Camel, which is growing into one of our major brands.

*JT estimate as of 2019

Tobacco Business Value Chain

R&D

Create Value through Innovation and Quality Improvement

- We are closely collaborating with all functions across the value chain to focus on fundamental research and product technology developments, using a global research platform. In particular, our R&D activities focus on these areas:
  - Strengthen product development and analytical capabilities in line with market needs while anticipating regulatory trends
  - Maintain existing products that comply with regulatory changes
  - Develop new technologies and improve production processes to maintain competitiveness and increase efficiency
  - Drive product innovation to enhance brand equity, including tobacco leaves, blends, filters, printing techniques and packaging
  - Develop RRP

Procurement

Ensure Stable Supply of Quality Tobacco Leaves

- We aim to strengthen our capability in ensuring a sustainable supply of tobacco leaves, which is one of the most important raw materials for our products.
  - Increase the proportion of leaves procured from our vertical integration bases in Africa, Brazil and the U.S.
  - Enhance the sustainability of tobacco farming by helping farmers to improve productivity as well as taking initiatives to support their communities
  - Maintain good relationships with external suppliers to ensure sufficient supply at competitive prices
- With regard to non-tobacco materials, we aim to mitigate the raising costs, mainly through investments in design enhancements and creating innovative products by effectively managing procurement lot-size.

Manufacturing

Support Top-line Growth through Delivering Quality Products

- We put great emphasis on improving product quality to meet consumer expectations towards innovative offerings. In addition, we consistently pursue an optimal manufacturing footprint, which ensures efficient and timely product deliveries to our markets.
  - Overcome manufacturing complexities that come with an increase in number of products, while ensuring high quality products and enhancing flexibility in the manufacturing process
  - Strengthen our ability for business continuity in times of emergencies
  - Pursue efficiency by managing cost increases and optimizing our manufacturing footprints

Marketing

Enhance Equity of Flagship Brands

- We focus our strategy on our core brands and we strive to enhance their equity through effective communications with consumers.
  - Support brand equity enhancement for our GFBs by appropriately allocating resources
  - Conduct effective marketing programs that comply with all applicable laws and regulations wherever we operate, as well as our Global Tobacco Marketing Principles

Sales & Distribution

Expand Product Availability by Leveraging Our Excellence in Sales Activities

- There are many channels for tobacco products such as supermarkets, convenience stores, street and train station kiosks, small independent retailers and vending machines. The importance of channels are different depending on each country. We increase availability of our products through various key channels by developing good relationship with retailers.
  - Strengthen relationships with key accounts, leveraging our trained sales forces
  - Apply most effective marketing initiatives suited for each market, taking market context into account such as channel development, consumers and competitors

Strategy and Business Review

Pharmaceutical Business

Results for the fiscal year ended December 31, 2019

Revenue declined by 22.3%, mainly due to the termination of license agreements for six anti-HIV drugs in Japan as well as lower overseas royalty income. Adjusted operating profit decreased 43.9% due to the revenue decline.

Key Highlights

Revenue

88.5 (JPY BN)

-25.5

Year-on-Year Change

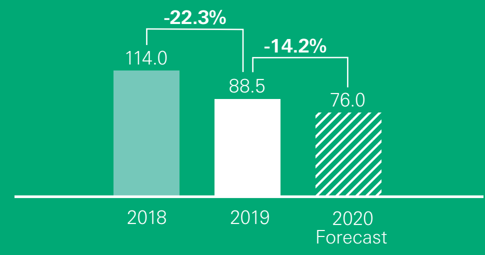
Adjusted Operating Profit

15.9 (JPY BN)

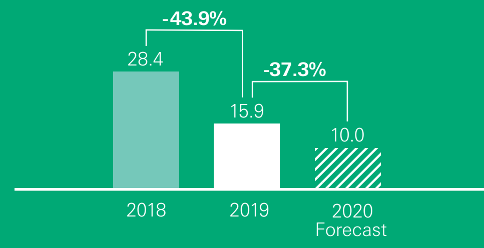
-12.5

Year-on-Year Change

Revenue (JPY BN)



Adjusted Operating Profit (JPY BN)



JT is committed to creating innovative, original drugs to support patients in the shortest time possible. We are proud to have received manufacturing and marketing approval for CORECTIM® Ointment 0.5%, for an indication of atopic dermatitis in Japan in January 2020. In addition, we filed a New Drug Application for JTZ-951 (generic name: enarodustat) for anemia associated with chronic kidney disease. We have been making steady progress in our R&D and will aim to contribute to sustainable profit growth.

Muneaki Fujimoto
President, Pharmaceutical Business

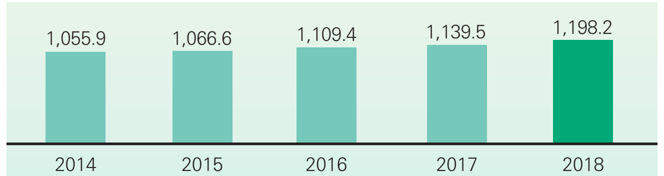
Industry Overview

The global pharmaceutical market continued to grow in 2018, reaching sales of approximately US$1,198.2 billion, an increase of 5.2% year-on-year,* due to increasing health awareness, population growth and development of public healthcare systems. While these factors result in a higher demand for more advanced drugs, governments are strengthening their control on drug prices by holding back medical costs, due to the rapidly aging society and fiscal deficits.

In order to control medical care expenses, the Japanese government has been promoting the use of generic drugs, leading the generic drugs market to expand in the Japanese pharmaceutical market. Additionally, a drastic reform of the drug pricing system will lead to a gradual price reduction each year from 2021, creating challenges for the industry. The drug price reduction rate in October 2019 was 2.4% on average, due to a consumption tax increase.

Our pharmaceutical business competes with not only numerous Japanese domestic companies, but also with foreign companies, including global mega pharma and start-up companies. We will continue to promote R&D and seek optimum timing to license out our compounds in order to accelerate our R&D and swiftly provide new drugs to patients around the world.

Worldwide Pharmaceutical Market* (USD BN)



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Our Performance and Outlook

- In-house development (2019 progress)
  - Entered the clinical trial stage:
    JTE-761 (RORγ antagonist) – Phase 1 (Overseas)
  - New Drug Application filed (Japan):
    JTE-052/delgocitinib (JAK inhibitor),
    JTZ-951/enarodustat (HIF-PH inhibitor)

For further details, please visit JT.com.

We steadily made progress in our R&D in 2019, as we had a new compound entering the clinical stage and two New Drug Applications filed in Japan, in spite of having a challenging year. Challenges included a decrease in revenue and adjusted operating profit due to the termination of exclusive license agreements for six anti-HIV drugs in Japan as well as lower overseas royalty income.

It was also a fruitful year for license activities as our group company, Torii Pharmaceutical Co., Ltd. (Torii), entered into a license agreement with BioCryst Pharmaceuticals, Inc. for exclusive marketing rights in Japan to the plasma kallikrein inhibitor BCX7353 in November. In the following month, we also signed an exclusive license agreement with Shenzhen Salubris Pharmaceuticals Co., Ltd. for the development and commercialization in Mainland China, Hong Kong, Macau and Taiwan of JTZ-951 (enarodustat).

While we expect 2020 to remain challenging, we will continue aiming towards contributing to sustainable profit growth. We started the year with receiving manufacturing and marketing approval for CORECTIM® Ointment 0.5% (generic name: delgocitinib), a Janus kinase (JAK) inhibitor, for an indication of atopic dermatitis in Japan. In addition, Torii has restructured its business and, in line with plans, started operating under the new structure in late 2019.

Our Sustainability Strategy

Our pharmaceutical business aims to create innovative, original drugs to support patients in the shortest time possible. As this business has a direct impact on human health and life, we not only strictly comply with all laws, regulations and industry standards, but we guide ourselves with a strong sense of ethics and responsibility. This is particularly the case in areas such as clinical trials and drug marketing, as well as animal experiments and managing chemical substances.

We set five specific targets for three focus areas in 2019, which we consider are essential for the sustainability of our business and for our stakeholders. For more details, please refer to page 28. The focus areas and the specific targets are available at JT.com as well.

R&D that Ensures Ethical Integrity

We carry out our research activities in an ethical manner and comply with all applicable laws, regulations and industry standards. We continue to strengthen our R&D capability which enables us to create innovative drugs by focusing our resources on specific therapeutic areas. In 2019, the JT Group invested 33.2 billion yen in our R&D activities.

We have established internal policy on animal experiments based on government legislation. Our Institutional Animal Care and Use Committee ensures that we follow the 3R concept: **Replacing** laboratory animals with other research materials where possible; **Reducing** the number of animals used; and **Refining** experiments to prevent animals from suffering unnecessary pain and distress.

We carry out periodic internal audits and assessments to ensure that we comply with this policy. Our practices are accredited by the Japan Health Sciences Foundation, an external authority that lists all accredited facilities on its website.

Quality Assurance of Pharmaceutical Products Production

The JT Group establishes a sustainable supply chain that delivers high quality products to patients. Our products marketed in Japan are mainly produced and distributed by Torii, while simultaneously outsourcing to contract manufacturers in order to build an efficient manufacturing structure.

We have also developed our own guidelines on how to conduct annual audits to ensure that our production methods fully comply with government recommendations. We began implementing these inspections in selected factories in 2017 and no issues were identified. We have been steadily expanding the scope of our guidelines since 2018, and they now cover 100% of our own factories* and contracted factories. We will continue to operate under these guidelines.

* In 2020, the JT Group will stop manufacturing operations of its pharmaceutical products in its own facilities and outsource all of them to contracted factories.

Responsible Promotion of Drugs

We formulate our own standards on the ethical promotion of prescription drugs, based on the guidelines on the sales information provision activities, issued by the Ministry of Health, Labor and Welfare. Torii's Medical Representatives (MRs) provide and collect information on pharmaceutical drugs to/from medical professionals appropriately and regularly participate in training programs to ensure adherence to these guidelines.

Transparency of Partnerships

In order to develop drugs that are more effective, we build partnerships with research institutes, universities and medical institutions. When we make financial contributions to our partners, we strive to ensure transparency by disclosing these payments on our website.

Strategy and Business Review

Processed Food Business

Results for the fiscal year ended December 31, 2019

Revenue decreased 1.7% as solid performance in the main staple food* category was offset by the decline in sales of products with lower profitability. Adjusted operating profit increased by 1.3 billion yen mainly driven by the positive contribution from pricing, product portfolio optimization as well as cost reduction initiatives, despite lower revenue and increases in raw material and distribution costs.

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

Key Highlights

Revenue

158.6 (JPY BN)

-2.8

Year-on-Year Change

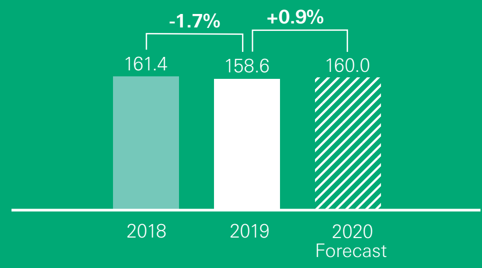
Adjusted Operating Profit

5.4 (JPY BN)

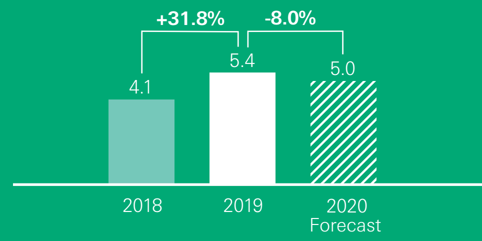
+1.3

Year-on-Year Change

Revenue (JPY BN)



Adjusted Operating Profit (JPY BN)



We have a mission of delivering safe, high quality food to our customers through our three businesses: frozen and ambient food, seasonings and bakery. In frozen and ambient food, our core business, we strive to achieve revenue growth and aim to increase our contribution to the Group's mid- to long-term sustainable profit growth, while optimizing manufacturing capabilities and enhancing the profitable product portfolio.

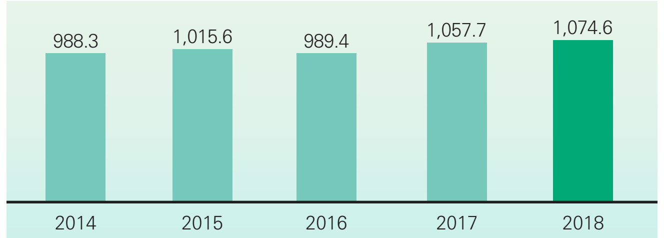
Hiromasa Furukawa
Food Business

Industry Overview

We expect the Japanese processed food industry to continue to grow as lifestyles change. Frozen foods can help meet the diverse needs of consumers with its abundant variety and convenience in recreating freshly served taste.

In 2018, annual consumption of frozen food in Japan increased 1.4% to 2,893,299 tons year-on-year, a record high. Domestic market size on a consumption basis, including imports, grew 1.6% year-on-year to 1,074.6 billion yen, exceeding one trillion yen for the second consecutive year.*

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



*Source: Japan Frozen Food Association

Our subsidiary, TableMark Co., Ltd., is competing against major players like Maruha Nichiro, Nichirei Foods, Ajinomoto Frozen Foods and Nippon Suisan Kaisha as well as a multitude of mid- or small-scale producers, although we are starting to see gradual segregation of competition within the industry according to the product categories these competitors respectively own.

These competitors are not the only ones we need to keep an eye out on. We believe it is necessary to monitor trends in sales channels amid the expansion of private brand products by various distribution companies; and the reorganization of wholesale entities. We also need to be aware of the continuing risk of price fluctuations in raw materials due to global food shortages.

Our Performance and Outlook

Strategy

- Strengthen our product branding, particularly for staple food products, through combining product development and consumer needs
- Strive to develop high value-added products to respond to changing consumer needs
- Mitigate the impact of rising raw material costs

Our business primarily engages in frozen and ambient foods, notably staple food products; seasonings including yeast extracts and oyster sauce; and products for bakery chain outlets mainly in the Tokyo metropolitan area.

We continue to take measures to improve profitability. In 2019, revenue decreased as the solid performance of the main staple food category was offset by the decline in sales of products with lower profitability. On the other hand, adjusted operating profit increased by 1.3 billion yen mainly driven by the positive contribution from pricing, product portfolio optimization as well as cost reduction initiatives, despite lower revenue and increases in raw material and distribution costs.

In 2020, we expect raw material and distribution costs will continue to increase. We will aim to achieve top line growth while enhancing optimal manufacturing capabilities and strengthening the profitable product portfolio in our core frozen and ambient food.

Our Sustainability Strategy

Our mission is to deliver safe, high quality food products to our consumers.

In 2019, we set eight specific targets for three focus areas which we consider to be essential for the sustainability of our business and for our stakeholders. For more details, please refer to page 28. The focus areas and the specific targets are available at JT.com as well.

Delivering Safe, High Quality Products

Our processed food business has 32 factories, including the one scheduled to operate from 2020, which produce a variety of food products, from frozen foods to seasonings and bakery products. We are dedicated to delivering safe and high quality food products to our consumers by thoroughly managing food safety based on the four priorities of food safety, food defense, food quality and food communication.

Food Safety Standards

- 31 of these factories inside and outside Japan have achieved FSSC 22000 certification, which is recognized by the Global Food Safety Initiative, the food industry's global body that promotes food safety management. Our newest factory, scheduled to operate from 2020, is also progressing towards this certification.
- All factories that are contracted to manufacture frozen food products on our behalf have also achieved the ISO 22000 or FSSC 22000 certification.

Food Defense Practices

- We protect our manufacturing processes and products from intentional contamination.
- We apply robust food defense guidelines across the supply chain, both in our own factories and our contracted factories; these guidelines are referred to during our annual audits.
- We strengthen our defense mechanisms against deliberate contamination by optimizing factory cameras and enhancing the way we manage chemical substances.

Enhancing Food Quality

- We ensure that all of our employees have deeper understandings of quality improvement through various initiatives conducted by each factory and customized e-learning materials.
- We listen to our consumers' suggestions for improving product quality, and swiftly share these with our factories and operations.
- We respond to our consumers' recommendations through our internal Quality Improvement Committee. This Committee is comprised of representatives from different divisions, including Product Development, Manufacturing, Distribution, Sales, Quality Control and our Consumer Call Center.
- Our consumer care service management system is compliant with ISO 10002, the international standard for customer satisfaction and complaints handling.

Food Communication

- We respond to consumers' requests to obtain information and disclose the precise factory where food products were made, or the country of origin the main ingredients came from.
- In order to ensure food safety, we utilize a system that records information about our products at every stage of the process, from the raw materials and production to processing, distribution and sales. This allows us to trace our product to any point, if necessary.
- We provide toll-free numbers on our product labels, which consumers can call to obtain information.

Message from the CFO

While maintaining a strong financial base, we aim for sustainable profit growth over the mid- to long-term and improved shareholder returns.

Naohiro Minami
Representative Director and Executive Vice President, Chief Financial Officer

2019 Financial Results

Revenue on a reported basis decreased 1.8% year-on-year, mainly due to the decline of cigarette sales volume in the Japanese domestic tobacco business, currency headwinds in the international tobacco business, impact from the termination of the license agreements for six anti-HIV drugs in Japan and lower overseas royalty income in the pharmaceutical business.

Adjusted operating profit decreased 13.4% mainly due to the decline in revenue. Excluding the impact of foreign exchange, adjusted operating profit at constant FX increased by 0.9%. This is the main indicator we use to evaluate our performance. The change was driven by the growth of the total tobacco business, which combines the Japanese domestic tobacco and international tobacco businesses, offsetting the decline in the pharmaceutical business.

Operating profit declined by 11.1% to 502.4 billion yen, mainly due to the decline in the consolidated adjusted operating profit, an increase in amortization related to acquisitions, restructuring costs in the international tobacco business and a decline in proceeds from sales of real estate assets, despite the one-time compensation gain related to the termination of license agreements for six anti-HIV drugs in the pharmaceutical business.

Profit also decreased by 9.7% to 348.2 billion yen, mainly due to the decline in operating profit and higher financing costs.

Free Cash Flow (FCF) reached 404.2 billion yen, driven by the stable cash generation ability of our business operations and supported by a one-time gain in 2019. Year-on-year, this represents an increase of 298.6 billion yen as the cash outlay, related to acquisitions in Bangladesh and Russia in 2018, has not recurred.

2020 Financial Forecast

Revenue, on a reported basis, is forecast to increase by 0.2%, as overall tobacco business growth will offset lower overseas royalty income in the pharmaceutical business.

Adjusted operating profit will decrease by 2.5% to 503.0 billion yen, as the overall growth of the tobacco business will be more than offset, mainly by the decline in the pharmaceutical business, costs related to headquarters transfer in 2020 and IT system investment. Adjusted operating profit at constant FX is expected to be stable year-on-year.

Operating profit is expected to decline by 6.2% to 471.0 billion yen. Positive impacts include the absence of restructuring costs in 2019 in the international tobacco business and the anticipated proceeds from sale of the headquarters building. These, however, will be more than offset by the decline in the consolidated adjusted operating profit and the non-recurrence in 2019 of a one-time compensation gain in the pharmaceutical business.

Profit is forecast to decrease 12.4% to 305.0 billion yen due to decline in operating profit and a higher effective tax rate relative to 2019, which was reduced by a one-time factor.

Regarding FCF, we expect continuous stable cash generation ability of our business operations, although FCF is expected to decrease by 34.2 billion yen to 370.0 billion yen mainly due to the non-recurrence of the one-time gain in 2019.

Shareholder Return Policy

We give the highest priority to business investments, which contribute to sustainable profit growth in the mid- to long-term and seek a balance between profit growth through business investment and shareholder returns under our resource allocation policy. Our policy remains unchanged, aiming to deliver stable, consistent growth in dividend per share based on the mid- to long-term profit growth outlook while maintaining a strong financial base. In addition, we continue to consider share buybacks in light of the outlook for our business environment and financial condition.

In determining the dividend, we are taking into account the profit level since 2019, following FX volatility in the past several years. However, the mid- to long-term growth rate outlook for adjusted operating profit at constant FX remains our primary indicator. Our mid- to long-term target remains the same; we aim for mid to high single digit growth over the mid- to long-term for adjusted operating profit at constant FX.

On the other hand, adjusted operating profit at constant FX in 2019 was below our target, as is the forecast for 2020. Furthermore, profit, from which dividends stem, has been trending downward due to currency headwinds over several years.

In addition, although we plan to meet our mid- to long-term target for the adjusted operating profit at constant FX in our Business Plan 2020, the uncertainty over profit remains high due to FX volatility and potentially some one-time factors.

Given these circumstances, our annual dividend per share for 2019 has been set at 154 yen, as announced at the beginning of 2019. For 2020, we plan to offer an annual dividend per share of 154 yen, unchanged from the previous year, to ensure stability of future dividends.

Investor Relations Activities

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

Our dedicated IR teams based in Tokyo and Geneva engages in daily dialogue with sell-side analysts and institutional investors on not only earnings announcements, but also ESG. We had approximately 500 meetings in 2019.

Our executive management team, including the president, executive vice president or senior vice president also visits domestic and overseas institutional investors for meetings. This includes visits to major cities in North America, Europe and Asia.

Moreover, we attend conferences held by brokers, both in Japan and overseas, to meet with sell-side analysts and institutional investors. We hold several briefing sessions for non-institutional investors every year.

In 2019, we held an RRP-manufacturing factory tour to respond to a request from sell-side analysts and institutional investors.

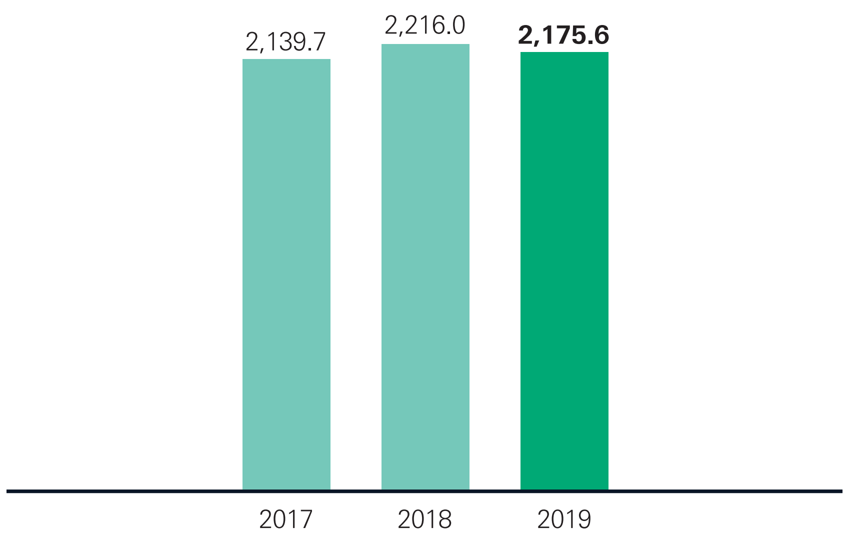
Going forward, we will continue to carry out IR activities that will meet the needs of shareholders and institutional investors.

Key Performance Indicators

Financial Performance Review

Revenue

(JPY BN)



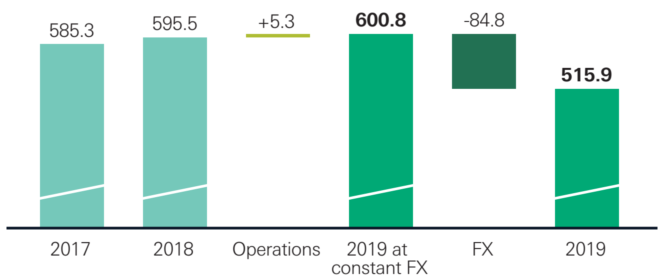
JPY **2,175.6** BN

1.8% decrease year-on-year

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

Adjusted Operating Profit

(JPY BN)



13.4% decrease to

JPY **515.9** BN (reported basis)

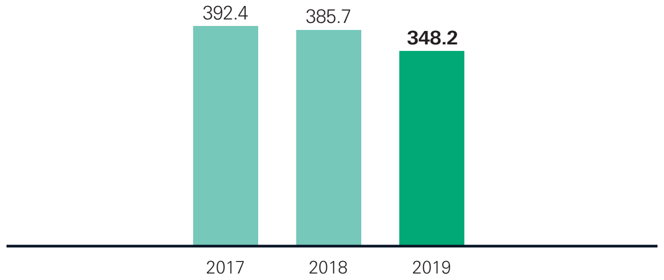
0.9% increase at constant currency

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

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

Profit

(JPY BN)



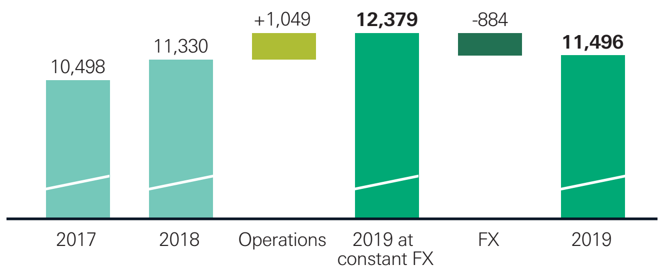
JPY **348.2** BN

9.7% decrease year-on-year

Profit attributable to owners of the parent company.

Core Revenue

International Tobacco Business (USD MM)

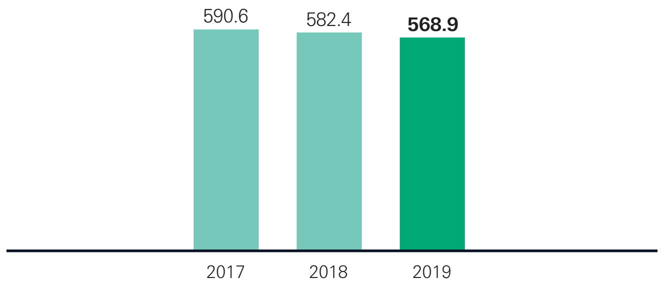


9.3% growth to

USD **12,379** MM (at constant currency)

U.S. dollar-based core revenue for the international tobacco business. Includes waterpipe tobacco and RRP, but excludes revenue from distribution, contract manufacturing and other peripheral businesses.

Japanese Domestic Tobacco Business (JPY BN)



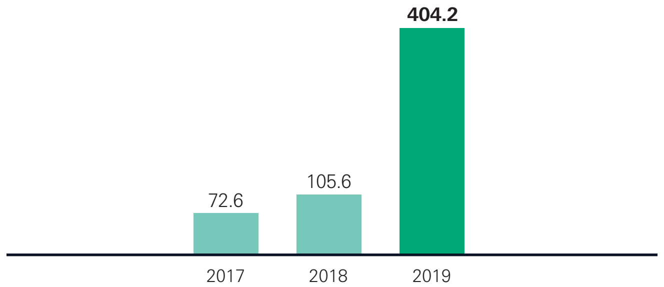
2.3% decrease to

JPY **568.9** BN

Core revenue for the Japanese domestic tobacco business. Includes revenue from domestic duty free, the China business, little cigars and RRP, but excludes revenue from distribution of imported tobacco in the Japanese domestic tobacco business, among others.

Free Cash Flow

(JPY BN)



JPY **404.2** BN

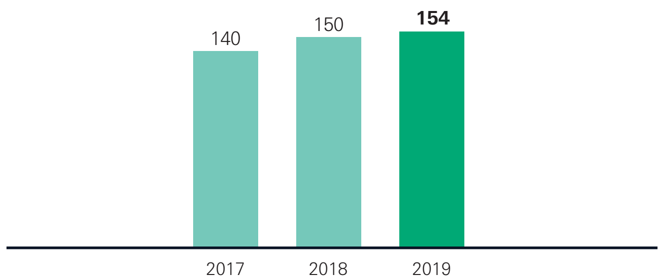
298.6 BN increase year-on-year

Free Cash Flow is sum of cash flows from operating activities and investing activities, but excludes the following items:

- From operating cash flow: depreciation from lease transactions, interest received, dividends received, interest paid and income taxes related to these items excluding lease transactions
- From investing cash flow: purchase of investment securities (both short-term and long-term), payments into time deposits, proceeds from sale or redemption of investment securities (both short-term and long-term), proceeds from withdrawal of time deposits and other investing activities not for business operation purposes

Dividend Per Share

(JPY)



4 yen increase to

154 yen

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

Non-Financial Performance Review

Dow Jones Sustainability Indices

We are very proud to be listed in the Asia-Pacific Dow Jones Sustainability Index for the sixth consecutive year, moving up to second place in the tobacco industry.
Highlights include:

- Improved scores and ranking across all economic, environmental and social dimensions
- Industry leader in the social dimension, with full scores in Corporate Citizenship and Philanthropy and Social Reporting
- Perfect scores of 100 also in Environmental Reporting and Climate Strategy
- In the economic dimension, we scored 100 in Materiality
- Recognized with SAM Bronze Class 2020 ranking and as a SAM Industry Mover 2020 for the first time

See The Sustainability Yearbook 2020 for more details.

MEMBER OF
Dow Jones Sustainability Indices
In collaboration with SAM

RRP

At the end of 2019, our RRP portfolio was present in **28** countries, with a choice of three tobacco vapor offerings (T-Vapor) and five types of e-cigarettes (E-Vapor).

Anti-Illicit Trade

We provided information to law enforcement that led to:
70+ counterfeit tobacco factories and storage locations raided
3.2 billion+ illegal cigarettes seized

Human Rights

We completed **9** Human Rights Impact Assessments in high-risk countries.

ARISE*

6,186 children off farms and into schools through the ARISE program

*Achieving Reduction of Child Labor in Support of Education

Agricultural Labor Practices

Of all the entities that provided us with tobacco leaf, either directly or through leaf merchants,
81% reported against Agricultural Labor Practices.

Community Investment

50 (USD MM) invested in our communities
10,256 employees volunteered **33,055** hours on company time
3,640 employees spent **22,841** hours of their own time taking part in volunteering activities

Human Resources

Our international tobacco business was certified as a Global Top Employer for the sixth consecutive year. We were certified as a Top Employer by the Top Employers Institute in **63** countries around the world. In Japan, JT was selected as a "White 500" company and achieved Gold status in the Pride Index Report of Japanese employers for the fourth consecutive year.

top EMPLOYER GLOBAL 2020
CERTIFIED EXCELLENCE IN EMPLOYEE CONDITIONS

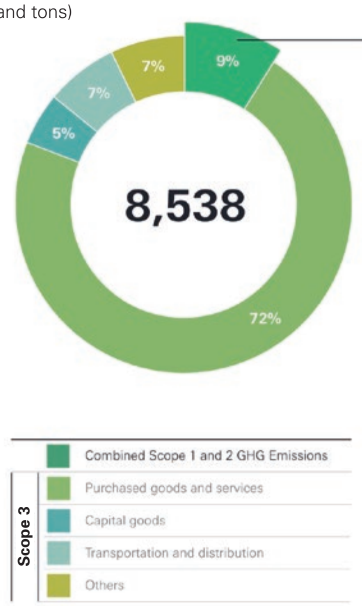
Compliance

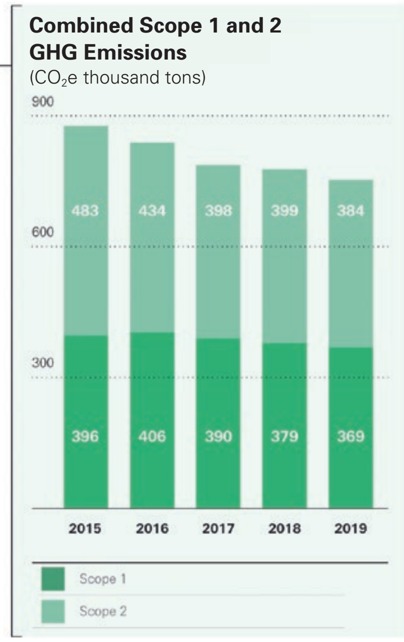
99.7% of our employees in our Japanese operations completed online training on the Code of Conduct.
30,000 employees attended training on our Code of Conduct in our international tobacco business.

Environment

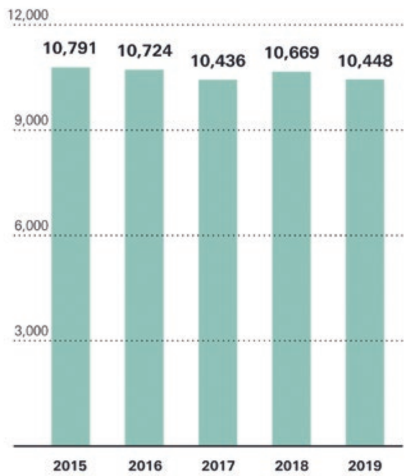
We strive to further reduce environmental impacts, focusing on the most significant environmental risks and opportunities for our business and stakeholders. Learn more about our Environment data at JT.com.

GHG Emissions in Our Value Chain in 2019
(CO_2e thousand tons)

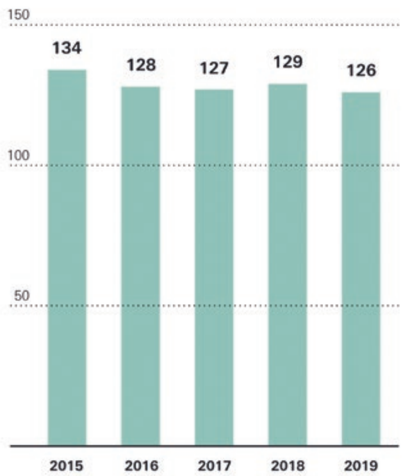




Water Withdrawal (Thousand m³)



Waste Generated (Thousand tons)



Note: The data have been restated in line with our recalculation policy. Learn more about our calculation methodology at JT.com.

This year, we regained our spot on CDP's prestigious "A List" for climate change, putting us in the top 2% of companies achieving A list status. We are also very proud to have achieved A list status for water security and to be recognized as a leader in supply chain engagement, both for the first time.

CDP A LIST 2019 CLIMATE | CDP SUPPLIER ENGAGEMENT LEADER 2019 | CDP A LIST 2019 WATER

Learn more about our non-financial data scope annotations at JT.com.
Any data without annotated scope in this report covers the entire JT Group including subsidiaries.

Risk Factors

The JT Group is a leading global tobacco company, selling products in more than 130 countries/regions. The Group is also present in pharmaceutical and processed food businesses. Due to our business characteristics and changing business environments, we are exposed to various risks.

Under our risk management framework, each division carefully monitors the development of events that may adversely affect our business. This enables us to identify the risks that may inflict a loss and take countermeasures against them. When risks are materialized, we promptly respond to minimize the impact.

We utilize internal guidelines for risk assessments, estimating the possibility of risk materializing and magnitude of potential impact that the risks have throughout each of our businesses. Based on these assessments, we report any material risks, which might have a significant impact on our business operations and financial results, to the CEO and decision is taken for implementation of countermeasures.

The following is not an exhaustive list or explanation of all risks which we may face. All the risk factors potentially have a material impact on our business operations and financial results.

Please read this chapter together with the forward-looking statements of this report.

1 Substantial or Repeated Tax Increases

Tobacco products are subject to excise or similar taxes in addition to consumption tax and value-added tax. Excise taxes are increased in many countries, including Japan, as a result of their governments' discussion regarding securing financial income as well as promoting public health. In general, value-added tax tends to increase as well. We revise our prices taking into account the expected volume decline after the price revision, in addition to fully passing on any tax increase to tobacco products. A tax increase within a reasonable range is manageable through such a price increase as well as our efforts to support the top-line and pursue cost efficiency. Most governments take a rational approach on tax increases, as they are aware that substantial or repeated tax increases can reduce their tax revenue. However, we have experienced tax increases in some markets that had significant impact on our business in the past.

Risk Description and Potential Impact

A substantial or repeated tax increases on tobacco products could result in lower consumption and increased illicit trade. In addition, this could accelerate down-trading to products in the lower-priced category, resulting in a decline of our shipment volume, revenue and profit.

Key Measures to Address the Risk

- Promote the understanding of relevant authorities that substantial or repeated tax increases do not necessarily serve their purpose.
- Optimize our product portfolio to meet volatile consumer preferences.
- Enhance our geographical portfolio to mitigate the negative impact of such tax increases in applicable markets.
- Further improve cost efficiency to secure our profitability.
- Adequately set each product price according to each market in order to minimize the impact of tax increases.

2 Increase in Illicit Trade

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

Illicit trade tends to increase in a market after substantial or repeated tax increases. Regulatory actions against ingredients and packages could also trigger the acceleration of illicit trade because it could make counterfeit manufacturing easier and detection of illicit products more difficult.

Risk Description and Potential Impact

An increase in illicit trade could reduce legitimate industry volume, leading to a decline in our shipment volume, revenue and profit. In addition, any costs associated with combatting illicit trade will cause more pressure on our earnings. Furthermore, it is possible that low quality counterfeits and improperly handled, smuggled products can cause damage to the credibility of genuine brands as well as the reputation of their owners.

Key Measures to Address the Risk

- Engage with governments, regulatory bodies and law enforcement agencies to eradicate illicit trade.
- Ensure we conduct business transactions with reputable business partners in accordance with our rigorous compliance policy.
- Raise awareness among our consumers of the negative consequences of purchasing illegally traded products.

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

Under this agreement signed in 2007, we contributed an annual US$50 million in the first five years from its execution and have been contributing an annual US$15 million in the subsequent ten years. This financial contribution is to support anti-smuggling and anti-counterfeiting initiatives led by the EU and its Member States.

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

We have been implementing and operating our Track and Trace system as part of our compliance policy for more than a decade; initially, as a self-regulation measure and later, to meet legal requirements in some countries/regions. We are complying with the regulations as of entry into force.

Tobacco Business: Regulatory Environment and Illegal Trade

3 Tightening Tobacco Regulations

The tobacco industry is highly regulated in various aspects, including advertising and promotion, and these regulations could influence our business performance and financial results.

For example, we may incur additional costs in order to comply with ingredients and packaging requirements. Furthermore, these regulatory attempts could lead to an increase in illicit trade and negatively influence our legitimate business. More prohibitive regulations on communication with consumers may also adversely affect our top-line performance.

As a responsible company, we comply with all of the laws and regulations where we operate. We believe that laws and regulations should differ in each country, reflecting their own legal, social and cultural background. Therefore, we endeavor to hold constructive dialogues with governments and regulators for a reasonable and balanced approach towards tobacco regulation.

Risk Description and Potential Impact

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

Key Measures to Address the Risk

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

Regulation and Other Relevant Laws

4 Competition

The JT Group competes fiercely in both Japanese domestic and overseas tobacco markets with our competitors.

In the Japanese domestic tobacco market, the liberalization of imported tobacco products took place in 1985, followed by the suspension of its custom duties in 1987. Since then, competition has intensified each year due to aggressive sales activities by competitors, diversified consumer preferences and rapid expansion of the RRP market.

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

Market Share can fluctuate due to a number of factors, including changes in regulations, consumer preferences and the economic conditions of each market, as well as competitors' pricing strategies or brand equity. Moreover, any temporary factors, such as new product launches and the associated promotional activities, can influence market share in the short-term.

Risk Description and Potential Impact

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

Key Measures to Address the Risk

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

5 Country Risks

The JT Group, especially the tobacco business, has consistently expanded our earnings base to secure long-term growth by making acquisitions, entering new markets as well as organic growth in each market. However, these geographical expansions may increase our exposure to country risks. In any market where we operate, we may face political, economic or social turmoil, which may negatively affect our operations and financial results.

Risk Description and Potential Impact

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

Key Measures to Address the Risk

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

6 Currency Fluctuations

As the JT Group operates globally, it is exposed to risks associated with currency fluctuations.

The reporting currency of our consolidated financial statements is in Japanese yen, while the financial statements of our international subsidiaries are reported in other currencies such as the Russian ruble, euro, British pound, Taiwanese dollar, U.S. dollar and Swiss franc. Therefore, exchange rate fluctuations of foreign currencies against the Japanese yen influence our reported financial results. As for the financial reporting of the international tobacco business, JT International Holding B.V. consolidates the financial results of the international tobacco subsidiaries and reports its consolidated financial statements in U.S. dollars. We often communicate the financial performance of our international tobacco business in U.S. dollars, which is affected by exchange rate fluctuations against the U.S. dollar. In principle, we do not hedge the risks that arise from the translation of financial statements. However, we hedge against risks that arise when equity denominated in each functional currency is translated into Japanese yen to be consolidated by using foreign currency-denominated, interest-bearing debts and part of these are designated as net investment hedges.

In addition, many Group subsidiaries make transactions in currencies other than their reporting currencies for day-to-day operations. Such transactions also involve the risk of exchange rate fluctuations. We mitigate these transaction risks through hedging activities; however, it is not possible to completely eliminate them.

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

Risk Description and Potential Impact

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

Key Measures to Address the Risk

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

7 Instability in the Procurement of Key Materials

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

Risk Description and Potential Impact

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

Key Measures to Address the Risk

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

8 Unfavorable Developments in Litigation

JT and some of its subsidiaries are defendants in lawsuits filed by plaintiffs seeking damages for harm allegedly caused by smoking, the marketing of tobacco products or exposure to tobacco smoke. As of December 31, 2019, 20 smoking and health-related cases were pending, in which one or more members of the JT Group were named as the defendant; or for which JT may have certain indemnity obligations pursuant to the agreement for matters such as JT's acquisition of RJR Nabisco Inc.'s non-U.S. tobacco business. JT and its subsidiaries, who are defendants in such lawsuits, believe that we have valid grounds to defend the claims in such lawsuits; however, we cannot predict the outcome of any pending or future litigation.

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

Risk Description and Potential Impact

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

Key Measures to Address the Risk

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

Litigation

9 Natural Disasters

The operations of the JT Group may be disturbed by natural disasters such as earthquakes, typhoons, floods, volcanic eruptions and others. Japan is one of the most important markets for our businesses, yet is subject in particular to various natural disasters. The Great East Japan Earthquake in 2011 was devastating. The impacts on JT Group included casualties among our employees, physical damage to our factories and supply shortages of certain tobacco product materials. This forced our tobacco business to temporarily suspend product shipment and limit shipment volume for an extended period.

We have developed a Business Continuity Plan, including the optimization of the global supply chain, in order to minimize the impact of such disasters.

Risk Description and Potential Impact

Natural disasters could cause damage to our business as well as our value chain, leading to disruption of our business and negatively impacting financial results.

Key Measures to Address the Risk

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

10 Climate Change

Climate change caused by global warming can trigger abnormal weather conditions that could cause various damages. These include flooding, landslides, severe heat, heavy snowfall and drought due to unseasonable weather changes, water resources depletion and loss of biodiversity.

Risk Description and Potential Impact

Climate change could adversely affect our results of operations by damaging the JT Group and our value chain.

Key Measures to Address the Risk

- Work to reduce environmental impact by reducing greenhouse gas emissions, using water resources efficiently and reducing waste.
- Establish a system to better understand the impacts of climate change on businesses and respond appropriately, such as formulating a scientifically based plan to reduce greenhouse gas emissions (SBT) in the JT Group Environment Plan 2030 and investigating scenario analyses.

Improving Our Environmental Impact

Regulation and other Relevant Laws

Tobacco Business

Regulation in International Markets

The regulatory environment for tobacco is getting stricter year by year, in the wake of the Framework Convention on Tobacco Control (FCTC), which came into force in February 2005. The Japanese government ratified the framework in June 2004.

The purpose of the FCTC is to control continuously and substantively the proliferation of smoking. Its provisions include price and tax measures; non-price measures to reduce demand (including protection from passive smoking, testing and measuring the contents and emissions of tobacco products and their information disclosure, product packaging and labeling, regulations on tobacco advertising, promotion and sponsorship), and measures related to the reduction of tobacco supply (including prevention of illicit trade and prohibition of sale of tobacco products to minors). All Parties to the FCTC are obligated to develop, implement, periodically update and review strategies, plans and programs for tobacco control. However, each party, has a right to determine the content, scope and specific implementation method of their own tobacco control.

After coming into force, the Parties of FCTC continue their discussions through regularly holding the Conferences of the Parties (COP) in order to develop the protocols (for which additional ratification, acceptance, accession and other are required to the FCTC Parties) and guidelines in view of implementation of each FCTC provision.

Specific regulations are also undertaken in each country. For example, Russia, a key market of the JT Group, enacted the comprehensive tobacco control law in February 2013 and has gradually been implementing it since June 2013. The law includes a retail display ban; restrictions on sales of tobacco products in certain retail stores; a ban on advertising, sponsorship and promotions; the introduction of minimal pricing; a ban on smoking in public places; and anti-illicit trade measures.

In addition, the EU revised the EU Tobacco Product Directive (EU TPD) announced in July 2001 and it entered into force in May 2014. The revised Directive includes the tightening of packaging and labeling regulations; restrictions on the use of additives including menthol for cigarettes and Fine Cut; regulations related to electronic cigarettes; and anti-illicit trade measures. Each member state has legislated their national laws based on the revised Directive.

Furthermore, the Australian government introduced plain packaging in December 2012, which prohibits displaying logos and brand images on tobacco packages. The regulation only allows product names to be displayed in the prescribed color, font, font size and font color. Various countries including France, U.K. and others have also introduced and legislated similar regulations, while other countries has been discussing its implementation.

With regards to the regulation in those new category products including RRP, new standards or frameworks for reduced risk claims have been established in a few countries such as the U.S. and European countries. In order to gain official approval from governments, activities in developing reduced risk claims have been intensified among major global tobacco manufacturers. At the same time, some countries have adopted different regulatory initiatives to these products. For instance, the U.S. newly implemented the prohibition of the sale of certain flavored E-Vapor products in February 2020. Moreover, some governments have applied the same level of regulations to these products as those to conventional tobacco products. However, we understand that no substantive global trend on regulations has been observed yet in this new product category.

Regulation in the Japanese Domestic Market

The Tobacco Business Act and its related acts, statutes, and voluntary rules regulate the sale and promotion activities of tobacco products in Japan. These regulations include the placement of caution statements on tobacco product advertisements and packages that urge caution over the relationship between the product consumption and health (hereinafter referred to as the Caution).

The amendment of Ordinance for Enforcement of the Tobacco Business Act (hereinafter referred to as the amendment of the Tobacco Ordinance) in November 2003 included the wording of the Caution on tobacco product packages. All tobacco products sold in Japan have complied with the amended act since July 2005. In addition, the Japanese Minister of Finance has indicated a Guideline for Advertising of Tobacco Products (hereinafter referred to as the Advertising Guideline) based on the Tobacco Business Act, Article 39 (caution statements) and Article 40 (advertising regulations). The Advertising Guideline was amended in March 2004 in accordance with the amendment of the Tobacco Ordinance.

Tobacco Institute of Japan (TIOJ) has voluntary rules regarding the packaging, advertising and sales promotion activities for tobacco products (hereinafter referred to as the Tobacco Rules) as per the Tobacco Ordinance. All member companies, including the JT Group, comply with the Tobacco Rules.

Under the meeting for the Financial System Council tobacco business subcommittee, a new labeling subcommittee was established in February 2016, which conducted an evaluation on the Advertising Guideline. The labeling subcommittee reported the results to the tobacco business subcommittee in June 2016, proceeding further discussions within the tobacco business subcommittee. As a result, the Regulation Review of the Caution and Advertising was published on December 28, 2018.

Based on the aforementioned review and a promulgation of a partial amendment of the Ordinance for Enforcement of the Tobacco Business Act; the Advertising Guideline; and Related Notices of the Tobacco Business Act on June 14, 2019, TIOJ revised the Tobacco Rules on the same day.

There are four criteria in this revision: the revision of standards for tobacco products; establishment of new rules for T-vapor products; establishment of new rules for T-vapor devices; and establishment of new rules for business activity and television advertising to advocate the improvement of smoking manners.

With regard to the Caution, the revision now requires (a) caution statement changes on tobacco product packages by July 1, 2020 and (b) more restrictive advertisement measures for tobacco products. The changes in (a) include wording revision, which reflects the latest scientific knowledge, and increasing the area of the statements at least 50% on the surface. With regard to (b), the measures include more effective ways to prevent minors' access to internet advertisements and new restrictions on the size and presentation methods for point-of-sale advertising.

The enactment of the Partial Amendment of the Health Promotion Act (Act No. 78 of July 25, 2018) (hereinafter referred to as the Act) in July 2018 strengthened measures to prevent unwanted passive smoking at facilities used by numerous people. The Act classifies the facilities into three types in terms of measures to take: Facility Type 1 includes schools, hospitals and administrative agencies; Facility Type 2 includes restaurants, offices, factories and any other facilities that do not fall under Facility Type 1 or facilities whose main purpose is not for smoking; and other facilities that do not fall in Facility Type 1 or 2 whose main purpose is to provide a place for smoking (includes public smoking areas, bars that are mainly for smoking and tobacco retailers). Facility Type 1 prohibits smoking within its site but allows designated outdoor smoking areas if they meet all of the requirements. Facility Type 2 prohibits indoor smoking but allows designated smoking rooms after meeting certain criteria. Additionally, a restaurant can allow indoor smoking once it meets certain requirements. Facilities whose main purpose is to provide a place for smoking allow smoking within their sites. We expect less smoking places to be available after the Act comes into full enforcement on April 1, 2020. We forecast a certain level of impact on our Group's business performance while it is difficult to predict the anticipated changes in smoking environment.

Impact on the Group's Business Performance

The JT Group expects regulations, such as the aforementioned and new ones (including those of local governments), to expand across Japan and other countries where we operate, although it is difficult to forecast the exact contents of possible laws, regulations and industry guidelines relating to sales activities, marketing, packaging and labeling, tobacco products and smoking.

We support any appropriate and rational tobacco regulations. Nevertheless, we also expect unfavorable impact on our business performance if there will be further enhancement of these regulations or if we are unable to adapt into them.

Tobacco Business Act

The importers and wholesalers of manufactured tobacco products must register with the Minister of Finance. On the other hand, retailers of manufactured tobacco products must obtain the license from the Minister of Finance. The retailers must sell the products manufactured by JT and imported tobacco products at the fixed retail price that is approved by the Minister of Finance. The Minister of Finance must approve the filed retail sales prices unless the prices are considered unfairly prejudicial to consumers.

The Tobacco Business Act requires the JT Group to enter into purchase contracts with Japanese tobacco growers annually, regarding the aggregate cultivation area for specific varieties of leaf tobacco and the prices for the leaf tobacco by variety and grade. The Group must purchase all leaf-tobacco-produced pursuant to such contracts, except those that are not suitable for the manufacture of tobacco products. Before entering into the contract, the JT Group shall submit a proposal to the Leaf Tobacco Deliberative Council (*hatabako shingi kai,* hereinafter referred to as the Council). The Group, with the approval of the Minister of Finance, appoints members for the Council among those who represent the domestic leaf tobacco growers and academic scholars. The proposal covers the area of domestic tobacco cultivation as well as the purchasing price of leaf tobacco and the Group shall honor the Council's opinions. Similar to many other agricultural products in Japan, production costs for domestic-grown leaf tobacco are higher than those that are foreign-grown. This results in the purchase price for the domestic-grown leaf tobacco (before re-drying) to be approximately three times higher than that of the foreign-grown leaf tobacco (after re-drying).

The Japan Tobacco Inc. Act

Pursuant to the Japan Tobacco Inc. Act (hereinafter referred to as the JT Act), JT was established to manage the business related to manufacturing, sale and import of tobacco products. Based on the JT Act, the Japanese government must hold over one-third of all of the Company's issued shares except for the class shares, which have no voting rights against all matters that can be resolved at our shareholders' meeting. The JT Act also states that it requires the approval of the Minister of Finance for any issuance of new shares and stock acquisition rights as well as for any issuance of new shares, stock acquisition rights and bonds with stock acquisition rights in case of a share-for-share exchange.

The JT Act also indicates that under the approval of the Minister of Finance, the JT Group may engage in businesses other than manufacturing, sales and imports of tobacco products or tobacco-related business that are essential to serve the purpose of the Group. Certain matters, including the appointment or dismissal of Directors, Executive

Officers and Audit & Supervisory Board Members; amendments to our Articles of Incorporation; distributions of surplus (excluding loss compensation); mergers; corporate splits or dissolution also require the approval from the Minister of Finance. The JT Group must submit its statement of financial position, statement of income and business report to the Minister of Finance within three months after the end of each fiscal year.

The supplementary provisions of the Reconstruction Financing Act* came into effect on December 2, 2011. This Act states that the government shall consider the possibility of full disposal of government-owned JT shares by reassessing owned JT shares through taking into account their involvement in the tobacco-related industries based on the Tobacco Business Act by the fiscal year ending March 31, 2023.

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

Voluntary Marketing Regulations

The JT Group's Global Marketing Principles

The JT Group complies with all regulations of the respective countries where we operate. At the same time, we pursue our business based on the JT Group's Global Marketing Principles (hereinafter referred to as the Principles), which value responsible marketing. The JT Group markets only towards existing adult consumers with the aim of maintaining brand loyalty and encouraging adult consumers to switch to our brands. Moreover, we recognize that youth smoking prevention is an issue that must be addressed by society as a whole. Based on the Principles, we will continue to operate our business appropriately, while working with governments and other relevant organizations to take steps towards preventing youth smoking.

Please refer to JT.com for more details.

Pharmaceutical Business

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

In Japan, the marketing of pharmaceutical products is subject to the supervision of the Ministry of Health, Labor and Welfare (MHLW) and relevant prefectures, primarily under the Act on Securing Quality, Efficacy and Safety of Products Including Pharmaceuticals and Medical Devices. This Act requires pharmaceutical companies to obtain an approval to conduct their manufacturing and distribution activities from every prefecture where they operate once every five years. In addition, the companies must obtain marketing approval for each of their products from the MHLW.

The Japanese universal health insurance system sets a list of pharmaceutical drugs and their official prices which medical insurance can cover. Moreover, drastic reform of the drug pricing system will create challenging circumstances due to annual drug price revision, constraints on the scope of price maintenance premium drugs, price reduction of long-listed drugs according to replacement rate and similar factors.

Processed Food Business

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

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

The Food Sanitation Act aims to prevent the sanitation hazards resulting from consumption of food and beverages. This Act requires food-related companies to take necessary measures under their own responsibility to ensure the safety of food, additives, tools and packages. The measures discussed in the Act include the acquisition of knowledge and skills, assurance of raw material safety and inspection. The Food Labeling Act sets the standards for the labeling of food intended for sale and defines the labeling requirements such as allergens, expiration date, materials or origin. Food-related companies and entities must comply with the standards to prepare their product labels.

While complying with the abovementioned laws and regulations, the JT Group is also striving to address in a high level of food safety control through four perspectives: Food Safety, Food Defense, Food Quality and Food Communication.

Litigation

JT and/or some of its subsidiaries are defendants in lawsuits filed by plaintiffs seeking damages for harm allegedly caused by smoking, the marketing of tobacco products or exposure to tobacco smoke. As of the fiscal year-end date, there were a total of 20 smoking and health-related cases pending in which one or more members of the JT Group were named as a defendant or for which JT may have certain indemnity obligations pursuant to the agreement for JT's acquisition of RJR Nabisco Inc.'s non-U.S. tobacco business. In addition, JT and some of its subsidiaries are also defendants in lawsuits other than the smoking and health-related cases.

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

On March 8, 2019, JTI-Mac filed for protection from its creditors under the Companies' Creditors Arrangement Act (CCAA). The Ontario Superior Court has granted the CCAA application and extended protection in favor of JTI-Mac. All the Canadian matters against JTI-Mac have been stayed by the court order. JTI-Mac carries on business in the ordinary course under the CCAA.

In recent decades, numerous, large-scale, smoking and health-related cases have been brought against tobacco product manufacturers in the U.S. and some of the cases initially resulted in verdicts with massive damage awards. JT and its subsidiaries are not defendants in any of these lawsuits, nor are they subject to any indemnity claims with respect to them. The JT Group's U.S. tobacco business does not include the business that it acquired from RJR Nabisco Inc. in 1999, as well as the Natural American Spirits' non-U.S. business that it acquired from the Reynolds American Inc. group in January 2016. Even now, the scale of the JT Group's U.S. tobacco business remains small. Hence, the Group considers potential exposure to smoking and health-related litigation in the U.S. to be low; we believe that litigation in the U.S. will not materially affect its businesses in the near future.

Following the 2015 acquisition of Logic Technology Development LLC, the JT Group operates an e-cigarette business in the U.S. The Group is aware of related ongoing litigation alleging health effects associated with e-cigarette use and harm caused to consumers by misleading representations and advertising for which plaintiffs are seeking damages and/or demanding health warnings against e-cigarette manufacturers in the U.S. However, as of the fiscal year-end date, neither JT nor any of its subsidiaries are a party to these cases.

Please refer to the "Consolidated Financial Statements, "Note" 38 Contingencies – Contingent Liabilities" for major lawsuits to which JT and some of its subsidiaries are named as defendants.

To date, The JT Group has never lost a case or paid any settlement award in connection with smoking and health-related litigation. However, the Group is unable to predict the outcome of currently pending or future lawsuits. A decision unfavorable to the JT Group and payment of substantial amount of monetary compensation could materially affect its financial performance. Moreover, regardless of the results of these lawsuits, critical media coverage may reduce social tolerance of smoking, strengthen public regulations concerning smoking and prompt the filing of a number of similar lawsuits against the JT Group, forcing it to bear litigation costs and materially affecting our business performance. Apart from smoking and health-related ones, the JT Group also may become the defendant in further litigation. When any problems arise on the Group's product quality, this will lead to a claim seeking profit liability. Such litigation cases may negatively affect its business performance or manufacture, sale and import and export of our products, should their outcomes prove unfavorable.

ABSOLUTE REQUIREMENTS FOR SUSTAINABILITY

Respect for Human Rights

We respect human rights across our value chain and recognize the Universal Declaration of Human Rights, the International Bill of Human Rights and the International Labour Organization's Declaration on Fundamental Principles and Rights at Work. The JT Group Human Rights Policy follows the framework provided by the UN Guiding Principles on Business and Human Rights (UNGPs).

Our Approach and Progress

Inform

We are working hard to embed human rights thinking in our Corporate culture and to improve employees' understanding of the human rights implications of business decisions. To do this, we provide regular training and continuously share information about human rights and the JT Group Human Rights Policy.

Assess

We conduct Human Rights Impact Assessments (HRIAs) to identify and assess actual and potential human rights risks. In line with the UNGPs, our HRIAs focus on the greatest risk to people, both within our own Company and through business relationships with our suppliers from farm to store. As a result of the HRIAs, we aim to address the identified risks of the rights-holders, meet our stakeholder expectations on respecting human rights and mitigate against the overall risks to people and the business.

Conducting human rights due diligence – through HRIAs – is part of our Corporate responsibility to prevent adverse impacts on people and ensure that the highest standards of behavior are upheld within our business and value chain. To achieve this, we are committed to assessing 100% of our high-risk countries by 2025, in our tobacco business.

As part of this commitment, we have completed nine HRIAs across our entire value chain in the last two years – in the Dominican Republic, Egypt, Ethiopia, Kazakhstan, Kyrgyzstan, Malaysia, Mexico, Myanmar and Tanzania. In our Japanese operations specifically, we started conducting due diligence in our processed food business in China and Thailand.

Over the last year, we have also conducted HRIAs in our tobacco leaf supply chain in various markets, including Ethiopia and India. These assessments provide a more comprehensive understanding of the human rights impacts within one specific part of our value chain — our tobacco supply chain and farming business — and the root causes of challenges that tobacco growers face in their communities.

Improve

We develop action plans to address issues identified through HRIAs and self-assessment questionnaires. Since 2018, we have developed nine action plans in our tobacco business and seven action plans in our processed food business, each with an agreed timeline. A Network of Human Rights Champions is responsible for ensuring that these action plans are managed and implemented by each country and respect for human rights is firmly established in the business.

The United Nations Guiding Principles on Business and Human Rights make the pathway clear: companies have a responsibility to respect the rights of those they impact through their business operations and supply chains.

As a company, we have embraced our obligation to respect human rights and are committed to tackling the challenges this will bring. We have made solid progress and will continue this work on our journey of continuous improvement.

Charlie Watson
Director, Human Rights, JT International S.A.

Learn more about our findings from HRIAs at JT.com.

Improving Our Social Impact

Our community investment policy determines a common goal across the JT Group: "To contribute to the development of sustainable societies, by helping to make communities more inclusive." We believe that everyone should have the opportunity to participate in society, and that inclusive societies are also better for business.

Our community investment programs are implemented according to our community investment policy. All of our programs have a positive impact on our communities while respecting the environment and the diversity of societies and individuals.

Our Focus Areas

Through long-term partnerships with local and international organizations, we are implementing about 400 community investment programs that contribute to the development of inclusive and sustainable societies across 68 countries. The programs are based on global and local needs and help communities become more inclusive and resilient. We are focusing on three specific issues:

1. Reducing inequalities, e.g., helping underprivileged people gain access to food and education.
2. Improving community resilience in disaster-prone areas, e.g., providing access to clean water.
3. Protecting the environment, e.g., replanting trees with the help of our employees.

Measurement and Evaluation

Our work is highly rated by external agencies, including the Dow Jones Sustainability Indices (DJSI), which recognizes us as the industry leader in "corporate citizenship and philanthropy," with a perfect score of 100.

To measure the social impact of our work, we use the LBG* Framework provided by Corporate Citizenship.

LBG CORPORATE CITIZENSHIP

* Global standard for measuring and reporting on corporate community investment

Our Contribution to Communities in 2019

Between 2015 and 2030 we will invest US$600 million to help make communities inclusive and resilient, with our employees contributing 300,000 volunteer hours.

Please refer to page 27 for more details on our progress towards our targets.

Total 50 (USD MM)
US$44,044,379 in cash
US$ 4,213,951 in management costs
US$ 1,109,297 in employee volunteer hours
US$ 303,483 in kind

33,055 Hours volunteered (only including volunteering during working hours)

398+ Community investment programs

689 Organizations supported

2,270,421 Beneficiaries

Note: We applied the average exchange rate for 2019 (US$1= 109.03 yen).

Learn more about our community investment activities at JT.com.

Improving Our Environmental Impact

Environmental issues, such as climate change, are of increasing societal concern. Our operations impact the environment through resource usage, emissions and waste generation, as do most industries. The environment also has a direct influence on our business. We all need to address environmental issues and, as a global organization, we recognize that we have a key role to play in reducing our impacts, not only from our own operations but across our value chain.

By implementing sustainable business practices, we are able to conserve resources, reduce waste, manage costs and meet growing consumer demand for more sustainable products – bringing benefits to both the environment and our business. This approach is explained in the JT Group Environment Policy.

Learn more about our approach to environment on JT.com.

The JT Group Environment Plan 2030*[1]

In 2019, we launched the JT Group Environment Plan 2030, which sets objectives and targets that address our key environmental risks and opportunities in relation to three focus areas: Energy and Emissions, Natural Resources and Waste.

Our GHG emission reduction target was approved as a science based target (SBT) by the Science Based Targets initiative (SBTi).

SCIENCE BASED TARGETS
DRIVING AMBITIOUS CORPORATE CLIMATE ACTION

	Objective	Target	Progress in 2019
Energy	Transition our operations to net zero carbon energy supply.	We will double the proportion of renewable electricity that we use to 25% by 2030 and 100% by 2050.	13.9%
Emissions	Reduce our greenhouse gas emissions to support the Paris Agreement on global climate change with the aim of achieving net zero carbon emissions from our operations.	We will reduce greenhouse gas emissions from our own operations by 32%.	-14.3%
		We will reduce emissions associated with our purchased goods and services by 23%.	+9.0%*[2]
		This will be achieved through a 40% reduction from our direct leaf supply chain and reductions in our non-tobacco materials, such as packaging.	p27
Water	Support global water stewardship by reducing our water withdrawal and by encouraging water risk management in our supply chain.	We will reduce water withdrawal associated with our tobacco business by 15%. To better understand water risk and use in our supply chain, by 2022, we will implement a water risk management process in our manufacturing supply chain.	p27
Forestry	Ensure a sustainable wood supply for our product supply chains and further contribute to forest conservation and rehabilitation.	To further focus our efforts on sustainable forest management, by 2020, we will have assessed the drivers for deforestation and forest degradation in communities where we source tobacco and developed action plans for improved wood resource use, forest conservation, and forest rehabilitation. We will replace all wood from natural forests used in the tobacco curing process of our directly contracted growers with renewable fuel sources.	p27
Waste	Further reduce the environmental impacts of waste associated with our processes and products.	We will reduce waste associated with our tobacco business by 20%. By 2020, we will have targets and action plans relating to the appropriate use and responsible disposal of materials, including plastics, used in our products and packaging.	p27

*[1] Baseline year for all targets is 2015. Target year is 2030 unless stated otherwise. The overall plan is to be reviewed every five years.
*[2] The main reason for the increase in GHG emissions associated with our purchased goods and services is leaf related emissions rise due to increased leaf volume sourced from Zambia and Tanzania, both of which use wood for curing that currently is predominantly non-renewable. We expect that the impact of initiatives to reduce leaf-related emissions will be seen from 2022 onwards, with curing barn upgrades and the increase in proportion of renewable wood used for curing in Zambia and Tanzania.

JT Group Environment Management

In our more complex operations, we align our approach to environmental management with internationally recognized standards – ISO 14001 and ISO 50001.*[3] In our smaller and less complex operations in Japan, we have implemented our own "JT Green System," which promotes a simple and consistent approach.

To objectively review our approach to environmental management and our overall performance, we use external disclosures and ratings agencies, such as CDP and the Dow Jones Sustainability Indices (DJSI). In 2019, we improved our rating in DJSI's environmental dimension and achieved the maximum score in Environmental Reporting and Climate Strategy.

MEMBER OF
Dow Jones Sustainability Indices
In collaboration with RobecoSAM

CDP A List and Supplier Engagement Leader

Since 2010 we have reported on our environmental impact to CDP, a leading external ratings agency and climate research provider. This year we regained our spot on CDP's prestigious "A List" for climate change (press release in January 2020), having done so previously in 2016. We are also very proud to report that we are included in the CDP A List as a global leader on water security for the first time (press release in February 2020) and recognized as a global leader in engaging our supply chain in addressing climate change.

CDP DISCLOSURE INSIGHT ACTION A LIST 2019 CLIMATE
CDP SUPPLIER ENGAGEMENT LEADER 2019
CDP DISCLOSURE INSIGHT ACTION A LIST 2019 WATER

Live barns in Malawi.*[4]

*[3] ISO 14001 and ISO 50001, are the internationally recognized standards for environmental management systems and energy management systems, respectively. These standards do not prescribe absolute performance requirements. Rather, they provide us with a framework to help build effective management systems that deliver continual improvement in environmental and energy performance.
*[4] Learn more about Live barns at JTI.com.

Good Governance and Business Standards

Dialogue between the Chairman of the Board and an Outside Director

Yukiko Nagashima
Outside Director

Yasutake Tango
Chairman of the Board

The JT Group appoints Outside Directors who can contribute to the Group's sustainable profit growth and enhance corporate value in the mid- to long-term, from the perspective of strengthening the supervisory functions and transparency of business.

The following is a dialogue between Yasutake Tango, the Chairman of the Board, and Yukiko Nagashima, an Outside Director since 2019.

Tango: Our management principles pursue the 4S model. We have been taking various initiatives to enhance our corporate governance, which is one of the key challenges for management, as part of pursuing the model.

Nagashima: It has been almost a year since I was appointed as an Outside Director of JT. By attending board meetings and participating in the decision-making process, I have realized that the 4S model is not just a slogan; it forms the core standard of making decisions in the Group. What really impressed me was when one of the Executive Officers was asked about the status of an acquired overseas tobacco company at a board meeting. His report included the feedback from the employees at the local factory of the acquired company that they were glad to be acquired, saying that their uniforms have now become much more hygienic. I was surprised to receive such an employee-centered report in addition to quantitative prior- and post-acquisition performance analyses, which are usually mandatory. The former report also made me realize that there are systems that enable the observation and reporting of what is happening on the frontlines from the 4S model perspective, reflecting the fact that the model has become the Group's mindset.

The 4S model pursued by the JT Group is a cornerstone for making decisions that takes into consideration the sustainability of business operations without being biased toward any particular stakeholder. Any decision making is conducted by comprehensively accounting for the relationships between and impacts on various stakeholders, ensuring that corporate activities are not just profit oriented. The JT Group introduced the 4S model in 1996, which is in harmony with the concept of sustainability, the global trend now embodied by ESG and the SDGs. I also think it is important for the Group to communicate that the 4S model is not just about seeking higher stakeholder satisfaction; it also enhances the growth of the Group.

Tango: Thank you. Throughout my business trips to our offices around the world or when addressing sustainability challenges, I notice the frontline employees are carrying out their duties while taking each stakeholder into consideration. I believe that, in line with your opinions, we must continuously pursue the 4S model.

Needless to say, good corporate governance is the foundation of pursuing the 4S model. The Board of Directors plays a role in making decisions on Group-wide management strategies and important matters. At the same time, the Board serves as the body supervising all business activities. To ensure board meetings run effectively, it is crucial that all attendees, including Outside Directors, engage in free, active and constructive debate and exchanges of opinion. To this end, proposals to the Board are explained in advance to attendees by the proposing party or the Corporate Strategy Division, which serves as the Board's secretariat. We strive to ensure that each attendee has enough time to fully assess every proposal. In addition to proposals, information that supports the forming of judgments during the decision-making process, such as the business environment surrounding the tobacco industry, is shared regularly. We also encourage Outside Directors to visit the frontlines of the Group worksites in Japan and overseas as much as possible. Furthermore, we have just taken measures to increase opportunities for Outside Directors and the Audit & Supervisory Board to get together and exchange opinions.

To evaluate the effectiveness of the Board of Directors, we conduct surveys of all Members of the Board and Audit & Supervisory Board Members on the operational framework, the agenda and the quality of the discussions at board meetings. Using the feedback from the survey, we conduct PDCA cycles to further enhance the effectiveness of the Board of Directors. On this point, what is your take on JT's Board of Directors, Ms. Nagashima?

Nagashima: In its evaluation of effectiveness, the JT Group goes beyond just scoring each element. The Group collects qualitative comments on both accomplishments and areas of concern. The frank opinions of each Member of the Board and the Audit & Supervisory Board Member are provided as feedback to the board meetings. I feel that one way the Board of Directors helps enhance its effectiveness is its assessment of new initiatives, asking what their aims are and how they are actually fairing in terms of achieving those aims. One such example was when the Advisory Panel on Nomination and Compensation was launched, we quickly added new effectiveness evaluation items related to the new panel.

Tango: The Advisory Panel on Nomination and Compensation, which you just mentioned, was established in 2019 through the integration of the formerly independent Compensation Advisory Panel and the Meeting for Talent Development, which discussed matters related to supporting the growth of candidates for top management positions. The purpose was to enhance the quality of debate by uniting the two panels and having the same members hold deliberations.

In terms of selecting our leaders for the next generation, I would like the CEO, CFO and other top management positions to be filled by people who can seriously tackle the challenges of the JT Group as well as take the initiative. In particular, I would like the young people who will lead the JT Group in the future to always carry out their work with a vision of what they want the JT Group to be in 10, 20 or even 30 years from now. I want them to figure out what they need to do now to realize their vision of the future and then proactively take on challenges. Some say that our young employees are relatively quiet compared to those in the past, who used to put pressure on the top management. I would like the young people to discuss what we need to do and take action with a mindset of leading the JT Group's future.

Nagashima: As you said, to ensure that the personnel responsible for the future of the Group are actively engaging in a wider environment, I think they need to lead their businesses not only by leveraging the global business foundations established by their forerunners but also by focusing on how tobacco is fundamentally defined and, from a longer-term perspective, on defining the ideal relationship between a tobacco product and society. I believe this would likely lead to more younger people putting pressure on top management, which you touched on earlier. Additionally, I think it is very important for the current top management to have discussions with those next leaders to speedily create future business opportunities.

In addition, to recruit and train the personnel responsible for the present and future growth of the JT Group and fully harness their abilities, it is extremely important that an appropriate executive remuneration system is in place. As an Outside Director, I am carrying out my responsibility to establish a competitive executive remuneration system befitting those work responsibilities while also assessing its fairness from a market perspective.

Tango: Last but not least, I would like to hear your thoughts on your role as an Outside Director with regard to issues related to the corporate governance and business of the JT Group.

Nagashima: This is not limited to corporate governance, but I feel it would be even better to more strongly communicate the goals and aspirations for businesses both internally and externally. The 4S model is ultimately a check sheet for operating a business. I think the starting point for conducting business is embracing the vision of what the JT Group wants to do and what it strives to be. The support of each stakeholder can only be gained through the results of these business efforts.

In addition, given the rapidly changing business environment, transformation is an indispensable tool. As we undertake transformation, I would like everyone to take up challenges in all areas with the belief that they will definitely succeed and while being unafraid of failure. Rather than craft a strategy to avoid failures, take up challenges with the belief that you will definitely succeed and enhance your quality of output as a result. Even if you fail, you will learn much more from the mistakes. I believe that this mindset is also in harmony with one of the strengths of the JT Group, which has continued to grow through transformation accomplished by taking up many challenges amid a challenging business environment.

The company where I worked has repeatedly disrupted its success models and launched new businesses. I often encountered occasions where we changed our personnel, organizations and strategies. In terms of corporate governance, we also changed our management structure, going from a privately owned business to a listed company.

In addition, I once served as CEO of one of the company's subsidiaries. What I learned from that experience was that a CEO's jobs are to make decisions and take responsibility. Management can choose from several options but to prove that they have chosen the right one, they must succeed. It is a series of tough decisions, and even if we fail, management must take responsibility as reflected in remuneration or position. The current tobacco industry requires its players to swiftly undertake various projects and I think this is a similar environment to the one I experienced.

As an Outside Director, I will continue to fulfill my duties through substantive debate while maintaining a healthy distance.

Corporate Governance

Basic Policy

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

Please refer to JT.com for more details on the JT Corporate Governance Policy.

Reasons for Choosing the Current Structure

The JT Group has a fair and independent Audit & Supervisory Board, which strengthens the supervisory function on management in securing objectivity and neutrality by monitoring the performance of the Members of the Board and Executive Officers. Under the supervision of the Audit & Supervisory Board, the Group is ensuring efficient operations with optimal size of the Board of Directors and through delegation of authority under the Executive Officer System. As part of the Company's efforts to establish an effective corporate governance system, it has established the JT Group Compliance Committee with the majority of the members consisting of external members and the Advisory Panel on Nomination and Compensation with the majority of the members consisting of Independent Outside Directors. Starting 2019, with an objective to further enhance objectivity and transparency of the management and to improve corporate governance, the JT Group has assigned an additional member to both the Outside Directors and Audit & Supervisory Board.

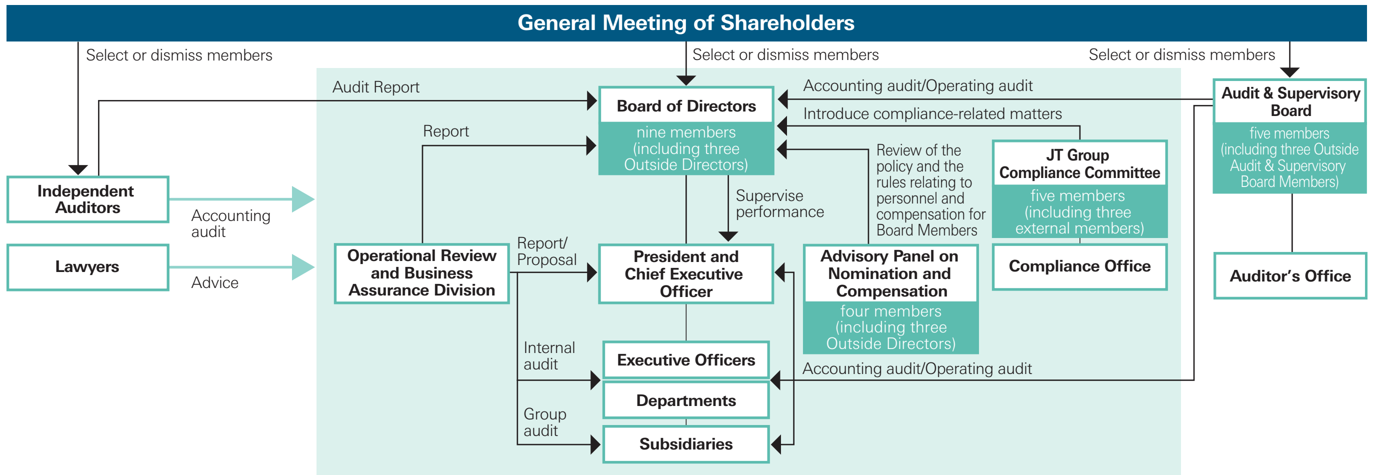
We have adopted our current Corporate Governance structure as these processes have been effective for operational execution and supervision.

Our Initiatives to Enhance Corporate Governance

Strengthen advisory function	Streamline decision-making system and enhance supervisory function	Pursue efficient business execution
Set up the Compliance Committee (FY2000)	Reduced number of Directors (FY2000)	Introduced Executive Officer System (FY2001)
Set up the Advisory Committee*[1] (FY2001)	Promoted the delegation of business execution to the Executive Officers (FY2000, FY2008 and FY2011)	
Set up the Compensation Advisory Panel*[2] (FY2006)	Invited Outside Directors (FY2012)	
Set up the Advisory Panel on Nomination and Compensation (2019)		

*[1] The Advisory Committee was abolished on June 30, 2014.
*[2] The Compensation Advisory Panel was integrated into the Advisory Panel on Nomination and Compensation on March 20, 2019.

Our Corporate Governance System (As of March 19, 2020)



The Advisory Panel on Nomination and Compensation

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

In 2019, it convened six times to confirm and discuss agenda, including a review of the existing executive remuneration plan, a proposal to revise the remuneration plan, the level of remuneration, processes for developing the pool of executive candidates. In addition, we had two Compensation Advisory Panel meetings before establishment of the Advisory Panel on Nomination and Compensation.

Members

Chair	Chairman of the Board	Yasutake Tango
Members	Independent Outside Director	Main Kohda
	Independent Outside Director	Koichiro Watanabe
	Independent Outside Director	Yukiko Nagashima

Nomination of Member of the Board Candidates and Dismissal of Executive Directors and Members of the Board Who Execute the Business

In the JT Corporate Governance Policy, nomination of Member of the Board candidates and dismissal of Executive Directors who are the directors with special titles and Members of the Board who execute the business and related matters shall be conducted according to the following.

Member of the Board candidates shall be nominated by resolution of the Board of Directors after receiving reports of the deliberations from the Advisory Panel on Nomination and Compensation. The President submits the initial proposal of the candidates to the Advisory Panel on Nomination and Compensation. Then the Advisory Panel on Nomination and Compensation deliberates while securing appropriate input from Independent Outside Directors.

If Executive Directors and Members of the Board who execute the business do not meet the required standards or have become unable to perform their duties, they shall be dismissed by the resolution of the Board of Directors. The Members of the Board who are not subject to dismissal shall request the Advisory Panel on Nomination and Compensation to examine and report back the content and results of their deliberations to the Board of Directors on the proposal for dismissal. This Advisory Panel on Nomination and Compensation secures appropriate input from Independent Outside Directors.

Further, when bringing up agenda items on the appointment of Member of the Board candidates to Ordinary General Meetings of Shareholders, and the dismissal of a Member of the Board who is Executive Officer by the Board of Directors, the JT Group shall disclose the reasons for the appointment of individual candidates and for their dismissal, respectively.

Selection and Dismissal Process

Process	Advisory Panel	Board of Directors
Selection Process for Member of the Board	**The Advisory Panel on Nomination and Compensation** Deliberate on the candidate proposed by the President and report its deliberations to the Board of Directors	**The Board of Directors** Resolution on a candidate proposal
Dismissal Process for Executive Directors and Members of the Board who execute the business	**The Advisory Panel on Nomination and Compensation** Deliberate on a proposal for dismissal and report the content and results of its deliberations to the Board of Directors	**The Board of Directors** Resolution on a proposal for dismissal

Succession Planning

The JT Group shall work on creating a succession pool of candidates with qualities to ensure sustainable profit growth and increase corporate value in the mid- to long-term by pursuing the 4S model.

We aspire to enhance the development of the executive candidate pool, in which candidates are nominated by the executive officers led by the CEO; enhance the succession plans and support the growth of such candidates, in consultation with Advisory Panel on Nomination and Compensation comprised mainly of Outside Directors.

Executive Remuneration

Executive Remuneration Policy

In order to achieve sustainable profit growth and increase company value over the mid- to long-term through pursuing the management principles of the 4S model, the Advisory Panel on Nomination and Compensation reviews and provides advice on the policy, framework and calculation method for remuneration of the Company's Members of the Board and Executive Officers in response to inquiries. The panel also monitors whether our executive remuneration level is reasonable. Based on the recommendation from the Advisory Panel on Nomination and Compensation, the key policies for the Company's executive remuneration are as follows:

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

Process of Executive Remuneration

The amount of remuneration for Directors is determined by resolution of the Board of Directors within the approved upper limits at the Ordinary General Meetings of Shareholders in light of deliberations by the Compensation Advisory Panel. These amounts are determined by benchmarking based on third-party research conducted on remuneration of corporate executives at major Japanese manufacturers that operate globally and possess comparable levels of size and profits with the JT Group. The remuneration of Audit & Supervisory Board Members is also benchmarked in the same way and is determined by deliberation among the Audit & Supervisory Board Members within the maximum remuneration approved at the Annual General Meeting.

Executive Remuneration Structure

		Original			New		
		Base salary	Executive bonus	Plan	Base salary	Executive bonus	Plan
Members of the Board (excluding Outside Directors)	Executive Officer	Applicable	Applicable	Applicable	Applicable	Applicable	Applicable
	Not an Executive Officer	Applicable	Not applicable	Applicable	Applicable	Not applicable	Not applicable
Outside Directors		Applicable	Not applicable	Not applicable	Applicable	Not applicable	Not applicable
Audit & Supervisory Board Members		Applicable	Not applicable	Not applicable	Applicable	Not applicable	Not applicable

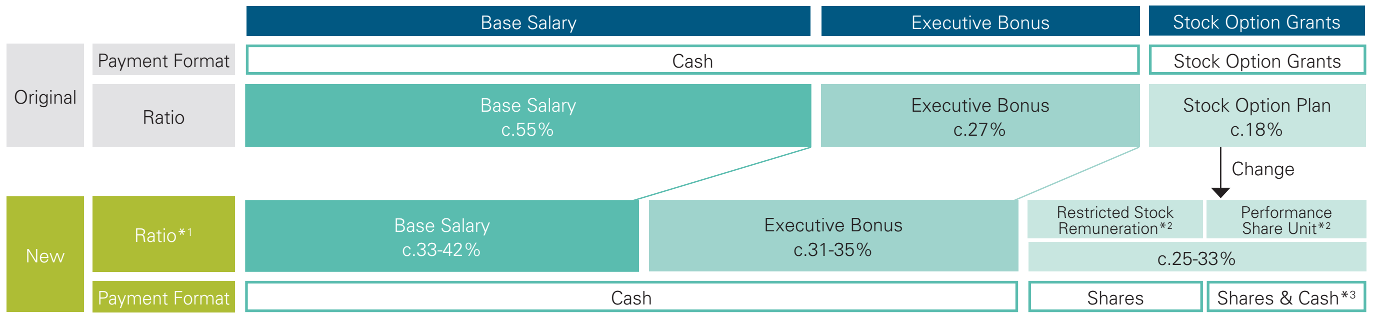
Remuneration for the Members of the Board also serving as Executive Officers

Remuneration for the Members of the Board also serving as Executive Officers (hereinafter referred to as Eligible Directors) is comprised of their "base salary," "executive bonus," and "stock option plan" as they are responsible for achieving assigned annual targets through their day-to-day management.

From 2020, Eligible Directors will be individually evaluated for achievement of their performance targets through execution of their duties that will lead to the Company's sustainable profit growth.

Additionally, in order to strengthen the efforts to enhance the mid- to long-term company value and to further promote shared value with the shareholders, the JT Group has proposed to abolish the existing stock option plan and to introduce the Restricted Stock Remuneration Plan and the Performance Share Unit Plan.

On a 100% grant basis, the composition of executive bonus and performance share unit remuneration will be as per the following illustration.



*1 The composition ratios vary depending on the duties of the Members of the Board. The ranges are indicated in the illustration.
*2 The ratio of the restricted stock remuneration and performance share units is approximately three to one.
*3 Under the Performance Share Unit Plan, 50% is paid as cash towards tax payment.
Note: The above illustration is based on certain assumptions of the Company's performance and the share price. The ratios may fluctuate depending on the Company's performance and the share price.

Remuneration for the Members of the Board who do not serve as Executive Officers (excluding Outside Directors)

Remuneration for the Members of the Board (excluding Outside Directors) who do not serve as Executive Officers is comprised of their "base salary" and "stock option" since they are required to make decisions on company-wide management strategies and fulfill supervisory functions to enhance company value. Effective from January 1, 2020, the remuneration is comprised of the "base salary" in order to place a greater emphasis on objectivity and neutrality and further focus on the supervisory functions, including monitoring the implementation of mid- to long-term growth strategies.

Remuneration for the Outside Directors and the Audit & Supervisory Board Members

Remuneration for both the Outside Directors and the Audit & Supervisory Board Members consists of the "base salary" alone to ensure, respectively, their independence and their responsibility to conduct audits.

Executive Remuneration Details

Base Salary

Until 2019, Executives were remunerated with a monthly "Fixed base salary" as per their responsibilities. From January 1, 2020, the Eligible Directors will be individually evaluated for achievement of their performance targets through execution of their duties that will lead to the JT Group's sustainable profit growth. Performance targets are set through interviews with the Group's President and the CEO at the beginning of year and evaluated at the end of year. The base salary for the following year will be set within a certain range reflecting the individual performance evaluations. However, an individual performance evaluation will not be applicable for the Group's President and the CEO.

Executive Bonus

Executive bonuses for Eligible Directors will be paid as monetary remuneration, reflecting annual performance. Adjusted operating profit at constant FX and profit results will be the performance indicators (KPI), which form the foundation of sustainable profit growth and shared value with the shareholders. Executive bonuses will be determined by adjusted operating profit at constant FX and profit in the ratio of 75% and 25%, respectively. Performance-linked payouts will be based on the KPI achievement in the range of 0% - 200%.

Stock Option Grants

The Company's stock options are designed based on a stock option grants plan, in which the exercise price is 1 yen (the amount paid by the person is 1 yen per share). The Board of Directors decides the number of units to be allocated for each term based on the fair value of the Company's shares, calculated by a third party.

The assigned stock options can be exercised only after one's positions as Directors, Audit & Supervisory Board Members and Executive Officers end. We do not intend to change this exercise condition in the future.

From 2020, we will abolish the existing stock option plan and introduce the restricted stock remuneration plan and the Performance Share Unit Plan for the Members of the Board also serving as Executive Officers. The stock options that were already granted will remain in force.

Restricted Stock Remuneration Plan (Effective from 2020)

Restricted Stock Remuneration Plan is designed to further enhance the shared value in the mid- to long-term between Eligible Directors and shareholders. Eligible Directors receive monetary compensation claims every year towards restricted shares and Eligible Directors will receive the allocation of JT's common shares by paying all of the monetary compensation claims in kind in accordance with the resolution of the Board of Directors (the allotment will be made from the treasury stock). The transfer restrictions on the allotted shares will be lifted upon resignation of such Eligible Director from the Company's Board of Directors or any other position specified by the Company's Board of Directors.

Performance Share Unit Plan (Effective from 2020)

The Performance Share Unit Plan is a performance-linked stock compensation system that aims to strengthen the shared value with shareholders in order to enhance the company value over the mid- to long-term and to commit to achieving business results over the mid-term. The Eligible Directors receive monetary compensation claims and cash after the Performance Evaluation Period, which is aligned with the duration of the JT Group's three-year business plan, in accordance with the performance achievement rate and other multi-year performance targets during the Performance Evaluation Period. The Advisory Panel on Nomination and Compensation deliberates and decides on the achievement rate of such targets for performance and other items during the Performance Evaluation Period. The remuneration for the performance share units will be disbursed at the end of the year as monetary remuneration claims and cash towards the acquisition of common stock. Each of the Eligible Directors will receive an allocation of the Company's common shares by paying all of the monetary compensation claims in kind in accordance with a resolution of the Board of Directors (the allotment will be made from treasury stock). Profit will be set as a KPI for the Performance Stock Unit Plan starting in 2020 and the performance-linked payout will be based on the KPI achievement in the range of 0% - 200%.

Overview of the Resolutions on Total Executive Remuneration at the Ordinary General Meeting of Shareholders

The ceiling for annual aggregate remuneration towards all Members of the Board was approved at our 34th Ordinary General Meeting of Shareholders (March 20, 2019) and our 35th Ordinary General Meeting of Shareholders (March 19, 2020) as listed below.

Original

		Remuneration amount	Members of the Board (excl. Outside Directors)		Outside Directors
			Executive Officer	Not an Executive Officer	
Base salary	Base salary	Up to 1.2 billion yen (incl. 80 million yen for Outside Directors)	Applicable	Applicable	Applicable
Short-term incentive	Executive bonus		Applicable	Not applicable	Not applicable
Mid- to long-term incentive	Stock option grants	Up to 240 million yen Stock option grant up to 960 units (192,000 shares equivalent)	Applicable	Applicable	Not applicable
	Total remuneration amount	1.44 billion yen			

New

	Remuneration amount	Members of the Board (excl. Outside Directors)		Outside Directors
		Executive Officer	Not an Executive Officer	
Base salary	Up to 1.1 billion yen (incl. 80 million yen for Outside Directors)	Applicable	Applicable	Applicable
Executive bonus		Applicable	Not applicable	Not applicable
Restricted stock	Up to 210 million yen (Up to 115,200 shares)	Applicable	Not applicable	Not applicable
Performance share units	Up to 130 million yen (Up to 76,800 shares)	Applicable	Not applicable	Not applicable
Total remuneration amount	1.44 billion yen			

Further, the maximum amount of annual aggregate remuneration towards all Audit & Supervisory Board Members was approved at our 34th Ordinary General Meeting of Shareholders (March 20, 2019) and will not exceed 240 million yen.

Total Amount of Remuneration in 2019

Category	Total amount of remuneration and other payments (Millions of yen)	Total amount of remuneration and other payments by its type (Millions of yen)			Number to be paid (Person)
		Basic salary	Executive bonus	Stock option grants	
Members of the Board (excluding Outside Directors)	659	467	77	115	6
Audit & Supervisory Board Members (excluding Outside Audit & Supervisory Board Members)	94	94	-	-	3
Outside Directors and Outside Audit & Supervisory Board Members	119	119	-	-	7
Total	**872**	**680**	**77**	**115**	**16**

Note: For "executive bonus," the amounts planned to be paid are shown.

Evaluation of Effectiveness of the Board of Directors

In the JT Group, all Members of the Board as well as Audit & Supervisory Board Members conduct questionnaire-based self-evaluations on the effectiveness of the Board of Directors in terms of its operation systems and supervisory functions as well as interactions with shareholders and investors. The Board of Directors Secretariat also conducts individual interviews with the aim of supplementing the results of the evaluations.

The Board of Directors then assesses and analyzes the results for further improvements in its effectiveness.

The JT Group confirmed the improvement of the Board of Directors' effectiveness in 2018. On the other hand, we found that there is room for improvement which includes strengthening cooperation between the Outside Directors and the Audit & Supervisory Board Members; and an information sharing process that could contribute to further enhancing the quality of decision-making at the Board of Directors. Consequently, we took various measures in 2019, which include increasing the number of meetings to exchange opinions between the Outside Directors and the Audit & Supervisory Board Members as well as improving the processes of advance explanation and information sharing in relation to items on the Board of Directors agenda.

From 2020, the JT Group will prioritize planning information sharing opportunities that will further enhance the supervisory functions of the Board of Directors; and determining the level of detail and depth of information to be shared. We decided to take these measures by taking account of the challenges identified in the evaluation conducted in 2019.

The JT Group will continue to take necessary measures to further enhance effectiveness, including the aforementioned ones.

The Board of Directors

The Board of Directors is responsible in making decisions for any critical matters including the JT Group strategy as well as in supervising all the activities of the Group. The structure of the Board of Directors is defined as follows.

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

The Board of Directors meeting, in principle, is held every month and more if necessary. The Board of Directors makes decisions on the matters required to be resolved by them under the Companies Act, such as any essential business plans, disposal or acquisition of important assets, significant amount of borrowings and conclusion of important agreements. For the purpose of supervising the Company's activities, the Board of Directors requires Member of the Board to report on the progress of operations at least on a quarterly basis. The JT Group had 14 board meetings attended by all members of the Board in 2019 to discuss important issues including the management plan.

The Audit & Supervisory Board

The Audit & Supervisory Board, entrusted by shareholders and ensured of its autonomy, conducts operating and accounting audits. We currently have five Audit & Supervisory Board Members including three Outside Audit & Supervisory Board Members. Collectively, the members have experience in management, legal, finance and accounting among other areas. The Audit & Supervisory Board Members possess various statutory rights in order to accomplish their roles and responsibilities. These include making requests to the Members of the Board, Executive Officers and employees to report to the Audit & Supervisory Board issuing injunctions to prevent illegal activities by Member of the Board representing the Company in the case of litigation between any Member of the Board and the Company; and dismissing the auditing firm. The Audit & Supervisory Board submits its report, containing the results of both the accounting and operating audits, to the Ordinary General Meeting of Shareholders. Members of the board or Executive Officers must report to the Audit & Supervisory Board any identified facts that may cause significant damage to the Company as well as other important matters concerning the management of the Company. The Audit & Supervisory Board Members can attend meetings of the Board of Directors and other important meetings. Members of the Board respond promptly and appropriately when they are requested by Audit & Supervisory Board Members to inspect important documents, conduct on-site inspections and submit reports. In addition, the audit department and the compliance departments collaborate with the Audit & Supervisory Board Members. Ms. Nagata and Mr. Obayashi attended all 14 meetings of the Audit & Supervisory Board held in 2019. Mr. Yamamoto, Mr. Mimura, and Mr. Yoshikuni attended all 10 meetings of the Audit & Supervisory Board held in 2019 following their appointment.

Directors and the Audit & Supervisory Board

Nine Directors (including three Outside Directors)

As of March 19, 2020

The Directors marked with * are also the Group's Executive Officers.

Yasutake Tango
Chairman of the Board

Date of birth: March 21, 1951
Term of office:
2 years from March 2020
Number of shares held: 13,800

April	**1974**	Entered Ministry of Finance Japan
October	**2006**	Director-General of the Financial Bureau, Ministry of Finance Japan
July	**2007**	Deputy Vice Minister, Ministry of Finance Japan
July	**2008**	Director-General of the Budget Bureau, Ministry of Finance Japan
July	**2009**	Administrative Vice Minister, Ministry of Finance Japan
December	**2010**	Corporate Auditor, The Yomiuri Shimbun Holdings
December	**2012**	Special Advisor to the Cabinet
June	**2014**	Chairman of the Board of the Company (Current Position)
June	**2015**	Outside Director, The Ogaki Kyoritsu Bank, Ltd. (Current Position)

Significant Concurrent Positions Outside the Company:
Outside Director, The Ogaki Kyoritsu Bank, Ltd.

Mr. Tango possesses abundant knowledge and experience on topics that include corporate governance, gained through diverse networking not limited to the public or private sectors as well as his important positions as Administrative Vice Minister of the Ministry of Finance in his longstanding experience in ministries and bureaus. Therefore, we propose his reelection as he currently serves as Chairman of the Board; chairman of the Advisory Panel on Nomination and Compensation; and chairman of the Compliance Committee of the Company. We believe his broad outlook and high standing in his field will be essential to the improvement of the governance of the Group going forward.

Mutsuo Iwai
Deputy Chairman of the Board
Date of birth: October 29, 1960
Term of office:
2 years from March 2020
Number of shares held: 27,000

April	**1983**	Joined the Company (Japan Tobacco and Salt Public Corporation)
June	**2003**	Vice President, Corporate Planning Division
July	**2004**	Vice President, Corporate Strategy Division
June	**2005**	Senior Vice President and Vice President, Food Business Division, Food Business
June	**2006**	Member of the Board and Executive Vice President, President, Food Business
June	**2008**	Executive Vice President, Chief Strategy Officer
June	**2010**	Member of the Board and Senior Vice President, Chief Strategy Officer and President, Food Business
June	**2011**	Member of the Board, Japan Tobacco Inc. Executive Vice President, JT International S.A.
June	**2013**	Senior Executive Vice President, Chief Strategy Officer
January	**2016**	Senior Executive Vice President, President, Tobacco Business
March	**2016**	Representative Director and Executive Vice President
January	**2020**	Member of the Board
March	**2020**	Deputy Chairman of the Board (Current Position)

Mr. Iwai was appointed to the position of Representative Director and Executive Vice President of the JT Group in March 2016. Despite unclear and uncertain business environments, his forceful execution of business, backed by accurate decision-making, has been a driver of the tobacco businesses. The broad and deep knowledge and insights he has cultivated through wide-ranging experience both in Japan and overseas, in areas such as the tobacco businesses, the food business, and Corporate Strategy, will be essential to the improvement of the governance and the strengthening of relationships with stakeholders.

Masamichi Terabatake*
Representative Director and President, Chief Executive Officer

Date of birth:
November 26, 1965
Term of office:
2 years from March 2020
Number of shares held: 21,400

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

Significant Concurrent Positions Outside the Company:
Managing Director, JT International Group Holding B.V.

Mr. Terabatake has been the President and Chief Executive Officer of the JT Group since January 2018 and was also named Representative Director in March of the same year. He has utilized his extensive experience and knowledge, as well as strong leadership in relation to global business management, into a range of duties such as the planning and execution of management strategy both in Japan and overseas and the execution of the business of the international tobacco business as Executive Vice President of JT International S.A., which has been the Group's growth driver. We acknowledge that his extraordinary insights and wider vision, together with his enhanced reforming capabilities, are indispensable for the management of the Group going forward.

Naohiro Minami*
Representative Director and Executive Vice President, Chief Financial Officer

Date of birth:
January 21, 1964
Term of office:
2 years from March 2020
Number of shares held: 14,800

April	**1986**	Joined the Company
December	**2005**	Controller
July	**2010**	Deputy Chief Financial Officer and Controller
June	**2012**	Senior Vice President, Chief Financial Officer and Controller
July	**2012**	Senior Vice President, Chief Financial Officer
January	**2018**	Executive Vice President
March	**2018**	Representative Director and Executive Vice President (Current Position)

Significant Concurrent Positions Outside the Company:
Supervisory Board Member, JT International Holding B.V.

Mr. Minami was appointed Executive Vice President of the JT Group in January 2018, and then Representative Director and Executive Vice President in March of the same year. He has fully leveraged the wide-ranging and deep knowledge in the field of accounting and finance that he cultivated during his service as Controller, and Senior Vice President, Chief Financial Officer, to play a key role in the management of the Group and contribute to its growth. We consider that his accurate decision-making and strategic thinking based on his diverse experience make a contribution to maintaining and broadening the management foundation that supports the expansion of the Group's business and will be indispensable in driving the Group's management further forward.

Kiyohide Hirowatari*
Representative Director and Executive Vice President

Date of birth: November 11, 1965
Term of office:
2 years from March 2020
Number of shares held: 9,200

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

Mr. Hirowatari was appointed Executive Vice President of the Company in January 2018 and then Representative Director and Executive Vice President in March of the same year. He utilizes his leadership and wide-ranging knowledge in such areas of corporate law, business management and HR, which he developed during his term in diverse and important roles, (including Senior Vice President, Chief Legal Officer; Head of Tobacco Business Planning Division, Tobacco Business and Senior Vice President, Human Resources); to maintain a foundation for the JT Group's sustainable growth and to formulate strategy. We believe that his keen insight and decision-making, cultivated from knowledge and experience in a broad range of fields, will be indispensable in the Group's management going forward.

Kazuhito Yamashita*
Director

Date of birth: February 4, 1963
Term of office:
2 years from March 2020
Number of shares held: 7,200

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

Mr. Yamashita has been Member of the Board and Senior Vice President of the JT Group since March 2019. He has served in such roles as Senior Vice President, Chief Corporate, Scientific & Regulatory Affairs Officer; and Head of China Division, focusing on promoting social and environmental issues and on the expansion of the overseas business. He has leveraged his wide-ranging experience and knowledge to contribute to establishing an environment conducive to the Group's business. His leadership and broad knowledge will be indispensable to the sustainability management that will form the foundation of the Group's sustainable growth going forward.

Main Kohda
Outside Director (Independent Outside Director)

Date of birth: April 25, 1951
Term of office:
2 years from March 2020
Number of shares held: 0

September	**1995**	Started independently as Novelist (Current Position)
January	**2003**	Member of Financial System Council, Ministry of Finance Japan
April	**2004**	Visiting Professor, Faculty of Economics, Shiga University
March	**2005**	Member of the Council for Transport Policy, Ministry of Land, Infrastructure, Transport and Tourism
November	**2006**	Member of the Tax Commission, Cabinet Office, Government of Japan
June	**2010**	Member of the Board of Governors, Japan Broadcasting Corporation
June	**2012**	Outside Director of the Company (Current Position)
June	**2013**	Outside Director, LIXIL Group Corporation
June	**2016**	Outside Director, Japan Exchange Group, Inc. (Current Position)
June	**2018**	Outside Director, Mitsubishi Motors Corporation (Current Position)

Significant Concurrent Positions Outside the Company:
Novelist
Outside Director, Japan Exchange Group, Inc.
Outside Director, Mitsubishi Motors Corporation

Ms. Kohda has been our Outside Director since June 2012. We have benefited from her in-depth knowledge of international finance; her broad experience gained from serving on government committees and similar positions; and her deep insight and objective point of view that she has demonstrated through her activities as a novelist being reflected in the management of the JT Group. She has worked tirelessly to supervise our business execution from a fair and independent standpoint. She has also contributed enormously to improving corporate governance in the Group through actively providing proposals and advice to the Board of Directors and the Advisory Panel on Nomination and Compensation of the Group. We believe her wide-ranging experience and broad knowledge are Indispensable for our management going forward.

Koichiro Watanabe
Outside Director (Independent Outside Director)

Date of birth: April 16, 1953
Term of office:
2 years from March 2020
Number of shares held: 0

April	**1976**	Joined The Dai-ichi Mutual Life Insurance Company
July	**2001**	Director, The Dai-ichi Mutual Life Insurance Company
April	**2004**	Managing Director, The Dai-ichi Mutual Life Insurance Company
July	**2004**	Managing Executive Officer, The Dai-ichi Mutual Life Insurance Company
July	**2007**	Director and Managing Executive Officer, The Dai-ichi Mutual Life Insurance Company
April	**2008**	Director and Senior Managing Executive Officer, The Dai-ichi Mutual Life Insurance Company
April	**2010**	Representative Director and President, The Dai-ichi Life Insurance Company, Limited
October	**2016**	Representative Director and President, Dai-ichi Life Holdings, Inc.
April	**2017**	Representative Director and Chairman of the Board, Dai-ichi Life Holdings, Inc. (Current Position) Representative Director and Chairman of the Board, The Dai-ichi Life Insurance Company, Limited (Current Position)
March	**2018**	Outside Director of the Company (Current Position)
May	**2019**	Vice Chair, Director, Keidanren (Japan Business Federation) (Current Position)

Significant Concurrent Positions Outside the Company:
Representative Director and Chairman of the Board, Dai-ichi Life Holdings, Inc.
Representative Director and Chairman of the Board, The Dai-ichi Life Insurance Company, Limited
Vice Chair, Director, Keidanren (Japan Business Federation)

Mr. Watanabe was appointed as our Outside Director in March 2018. We have benefited from his outstanding experience in corporate management which, over the course of many years, he has used to drive business operations that successfully combined both healthy financials and high profitability, being reflected in the management of the JT Group. He has worked tirelessly to supervise business execution from a fair and independent standpoint. He has also contributed enormously to improving corporate governance in the Group through actively providing proposals and advice to the Board of Directors and the Advisory Panel on Nomination and Compensation of the Group. He has abundant experience in working to strengthen the governance structure. He also has objective, wide-ranging insight from an investor perspective; and is well versed with capital markets. We believe these attributes to remain indispensable for the Group going forward.

Yukiko Nagashima
Outside Director (Independent Outside Director)

Date of birth: April 4, 1961
Term of office:
2 years from March 2020
Number of shares held: 0

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

Significant Concurrent Positions Outside the Company:
Standing Audit and Supervisory Board Member, Recruit Holdings Co., Ltd.
Standing Audit and Supervisory Board Member, Recruit Co., Ltd.

Ms. Nagashima has been our Outside Director since March 2019. We have benefited from her experience in corporate management and execution of business in a wide range of fields, such as emerging businesses and temporary staffing. Her objective point of view based on her experience as a Member of the Audit & Supervisory Boards is reflected in the management of the JT Group. She has worked tirelessly to supervise business execution from a fair and independent standpoint. She has also contributed enormously to improving corporate governance in the Group through actively providing proposals and advice to the Board of Directors and the Advisory Panel on Nomination and Compensation of the Group. We believe that her experience and knowledge from the perspectives of both management and audit will be indispensable in the Group's management going forward.

Five Audit & Supervisory Board Members (including three Outside Audit & Supervisory Board Members)

As of March 19, 2020

Ryoko Nagata

Standing Audit & Supervisory Board Member

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

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

Ms. Nagata was appointed as an Audit & Supervisory Board Member of the JT Group in March 2018. She has contributed in the Group's auditing through leveraging her abundant experience and her wide-ranging insights with regard to the Group's business operations across operational businesses and internal departments. We believe her experience and knowledge will be indispensable to the improvement of the corporate governance of the Group going forward.

Hiroshi Yamamoto

Standing Audit & Supervisory Board Member

Date of birth: November 29, 1963
Term of office: 4 years from March 2019
Number of shares held: 2,600

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

Mr. Yamamoto has served in such roles as the Vice President of the Non-Tobacco Material Procurement Division of the Tobacco Business and as Vice President of the Operational Review and Business Assurance. He particularly played an important role in the latter position by enhancing the Group's corporate governance in its business operations. We believe he will fulfill his duties as an Audit & Supervisory Board Member in relation to the effective auditing of the Group through his detailed, deep and wide-ranging knowledge as well as experience across all business operations and in direct departments.

Toru Mimura

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

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

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

Significant Concurrent Positions Outside the Company:
Attorney at Law, Shiba International Law Offices

Mr. Mimura has deep knowledge of such fields as finance, global risk management, geopolitics and corporate law through his extensive experience over many years of serving in a wide range of important positions in ministries and bureaus, in addition to his role as research institute chairman. We believe that his broad and deep knowledge can make a significant contribution to the effective auditing of the JT Group in this highly uncertain business environment. In addition, we believe his roles as Standing Audit & Supervisory Board Member and Outside Audit & Supervisory Board Member facilitated improvements to auditing from a third-party perspective and led to a strengthening of the Group's corporate governance, for which reason we propose his election as Outside Audit & Supervisory Board Member.

Mr. Mimura meets all requirements for becoming an Independent Director prescribed by the Tokyo Stock Exchange, Inc. However, the JT Group does not intend to appoint him as our Independent Director, taking into account the Group's prescribed criteria of independence and his professional experience at the Ministry of Finance. It has been more than eight years since Mr. Mimura resigned from his post at the Ministry of Finance.

Hiroshi Obayashi

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

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

April	1970	Judicial Apprentice
April	1972	Appointed as Public Prosecutor
May	2001	Director-General of the Rehabilitation Bureau, Ministry of Justice
January	2002	Deputy Vice-Minister of Justice, Ministry of Justice
June	2004	Director-General of the Criminal Affairs Bureau, Ministry of Justice
June	2006	Vice-Minister of Justice, Ministry of Justice
July	2007	Superintending Prosecutor, Sapporo High Public Prosecutors' Office
July	2008	Superintending Prosecutor, Tokyo High Public Prosecutors' Office
June	2010	Prosecutor-General
March	2011	Registered as Attorney at Law
April	2011	Outside Audit & Supervisory Board Member, Daiwa Securities Co., Ltd. (Current Position)
June	2013	Outside Director, Mitsubishi Electric Corporation (Current Position)
June	2014	Outside Audit & Supervisory Board Member, Nippon Steel & Sumitomo Metal Corporation (Current Nippon Steel Corporation) (Current Position)
March	2015	Outside Audit & Supervisory Board Member of the Company (Current Position)

Significant Concurrent Positions Outside the Company:
Attorney at Law, Obayashi Law Office
Outside Audit & Supervisory Board Members, Daiwa Securities Co. Ltd.
Outside Director, Mitsubishi Electric Corporation
Outside Audit & Supervisory Board Members, Nippon Steel Corporation

Mr. Obayashi has been our Audit & Supervisory Board Member since March 2015. In addition to his extensive experience in the legal circles, Mr. Obayashi has significant experience as an Outside Director and Outside Audit & Supervisory Board Member across a wide range of industries. We consider his deep knowledge and experience to be indispensable to improving the Group's corporate governance going forward. We also believe that he can fulfill his duties as Outside Audit & Supervisory Board Member for the aforementioned reasons and the fact that he has sufficiently carried out his responsibilities as an Audit & Supervisory Board Member of the JT Group, despite having no experience of being involved in company management other than being an Outside Audit & Supervisory Board Member.

Koji Yoshikuni

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

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

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

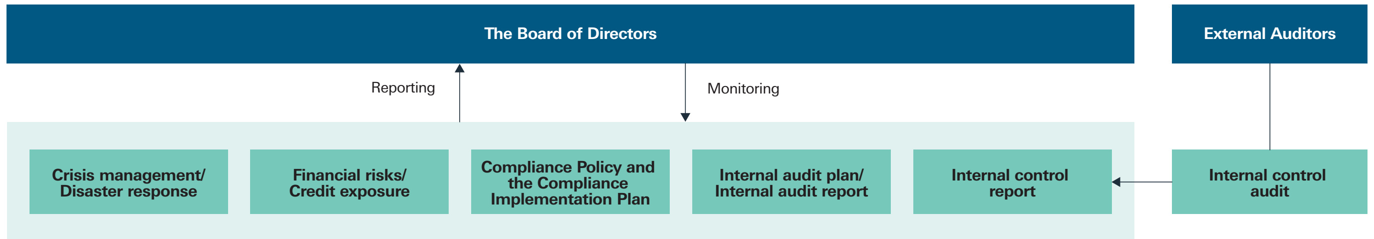
Mr. Yoshikuni has served in such roles at Japan Broadcasting Corporation as the Director Responsible for Finance of News Department, Chief of Secretariat for Board of Governors, and Executive Director. He has knowledge of politics and economics cultivated over long years in his journalist career as well as management experience that make him well-versed with all business operations and internal departments. We believe him to utilize his knowledge to play a significant role, as an Audit & Supervisory Board Member, in improving the Group's corporate governance.

Internal Control System & Risk Management System

Overview

The JT Group strives to optimize its system to conduct appropriate business operation by reinforcing internal control including compliance, internal audit and risk management. We regularly report any information related to these internal controls to the Board of Directors. In addition, we have the Auditor's Office, a department reporting to the Audit & Supervisory Board, to help our Audit & Supervisory Board Members effectively perform their duties. The JT Group works with its Group companies to enhance the framework for compliance (including the concern reporting system), credible financial reporting, risk management and internal audit.

Internal Control Framework



Compliance

The JT Group created a Code of Conduct based on our internal guidelines approved by the Board of Directors. Under the Code of Conduct, we expect all directors and employees to fully comply with applicable laws, our Articles of Incorporation, social norms and other compliance standards. In addition, the Board of Directors has established a framework as described below to ensure fair and effective compliance practices.

- Set up the JT Group Compliance Committee, which reviews and discusses compliance-related matters as well as reports directly to the Board of Directors
- Appoint an Executive Officer responsible for the Compliance Office
- Deliberate the Annual Compliance Plan and its action plans approved by the Board of Directors.
- Report the status of implemented compliance initiatives to the Board of Directors

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

The JT Group has both internal and external hotlines, which employees can use to consult or report any violations or possible violations of the JT Group Code of Conduct. The Compliance Office is responsible for investigating reported cases and implementing corrective measures after discussing with the relevant divisions. The JT Group Compliance Committee reviews any significant cases, and further reports to the Board of Directors if necessary.

The JT Group Compliance Committee is led by the Chairman of the Board, with the majority of the members consisting of external members. The JT Group Compliance Committee met three times in 2019, and discussed initiatives to promote compliance throughout the Group among other matters.

Credible Financial Reporting

The JT Group has introduced an internal control system in accordance with the Financial Instruments and Exchange Act and other standards, in order to ensure the credibility of the Group's financial reporting. In addition, the Group has created a dedicated division to review the internal control system and report the result of the assessment. The credibility of our financial reporting is confirmed by the external accounting auditor who makes an assessment of our internal control system based on the Internal Control Report we prepare.

Risk Management

Financial Risk Management

The JT Group has set up the internal guidelines for financial risk management. Our Group CFO presents the relevant reports to the Group CEO and the Board of Directors on a quarterly basis.

Crisis Management and Disaster Control

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

Other Risk Managements

In accordance with the Rules Defining the Extent of Responsibility and Authority, we delegate the management of other risks to relevant divisions, where they are to identify and monitor the risks in their areas of responsibility. These divisions will report significant risks to the CEO, together with a request for approval to implement countermeasures against them, whenever necessary.

Please refer to "Risk Factors" for more information on the JT Group's risks.

Internal Audit System

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

The Board of Directors, Audit & Supervisory Board and Executive Officers

As of March 19, 2020

The Board of Directors

Chairman of the Board

Yasutake Tango

Deputy Chairman of the Board

Mutsuo Iwai

Representative Directors

Masamichi Terabatake
Naohiro Minami
Kiyohide Hirowatari

Directors

Kazuhito Yamashita
Main Kohda*1
Koichiro Watanabe*1
Yukiko Nagashima*1

*1 Outside Directors under the Companies Act of Japan

The Audit & Supervisory Board

Standing Audit & Supervisory Board Members

Ryoko Nagata
Hiroshi Yamamoto
Toru Mimura*2

Audit & Supervisory Board Members

Hiroshi Obayashi*2
Koji Yoshikuni*2

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

Executive Officers

President

Masamichi Terabatake
Chief Executive Officer

Executive Vice Presidents

Naohiro Minami
Chief Financial Officer and Communications

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

Senior Vice Presidents

Kazuhito Yamashita
Compliance, Sustainability Management and General Affairs

Junichi Fukuchi
Chief Executive Officer of Japanese Tobacco Business, Tobacco Business Planning, Tobacco Business

Senior Vice Presidents

Yuki Maeda
Chief Financial Officer of Japanese Tobacco Business, Tobacco Business

Eiichi Kiyokawa
Sales, Tobacco Business

Kenji Ogura
Corporate, Scientific & Regulatory Affairs, Tobacco Business

Chigusa Ogawa
Leaf Procurement, Tobacco Business

Yasuhiro Nakajima
Head of RRP Japan Office, Tobacco Business

Shuichi Hirosue
Marketing, Tobacco Business

Hiroyuki Miki
R&D, Tobacco Business

Akihiro Koyanagi
Manufacturing, Tobacco Business

Toru Oguchi
Head of China Division, Tobacco Business

Toru Hijikata
Quality Assurance, Tobacco Business

Muneaki Fujimoto
President, Pharmaceutical Business

Shigenori Ohkawa
Head of Central Pharmaceutical Research Institute, Pharmaceutical Business

Hiromasa Furukawa
Food Business

Kei Nakano
Corporate Strategy

Takehisa Shibayama
Digitalization

Takanori Kikuchi
General Affairs

Koichi Mori
Human Resources

Hiroyuki Fukuda
Communications

Osamu Hirose
Legal

Hisato Imokawa
Sustainability Management

Members of the JTI Executive Committee

As of January 1, 2020

Eddy Pirard
President and Chief Executive Officer

Koji Shimayoshi
Executive Vice President and Deputy CEO

Roland Kostantos
Chief Operating Officer

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

Howard Parks
Senior Vice President, People & Culture, and Chief Compliance Officer

Daniel Torras
Senior Vice President, Reduced-Risk Products

Takehiko Tsutsui
Senior Vice President, Business Development and Corporate Strategy

Suzanne Wise
Senior Vice President, Corporate Affairs and Communications

Wade Wright
Senior Vice President, Legal and Regulatory Affairs

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

Yves Barbier
Senior Vice President, Marketing and Sales

Antoine Ernst
Senior Vice President, Chief Transformation Officer

Stefan Fitz
Regional President, Western Europe

Marchant Kuys
Regional President, Americas

Hiroyuki Miki
Senior Vice President, R&D, Chief Quality Officer

Jorge da Motta
Regional President, Asia Pacific

Andrew Newton
Senior Vice President, Global Supply Chain

Kevin Tomlinson
Regional President, Eastern Europe

FINANCIAL INFORMATION

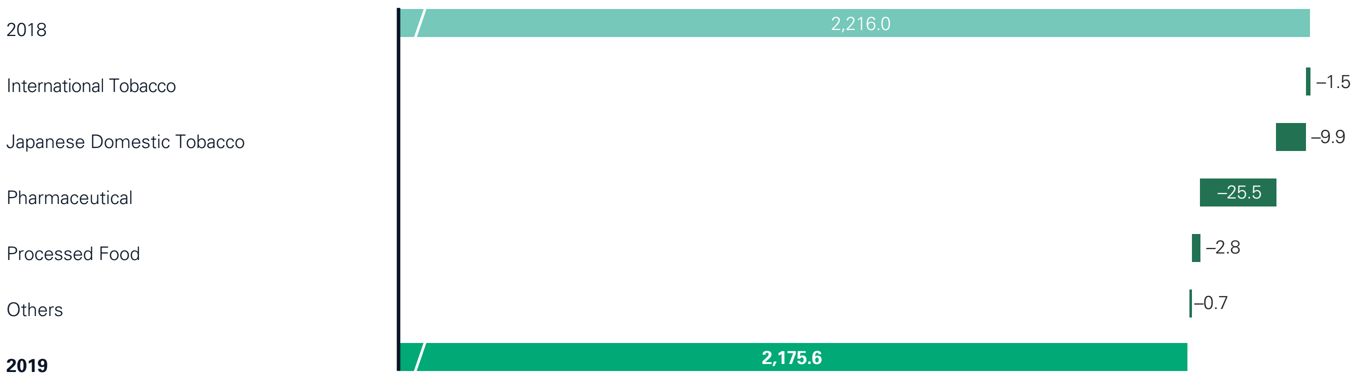
Financial Review

Analysis of the Results

Results for the fiscal year ended December 31, 2019

Revenue*1

Billions of yen



Revenue decreased 40.3 billion yen or 1.8% year-on-year to 2,175.6 billion yen mainly due to lower revenue in the Japanese domestic tobacco business, pharmaceutical business and processed food business. In the international tobacco business, the solid performance driven by price/mix contribution was offset by currency headwinds.

Adjusted Operating Profit*2/Operating Profit

Billions of yen

Adjusted operating profit decreased 79.5 billion yen or 13.4% year-on-year to 515.9 billion yen, mainly due to unfavorable currency movements in the international tobacco business.

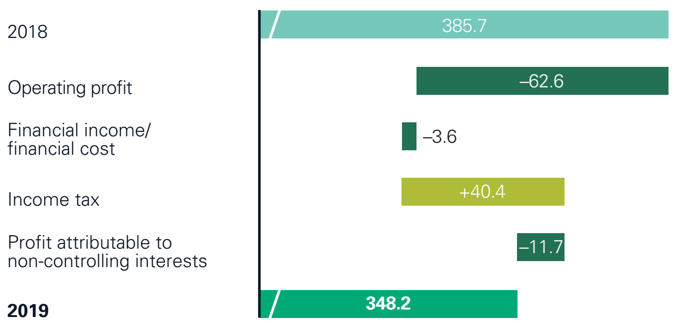
- In the international tobacco business, adjusted operating profit declined. Unfavorable currency movements and further investments in recently acquired businesses and in RRP offset price/mix and positive volume contribution.
- In the Japanese domestic tobacco business, adjusted operating profit declined due to an impairment of capsule manufacturing machines for low-temperature heating products and the top-line decline, which more than offset the positive cigarette price/mix variance.
- In the pharmaceutical business, adjusted operating profit declined due to the revenue decline.

Adjusted operating profit at constant foreign currency increased 0.9% year-on-year.

Operating profit decreased 11.1% year-on-year to 502.4 billion yen due to a decrease in adjusted operating profit, a decline in proceeds from sales of real estate assets, a higher trademark amortization and recognition of restructuring costs related to the transformation in the international tobacco business. This was in spite of one-time compensation gains related to the termination of the six anti-HIV drugs license agreements in the pharmaceutical business.

Profit*3

Billions of yen



Profit decreased 37.5 billion yen or 9.7% year-on-year to 348.2 billion yen, due to the decline in operating profit and increase in financing costs. This was partially offset by favorable contributions from one-time factors leading to a lower effective tax rate.

- Financial costs increased (negative impact in the graph) mainly due to an increase in interest expense associated with demand for working capital in the international tobacco business.
- Income tax expenses decreased (positive impact in the graph) due to a lower effective tax rate and decline in profit before income tax.

Revenue by Business Segment

	Billions of yen	
	2018	2019
Revenue	2,216.0	**2,175.6**
International Tobacco	1,312.3	**1,310.9**
Core revenue*4	1,250.7	**1,253.0**
Japanese Domestic Tobacco	621.4	**611.5**
Core revenue*5	582.4	**568.9**
Pharmaceutical	114.0	**88.5**
Processed Food	161.4	**158.6**
Others	6.8	**6.1**

Average Exchange Rate

	2018	2019
USD/JPY	110.44	**109.03**
USD/RUB	62.68	**64.74**
USD/GBP	0.75	**0.78**
USD/EUR	0.85	**0.89**

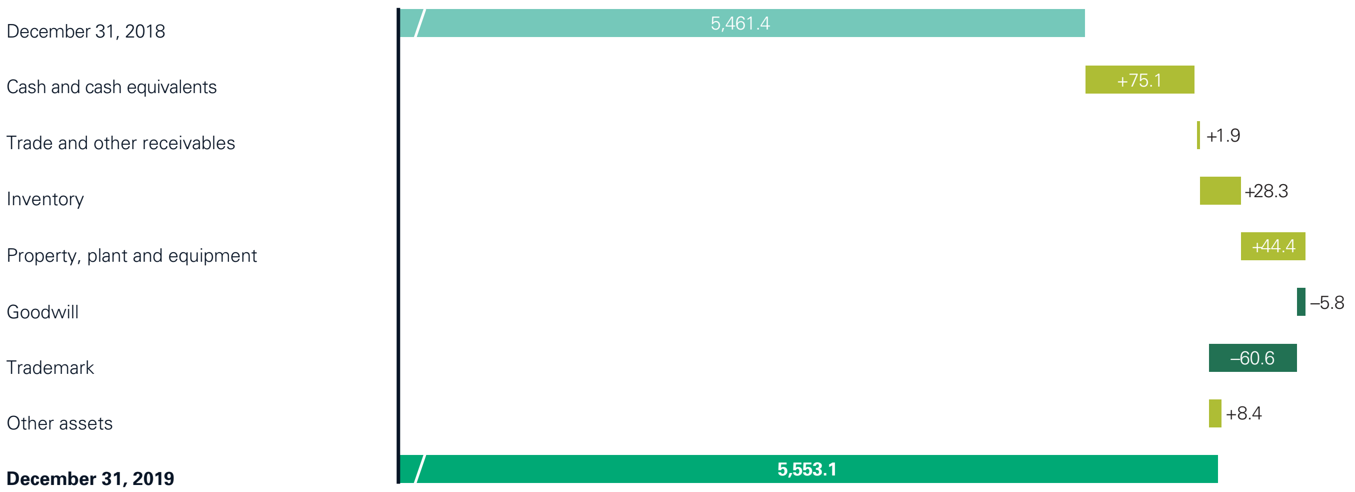
Adjusted Operating Profit and Operating Profit by Business Segment

	Billions of yen	
	2018	2019
Consolidated: Operating profit	565.0	**502.4**
International Tobacco	339.5	**274.0**
Japanese Domestic Tobacco	192.5	**171.0**
Pharmaceutical	26.3	**72.7**
Processed Food	2.9	**5.5**
Others/Elimination	3.8	**(20.8)**
Adjustments, Total*6	(30.5)	**(13.6)**
International Tobacco	(45.0)	**(66.7)**
Japanese Domestic Tobacco	(16.5)	**(16.2)**
Pharmaceutical	(2.1)	**56.8**
Processed Food	(1.2)	**0.1**
Others/Elimination	34.4	**12.5**
Consolidated: Adjusted operating profit	595.5	**515.9**
International Tobacco	384.5	**340.8**
Japanese Domestic Tobacco	209.0	**187.2**
Pharmaceutical	28.4	**15.9**
Processed Food	4.1	**5.4**
Others/Elimination	(30.6)	**(33.4)**

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

*1 Excludes tobacco excise and other similar taxes, as well as agency transactions, in which the JT Group acts as an agent.
2 Adjusted operating profit = Operating profit + amortization cost of acquired intangibles arising from business acquisitions + adjusted items (income and costs).
*3 Profit attributable to owners of the parent
*4 Includes waterpipe tobacco and RRP, but excludes revenue from distribution, contract manufacturing and other peripheral businesses.
*5 Includes revenue from domestic duty free, the China business, little cigars and RRP, but excludes revenue from distribution of imported tobacco in the Japanese domestic tobacco business among others.
6 Amortization cost of acquired intangibles arising from business acquisitions ± adjusted items (income and costs).
* Adjusted items (income and costs) = Impairment losses on goodwill ± restructuring income and costs ± others

Consolidated Statement of Financial Position (Assets) Billions of yen



Total assets increased 91.7 billion yen to 5,553.1 billion yen, mainly led by the increase in cash and cash equivalents as a result of improvement in business activities.

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

Total liabilities increased 48.5 billion yen to 2,809.5 billion yen mainly due to an increase in lease obligations associated with the adoption of IFRS 16.

Total equity increased 43.2 billion yen to 2,743.6 billion yen.

1. Significant Accounting Policies

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

The JT Group has applied IFRS 16 since 2019. Please refer to page 106 for more details on the significant accounting policies.

2. Non-GAAP Financial Measures

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

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

Core Revenue

For the tobacco business, core revenue is additionally disclosed as a breakdown of revenue. Specifically, the core revenue for the Japanese domestic tobacco business includes revenue from domestic duty free, the China business, little cigars and RRP, but excludes revenue from distribution of imported tobacco in the Japanese domestic tobacco business among others.

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

Adjusted Operating Profit

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

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

3. Analysis of Consolidated Financial Results for 2019

- "Revenue," "Adjusted Operating Profit/Operating Profit" and "Profit" pages 92 to 93
- "Assets," "Debt" and "Equity" page 94
- Please refer to "Review of Operations" for an analysis of financial results by business segment.

Results and Plans of Capital Expenditures

Capital expenditures include outlays on property, plant and equipment such as land, buildings and structures, machinery as well as vehicles and others; and intangible assets such as goodwill, trademark, software and others. These capital expenditures are necessary for enhancing the productivity of our factories and other facilities; strengthening our competitiveness; and operating in various business fields. In 2019, total capital expenditures amounted to 131.4 billion yen.

Capital Expenditure

	Billions of yen	
	2018	2019
Total	159.8	**131.4**
International Tobacco	75.7	**78.3**
Japanese Domestic Tobacco	55.4	**34.8**
Pharmaceutical	11.3	**7.0**
Processed Food	12.7	**6.1**
Others/Elimination	4.6	**5.2**

In the international tobacco business, capital expenditures amounted to 78.3 billion yen, which was spent on manufacturing facilities overseas. In the Japanese domestic tobacco business, capital expenditures amounted to 34.8 billion yen which was mainly spent on the RRP-related manufacturing facilities. In the pharmaceutical business, capital expenditures amounted to 7.0 billion yen which was primarily spent on the construction and equipping of a joint facility of Toxicology Research Laboratories and Pharmaceutical Frontier Research Laboratories. In the processed food business, capital expenditures amounted to 6.1 billion yen, which was spent on constructing new buildings and facilities to enhance and maintain production capacity and the optimal production system. These capital expenditures were internally funded through cash generated by operations and borrowings.

Plans for New Installations and Disposal of Facilities

Based on the JT Group's management principles, we will prioritize our mid- to long-term resource allocations on business investments for mid- to long-term sustainable profit growth. We position the international and Japanese domestic tobacco businesses as our core business and profit growth drivers and place top priority on business investments that will lead to their sustainable profit growth. Meanwhile, regarding the pharmaceutical and processed food businesses, we will strive to strengthen foundations that will lead to future profit contribution and will make investments to that end. Based on this policy, we estimate our capital expenditure plan to total 144.0 billion yen for 2020. In addition, we are planning to sell our fixed asset related to JT headquarters building within 2020. The amount of sale is to be confirmed.

As the JT Group companies have wide-ranging plans for their capital expenditure, we disclose the figures by segment. Our actual capital expenditures may significantly differ from the planned figures mentioned above, due to a number of factors, including those mentioned in "Risk Factors."

4. Dividends

The year-end dividends for 2019 were 77 yen per share. Including interim dividends per share of 77 yen, total annual dividends per share rose to 154 yen per share, a 4 yen increase year-on-year.

The year-end dividends related to the current year are recognized in the following year for accounting purposes. The year-end dividend related to 2018 (record date of December 31, 2018) and the interim dividends for 2019 (record date of June 30, 2019) are recorded in the financial statements for 2019. Please refer to page 138 for more details.

5. Capital Management

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

The JT Group's financial policy maintains a solid financial base. This provides us with the capacity to withstand any adversity arising out of a volatile environment, such as economic crisis. It also allows for sufficient flexibility to capture attractive investment opportunities. The JT Group monitors financial indicators in order to maintain a well-balanced capital structure that ensures an appropriate return on equity and a financial base for future investment. We monitor credit ratings for a solid financial base and ROE (Return On Equity) for profitability as well as internal and external environment fluctuation. The JT Group manages net interest-bearing debt, where cash and cash equivalents are deducted from interest-bearing debt, and capital (the part attributable to owners of the parent company), which are detailed below as of each year-end:

Capital Management

	Billions of yen	
	As of Dec. 31, 2018	**As of Dec. 31, 2019**
Interest-bearing debt	987.6	**974.5**
Cash and cash equivalents	(282.1)	**(357.2)**
Net interest-bearing debt	705.5	**617.3**
Capital (equity attributable to owners of the parent company)	2,630.6	**2,662.7**

Capital Expenditure Plan

	2020 (Billions of yen)	Main purpose of investing	Funding
International Tobacco	80.0	RRP-related investment and improvement in product specifications	Internally funded
Japanese Domestic Tobacco	29.0	RRP- and IT-related investment	Same as above
Pharmaceutical	10.0	Maintenance and reinforcement of R&D	Same as above
Processed Food	14.0	Increase in production capacity, increase of productivity, maintenance and replacement of facilities	Same as above

Share Buy-back

The JT Group held 226,196,566 shares of common stock as treasury stock as of December 31, 2019, amounting to 11.31% of the total number of shares issued.

A repurchase of our shares requires cash outlays. In order to repurchase our shares in a flexible manner, we amended the Articles of Incorporation at the Ordinary General Meeting of Shareholders held on June 24, 2004 allowing us to repurchase based on a decision made by the Board of Directors. We may continue to hold the repurchased shares as treasury stock or use them for other purposes. Stock repurchase provides our management with an additional option for increasing flexibility and speed in capital management in order to adapt to a rapidly changing business environment.

6. Financial Activities

The JT Group's Treasury Division provides Group-wide support to enable secure and efficient financing activities. We are exposed to various financial risks: credit risks, liquidity risks, foreign exchange risks, interest rate risks and market price fluctuation risks. We conduct our treasury activities pursuant to a set of Group-wide financial risk management policies and the results are reported to the Group CEO and the Board of Directors on a regular basis. Please refer to page 146 for more details.

Intra-group Cash Management

To maximize the JT Group's overall cash efficiency, we prioritize utilizing internal financing mainly through the Cash Management Systems (CMS) within our Group, where legally permissible and economically viable.

External Funding

We basically found our short-term working capital needs through short-term borrowings from financial institutions, commercial paper or a combination of both. We fund our mid- to long-term capital needs through long-term borrowings from financial institutions, bonds, equity or a combination of those previously stated.

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

External Investments

The JT Group always makes its financial investments by taking into account safety, liquidity and optimal yield. We do not allow any speculative dealings in pursuit of profit margin. We also report the investment results to the Group CEO and the Board of Directors on a regular basis.

7. 2019 and 2018 Cash Flow Results

Cash and cash equivalents at the end of 2019 increased by 75.1 billion yen from the end of 2018 to 357.2 billion yen. Cash and cash equivalents at the end of 2018 were 282.1 billion yen.

Cash Flows in Operating Activities

Net cash flows from operating activities during 2019 were 540.4 billion yen. This was mainly due to payments of Japanese domestic and international tobacco excise and income taxes and the generation of a stable cash inflow from the total tobacco business. Net cash flows from operating activities in 2018 were 461.4 billion yen.

Cash Flows in Investing Activities

Net cash flows used in investing activities during 2019 were 123.6 billion yen. This was mainly due to an increase in property, plant and equipment. Net cash flows used in investing activities in 2018 were 383.3 billion yen.

Cash Flows in Financing Activities

Net cash flows used in financing activities during 2019 were 333.8 billion yen. Bonds issued in 2019 partially offset the increase of dividends per share, buybacks and repayments of borrowings. Net cash flows used in financing activities in 2018 were 62.4 billion yen.

8. Liquidity

We have historically had, and expect to continue to have, significant cash flows from operating activities. We expect that cash generated from operating activities will continue to be stable and cover funds needed for daily business activities. The JT Group had 470.4 billion yen in committed facilities for both domestic and international major financial institutions on December 31, 2019, of which 100% was unused. In addition, we have a commercial paper program, uncommitted facilities, a domestic bond shelf registration and EMTN program.

Long-term Debt

Our bonds issued (including the current portion) as of December 31, 2018 and December 31, 2019 accounted for 610.4 billion yen and 666.6 billion yen, respectively. Our long-term borrowings as loans from financial institutions (including the current portion) accounted for 129.3 billion yen in 2018 and 115.3 billion yen in 2019. Maturities of interest bearing debts are shown in the table below.

As of December 31, 2019, our long-term debt was rated A1 by Moody's Japan K.K. (Moody's), AA- by Standard & Poor's Ratings Japan K.K. (S&P) and AA by Rating and Investment Information Inc. (R&I), with a "stable" outlook from Moody's, a "negative" outlook from S&P and a "stable" outlook from R&I.

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

Short-term Debt

Our short-term borrowings totaled 166.0 billion yen as of December 31, 2018 and 192.6 billion yen as of December 31, 2019. Commercial paper totaled 72.0 billion yen as of December 31, 2018 and 0 yen as of December 31, 2019.

Liquidity

Billions of yen

Year ended December 31, 2019	Book Value	Due within 1 year	Due after 1 year through 2 years	Due after 2 years through 3 years	Due after 3 years through 4 years	Due after 4 years through 5 years	Due after 5 years
Short-term borrowings as loans	192.6	192.6	—	—	—	—	—
Long-term borrowings as loans (current portion)	11.6	11.6	—	—	—	—	—
Bonds (current portion)	80.0	80.0	—	—	—	—	—
Long-term borrowings as loans	103.7	—	11.2	41.2	11.2	20.1	20.2
Bonds	586.6	—	82.2	30.0	117.5	—	360.4
Total	**974.5**	**284.1**	**93.4**	**71.2**	**128.7**	**20.1**	**380.6**

Consolidated Financial Statements

Consolidated Statement of Financial Position

Japan Tobacco Inc. and Consolidated Subsidiaries
As of December 31, 2018 and 2019

Millions of yen

Assets	2018	2019
Current assets		
Cash and cash equivalents (Note 7)	282,063	**357,158**
Trade and other receivables (Note 8)	456,591	**458,513**
Inventories (Note 9)	649,238	**677,586**
Other financial assets (Note 10)	35,633	**21,943**
Other current assets (Note 11)	385,872	**410,443**
Subtotal	1,809,396	**1,925,643**
Non-current assets held-for-sale (Note 12)	10	**30**
Total current assets	1,809,406	**1,925,673**
Non-current assets		
Property, plant and equipment (Note 13, 15)	758,841	**803,239**
Goodwill (Note 14)	2,008,416	**2,002,595**
Intangible assets (Note 14)	503,076	**440,434**
Investment property (Note 16)	17,558	**16,588**
Retirement benefit assets (Note 22)	57,140	**67,377**
Investments accounted for using the equity method	66,807	**52,903**
Other financial assets (Note 10)	115,046	**109,568**
Deferred tax assets (Note 17)	125,109	**134,696**
Total non-current assets	3,651,993	**3,627,397**
Total assets	5,461,400	**5,553,071**

Millions of yen

Liabilities and equity	2018	2019
Liabilities		
Current liabilities		
Trade and other payables (Note 18)	380,516	**408,597**
Bonds and borrowings (Note 19)	250,466	**284,135**
Income tax payables	72,449	**69,543**
Other financial liabilities (Note 19)	4,486	**21,862**
Provisions (Note 20)	6,078	**16,570**
Other current liabilities (Note 21)	716,190	**701,050**
Total current liabilities	1,430,185	**1,501,757**
Non-current liabilities		
Bonds and borrowings (Note 19)	727,314	**690,367**
Other financial liabilities (Note 19)	10,067	**41,062**
Retirement benefit liabilities (Note 22)	321,838	**320,614**
Provisions (Note 20)	3,780	**19,463**
Other non-current liabilities (Note 21)	179,274	**155,768**
Deferred tax liabilities (Note 17)	88,497	**80,430**
Total non-current liabilities	1,330,770	**1,307,702**
Total liabilities	2,760,955	**2,809,459**
Equity		
Share capital (Note 23)	100,000	**100,000**
Capital surplus (Note 23)	736,400	**736,400**
Treasury shares (Note 23)	(442,829)	**(492,469)**
Other components of equity (Note 23)	(423,357)	**(431,741)**
Retained earnings	2,660,381	**2,750,506**
Equity attributable to owners of the parent company	2,630,594	**2,662,696**
Non-controlling interests	69,851	**80,916**
Total equity	2,700,445	**2,743,611**
Total liabilities and equity	5,461,400	**5,553,071**

Consolidated Statement of Income

Japan Tobacco Inc. and Consolidated Subsidiaries
Years Ended December 31, 2018 and 2019

		Millions of yen
	2018	2019
Revenue (Notes 6, 25)	2,215,962	**2,175,626**
Cost of sales (Notes 14, 22)	(933,034)	**(942,299)**
Gross profit	1,282,928	**1,233,326**
Other operating income (Note 26)	48,532	**95,725**
Share of profit in investments accounted for using the equity method	3,931	**5,011**
Selling, general and administrative expenses (Notes 12, 13, 14, 16, 22, 27, 33)	(770,407)	**(831,707)**
Operating profit (Note 6)	564,984	**502,355**
Financial income (Notes 28, 34)	5,754	**8,402**
Financial costs (Notes 22, 28, 34)	(39,252)	**(45,526)**
Profit before income taxes	531,486	**465,232**
Income taxes (Note 17)	(144,055)	**(103,609)**
Profit for the period	387,431	**361,622**
Attributable to		
Owners of the parent company	385,677	**348,190**
Non-controlling interests	1,755	**13,432**
Profit for the period	387,431	**361,622**
Earnings per share		
Basic (Yen) (Note 30)	215.31	**195.97**
Diluted (Yen) (Note 30)	215.20	**195.87**

Reconciliation from “Operating profit” to “Adjusted operating profit”

		Millions of yen
	2018	2019
Operating profit	564,984	**502,355**
Amortization cost of acquired intangibles arising from business acquisitions	61,772	**69,623**
Adjustment items (income)	(40,447)	**(84,467)**
Adjustment items (costs)	9,154	**28,415**
Adjusted operating profit (Note 6)	595,463	**515,927**

Consolidated Statement of Comprehensive Income

Japan Tobacco Inc. and Consolidated Subsidiaries
Years Ended December 31, 2018 and 2019

		Millions of yen
	2018	2019
Profit for the period	387,431	**361,622**
Other comprehensive income		
Items that will not be reclassified to profit or loss		
Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income (Notes 29, 34)	(8,215)	**(2,484)**
Remeasurements of defined benefit plans (Notes 22, 29)	(3,195)	**(2,811)**
Total of items that will not be reclassified to profit or loss	(11,410)	**(5,295)**
Items that may be reclassified subsequently to profit or loss		
Exchange differences on translation of foreign operations (Notes 29, 34)	(247,731)	**9,879**
Net gain (loss) on derivatives designated as cash flow hedges (Notes 29, 34)	1,012	**(391)**
Total of items that may be reclassified subsequently to profit or loss	(246,719)	**9,489**
Other comprehensive income (loss), net of taxes	(258,129)	**4,194**
Comprehensive income (loss) for the period	129,302	**365,816**
Attributable to		
Owners of the parent company	128,340	**352,953**
Non-controlling interests	962	**12,863**
Comprehensive income (loss) for the period	129,302	**365,816**

Consolidated Statement of Changes in Equity

Japan Tobacco Inc. and Consolidated Subsidiaries
Years Ended December 31, 2018 and 2019

Millions of yen

	Equity attributable to owners of the parent company				Other components of equity		
	Share capital	Capital surplus	Treasury shares	Subscription rights to shares	Exchange differences on translation of foreign operations	Net gain (loss) on derivatives designated as cash flow hedges	Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income
As of January 1, 2018	100,000	736,400	(443,636)	1,964	(207,884)	(88)	38,670
Profit for the period	—	—	—	—	—	—	—
Other comprehensive income (loss)	—	—	—	—	(247,034)	1,012	(8,239)
Comprehensive income (loss) for the period	—	—	—	—	(247,034)	1,012	(8,239)
Acquisition of treasury shares (Note 23)	—	—	(0)	—	—	—	—
Disposal of treasury shares (Note 23)	—	—	807	(691)	—	—	—
Share-based payments (Note 33)	—	—	—	274	—	—	—
Dividends (Note 24)	—	—	—	—	—	—	—
Changes in the scope of consolidation	—	—	—	—	—	—	—
Changes in the ownership interest in a subsidiary without a loss of control	—	—	—	—	—	—	—
Transfer from other components of equity to retained earnings	—	—	—	—	—	—	(860)
Other increase (decrease)	—	—	—	—	—	(480)	—
Total transactions with the owners	—	—	807	(417)	—	(480)	(860)
As of December 31, 2018	100,000	736,400	(442,829)	1,547	(454,918)	443	29,570
Profit for the period	**—**	**—**	**—**	**—**	**—**	**—**	**—**
Other comprehensive income (loss)	**—**	**—**	**—**	**—**	**10,553**	**(391)**	**(2,486)**
Comprehensive income (loss) for the period	**—**	**—**	**—**	**—**	**10,553**	**(391)**	**(2,486)**
Acquisition of treasury shares (Note 23)	**—**	**—**	**(50,001)**	**—**	**—**	**—**	**—**
Disposal of treasury shares (Note 23)	**—**	**—**	**361**	**(281)**	**—**	**—**	**—**
Share-based payments (Note 33)	**—**	**—**	**—**	**290**	**—**	**—**	**—**
Dividends (Note 24)	**—**	**—**	**—**	**—**	**—**	**—**	**—**
Changes in the scope of consolidation	**—**	**—**	**—**	**—**	**—**	**—**	**—**
Changes in the ownership interest in a subsidiary without a loss of control	**—**	**—**	**—**	**—**	**—**	**—**	**—**
Transfer from other components of equity to retained earnings	**—**	**—**	**—**	**—**	**—**	**—**	**(15,883)**
Other increase (decrease)	**—**	**—**	**—**	**—**	**—**	**(185)**	**—**
Total transactions with the owners	**—**	**—**	**(49,640)**	**10**	**—**	**(185)**	**(15,883)**
As of December 31, 2019	**100,000**	**736,400**	**(492,469)**	**1,556**	**(444,366)**	**(132)**	**11,201**

Millions of yen

	Equity attributable to owners of the parent company					
	Other components of equity					
	Remeasurements of defined benefit plans	Total	Retained earnings	Total	Non-controlling interests	Total equity
As of January 1, 2018	—	(167,338)	2,536,262	2,761,687	80,340	2,842,027
Profit for the period	—	—	385,677	385,677	1,755	387,431
Other comprehensive income (loss)	(3,075)	(257,337)	—	(257,337)	(792)	(258,129)
Comprehensive income (loss) for the period	(3,075)	(257,337)	385,677	128,340	962	129,302
Acquisition of treasury shares (Note 23)	—	—	—	(0)	—	(0)
Disposal of treasury shares (Note 23)	—	(691)	(116)	0	—	0
Share-based payments (Note 33)	—	274	2	275	36	311
Dividends (Note 24)	—	—	(259,724)	(259,724)	(1,914)	(261,638)
Changes in the scope of consolidation	—	—	—	—	139	139
Changes in the ownership interest in a subsidiary without a loss of control	—	—	495	495	(9,713)	(9,218)
Transfer from other components of equity to retained earnings	3,075	2,215	(2,215)	—	—	—
Other increase (decrease)	—	(480)	—	(480)	—	(480)
Total transactions with the owners	3,075	1,318	(261,558)	(259,433)	(11,452)	(270,885)
As of December 31, 2018	—	(423,357)	2,660,381	2,630,594	69,851	2,700,445
Profit for the period	**—**	**—**	**348,190**	**348,190**	**13,432**	**361,622**
Other comprehensive income (loss)	**(2,913)**	**4,763**	**—**	**4,763**	**(569)**	**4,194**
Comprehensive income (loss) for the period	**(2,913)**	**4,763**	**348,190**	**352,953**	**12,863**	**365,816**
Acquisition of treasury shares (Note 23)	**—**	**—**	**—**	**(50,001)**	**—**	**(50,001)**
Disposal of treasury shares (Note 23)	**—**	**(281)**	**(80)**	**0**	**—**	**0**
Share-based payments (Note 33)	**—**	**290**	**(19)**	**271**	**47**	**319**
Dividends (Note 24)	**—**	**—**	**(270,936)**	**(270,936)**	**(2,051)**	**(272,987)**
Changes in the scope of consolidation	**—**	**—**	**—**	**—**	**—**	**—**
Changes in the ownership interest in a subsidiary without a loss of control	**—**	**—**	**(1)**	**(1)**	**206**	**205**
Transfer from other components of equity to retained earnings	**2,913**	**(12,971)**	**12,971**	**—**	**—**	**—**
Other increase (decrease)	**—**	**(185)**	**—**	**(185)**	**—**	**(185)**
Total transactions with the owners	**2,913**	**(13,146)**	**(258,065)**	**(320,851)**	**(1,798)**	**(322,650)**
As of December 31, 2019	**—**	**(431,741)**	**2,750,506**	**2,662,696**	**80,916**	**2,743,611**

Consolidated Statement of Cash Flows

Japan Tobacco Inc. and Consolidated Subsidiaries
Years Ended December 31, 2018 and 2019

		Millions of yen
	2018	**2019**
Cash flows from operating activities		
Profit before income taxes	531,486	**465,232**
Depreciation and amortization	158,671	**183,852**
Impairment losses	8,454	**16,124**
Interest and dividend income	(5,751)	**(7,944)**
Interest expense	16,343	**27,557**
Share of profit in investments accounted for using the equity method	(3,931)	**(5,011)**
(Gains) losses on sale and disposal of property, plant and equipment, intangible assets and investment property	(34,905)	**(8,299)**
(Increase) decrease in trade and other receivables	(30,818)	**10,673**
(Increase) decrease in inventories	(53,058)	**(32,817)**
Increase (decrease) in trade and other payables	(4,618)	**28,294**
Increase (decrease) in retirement benefit liabilities	(8,864)	**(9,526)**
(Increase) decrease in prepaid tobacco excise taxes	(36,662)	**(21,864)**
Increase (decrease) in tobacco excise tax payables	53,408	**3,891**
Increase (decrease) in consumption tax payables	(11,026)	**29,592**
Other	8,969	**16,766**
Subtotal	587,697	**696,521**
Interest and dividends received	11,743	**15,340**
Interest paid	(13,685)	**(24,346)**
Income taxes paid	(124,366)	**(147,105)**
Net cash flows from operating activities	461,389	**540,410**
Cash flows from investing activities		
Purchase of securities	(36,705)	**(45,401)**
Proceeds from sale and redemption of securities	10,159	**77,200**
Purchase of property, plant and equipment	(138,605)	**(111,366)**
Proceeds from sale of investment property	46,868	**15,863**
Purchase of intangible assets	(20,205)	**(22,004)**
Payments into time deposits	(878)	**(218)**
Proceeds from withdrawal of time deposits	812	**409**
Payments for business combinations	(247,632)	**—**
Subsequent payments for past fiscal years' business combinations	(4,589)	**(40,127)**
Other	7,467	**2,073**
Net cash flows from investing activities	(383,307)	**(123,571)**
Cash flows from financing activities		
Dividends paid to owners of the parent company (Note 24)	(259,671)	**(270,871)**
Dividends paid to non-controlling interests	(1,747)	**(1,913)**
Capital contribution from non-controlling interests	109	**358**
Increase (decrease) in short-term borrowings and commercial paper (Note 32)	(133,849)	**(44,976)**
Proceeds from long-term borrowings (Note 32)	59,135	**—**
Repayments of long-term borrowings (Note 32)	(2,710)	**(11,568)**
Proceeds from issuance of bonds (Note 32)	341,516	**59,435**
Redemption of bonds (Note 32)	(54,086)	**—**
Repayments of lease liabilities (Note 32)	(1,637)	**(14,294)**
Acquisition of treasury shares	(0)	**(50,001)**
Payments for acquisition of interests in subsidiaries from non-controlling interests	(9,421)	**(1)**
Other	0	**0**
Net cash flows from financing activities	(62,360)	**(333,832)**
Net increase (decrease) in cash and cash equivalents	15,721	**83,008**
Cash and cash equivalents at the beginning of the period	285,486	**282,063**
Effect of exchange rate changes on cash and cash equivalents	(19,145)	**(7,913)**
Cash and cash equivalents at the end of the period (Note 7)	282,063	**357,158**

Notes to Consolidated Financial Statements

Japan Tobacco Inc. and Consolidated Subsidiaries
Years Ended December 31, 2018 and 2019

1. Reporting Entity

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

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

The Group's consolidated financial statements for the year ended December 31, 2019 were approved on March 19, 2020 by Masamichi Terabatake, President and Chief Executive Officer.

2. Basis of Preparation

(1) Compliance with IFRS

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

(2) Basis of Measurement

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

(3) Functional Currency and Presentation Currency

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

(4) Changes in Method of Presentation

(Consolidated Statement of Cash Flows)

"Subsequent payments for past fiscal years' business combinations," which were included in "Other" of "Cash flows from investing activities" on the consolidated statement of cash flows for the year ended December 31, 2018 have been presented separately to reflect the increase of materiality for the year ended December 31, 2019. In order to reflect the change in method of presentation, the consolidated statement of cash flows for the year ended December 31, 2018 has been reclassified.

Accordingly, ¥4,589 million included in "Other" of "Cash flows from investing activities" on the consolidated statement of cash flows for the year ended December 31, 2018 has been reclassified as "Subsequent payments for past fiscal years' business combinations."

3. Significant Accounting Policies

(1) Basis of Consolidation

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

A. Subsidiaries

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

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

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

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

B. Associates

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

C. Joint Arrangements

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

(2) Business Combination

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

(3) Foreign Currency Translation

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

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

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

(4) Financial Instruments

A. Financial Assets

(i) Initial Recognition and Measurement

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

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

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

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

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

(ii) Subsequent Measurement

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

(a) Financial Assets Measured at Amortized Cost

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

(b) Other Financial Assets

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

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

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

(iii) Derecognition

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

B. Impairment of Financial Assets

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

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

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

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

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

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

C. Financial Liabilities

(i) Initial Recognition and Measurement

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

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

(ii) Subsequent Measurement

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

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

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

(b) Financial Liabilities Measured at Amortized Cost

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

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

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

(iii) Derecognition

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

D. Offsetting of Financial Instruments

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

E. Derivatives and Hedge Accounting

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

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

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

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

(i) Fair Value Hedge

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

(ii) Cash Flow Hedge

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

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

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

(iii) Hedge of Net Investment in Foreign Operations

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

F. Fair Value of Financial Instruments

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

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

(5) Cash and Cash Equivalents

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

(6) Inventories

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

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

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

(7) Property, Plant and Equipment

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

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

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

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

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

(8) Goodwill and Intangible Assets

A. Goodwill

Goodwill is stated at acquisition cost less accumulated impairment losses.

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

B. Intangible Assets

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

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

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

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

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

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

(9) Leases

At inception of a contract, the Group assesses whether the contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The Group elects not to recognize right-of-use assets and lease liabilities for short-term leases within 12 months and leases of low-value assets.

If a contract is, or contains, a lease, except for short-term leases and leases of low-value assets, the Group recognizes right-of-use assets and lease liabilities on the consolidated statement of financial position at the commencement date. The Group recognizes the lease payments associated with short-term leases and leases of low-value assets as an expense on a straight-line basis over the lease term.

Right-of-use asset is measured by using the cost model and is stated at cost less accumulated depreciation and accumulated impairment losses.

An acquisition cost of a right-of-use asset includes the amount of the initial measurement of the lease liability, any lease payments made at or before the commencement date, and any initial direct costs. The right-of-use asset is depreciated using the straight-line method over its estimated useful life or lease term, whichever is shorter. The lease liability is initially measured at the present value of the lease payment that is not paid at the commencement date. The lease payments are apportioned between the financial cost and the reduction in the lease liability based on the effective interest method. The financial costs are recognized in the consolidated statement of income.

(10) Investment Property

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

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

(11) Impairment of Non-financial Assets

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

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

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

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

(13) Post-employment Benefits

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

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

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

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

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

(14) Share-based Payments

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

(15) Provisions

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

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

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

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

(16) Revenue

A. Revenue from Contracts with Customers

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

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

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

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

B. Interest Income

Interest income is recognized using the effective interest rate method.

C. Dividend Income

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

(17) Government Grants

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

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

(18) Borrowing Costs

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

(19) Income Taxes

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

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

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

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

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

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

Assets and liabilities are recognized as estimated amounts if uncertain tax position of income taxes arising from interpretation of tax laws and regulations is probable.

The Company and certain subsidiaries apply for the consolidated taxation system.

(20) Treasury Shares

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

(21) Earnings per Share

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

(22) Dividends

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

(23) Contingencies

A. Contingent Liabilities

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

B. Contingent Assets

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

(24) Adjusted Financial Measures

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

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

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

(Changes in Accounting Policies)

The Group has adopted the following new accounting standards, amended standards and new interpretations from the year ended December 31, 2019.

IFRS		Description of new standards and amendments
IFRS 16	Leases	Amendments to accounting treatment for lease arrangements
IAS 19	Employee Benefits	Clarifying treatment on a defined benefit plan curtailment or settlement

In adopting IFRS 16, the Group used a transition method by which the cumulative effect of initially adopting this standard was recognized at the date of initial application.

The lessee's weighted average incremental borrowing rate which applied to lease liabilities on the consolidated statement of financial position at the date of initial application is 4.1%.

The difference between the total amount of future minimum lease payments under non-cancellable operating leases (discounted by the lessee's incremental borrowing rate above) which were disclosed upon adopting IAS 17, "Leases" (hereinafter referred to as "IAS 17"), at the end of the consolidated year immediately before the initial application and the lease liabilities on the consolidated statement of financial position at the date of initial application is mainly due to the estimation difference of the lease term of lands and buildings for the period which exceeds the non-cancellable period.

The Group has adopted this standard for contracts that were previously identified as leases adopting IAS 17 and IFRIC 4, "Determining whether an Arrangement Contains a Lease" (hereinafter referred to as "IFRIC 4"), without reassessing whether a contract is, or contains, a lease at the date of initial application. The Group has not adopted this standard for contracts that were not previously identified as containing a lease adopting IAS 17 and IFRIC 4.

For leases previously classified as operating leases adopting IAS 17, the following practical expedients permitted as transition methods are adopted:

- A single discount rate is applied to a portfolio of leases with reasonably similar characteristics.
- Leases for which the lease term ends within 12 months of the date of initial application are accounted for in the same way as short-term leases.
- Initial direct costs are excluded from the measurement of right-of-use assets at the date of initial application.

As a result of the adoption of IFRS 16, "Assets" and "Liabilities" increased by ¥39,033 million at the date of initial application. There is an immaterial impact on operating profit and profit for the period.

In order to reflect the change in accounting method in accordance with the adoption of IFRS 16, "Repayments of finance lease obligations," which was presented in "Cash flows from financing activities" on the consolidated statement of cash flows for the year ended December 31, 2018, has been presented as "Repayments of lease liabilities" from the year ended December 31, 2019.

The effect of adopting IAS 19 on the consolidated financial statements is immaterial.

4. Significant Accounting Estimates and Judgments

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

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

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

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

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

Such indications include, but are not limited to significant changes with adverse effect on the results of past or projected business performance, significant changes in the use of acquired assets or in overall business strategy, and significant deteriorations in industry or economic trends. With regard to goodwill, an impairment test is conducted at least once a year, regardless of whether there are any indicators of impairment.

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

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

B. Post-employment Benefits

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

The present value of defined benefit obligations on each of these plans and the related service costs are calculated based on actuarial assumptions. These actuarial assumptions make use of estimates and judgments on a number of variables, including discount rates and inflation rate.

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

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

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

C. Provisions

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

These provisions are recognized based on best estimates of the expenditure required to settle the obligations, taking into account the pertinent risks and uncertainties which exist at the year-end for those obligations.

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

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

D. Income Taxes

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

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

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

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

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

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

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

E. Contingencies

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

The content of contingencies is described in "38. Contingencies."

5. New Accounting Standards Not Yet Adopted by the Group

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

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

IFRS		Mandatory adoption (From the year beginning)	To be adopted by the Group	Description of new standards and amendments
IFRS 3	Business Combinations	January 1, 2020	Year ending December 2020	Amendments to definition of "business"
IFRS 7	Financial Instruments Disclosures	January 1, 2020	Year ending December 2020	Amendments to provide relief from potential effects of the uncertainty caused by interest rate benchmark reform
IFRS 9	Financial Instruments	January 1, 2020	Year ending December 2020	Amendments to provide relief from potential effects of the uncertainty caused by interest rate benchmark reform
IFRS 17	Insurance Contracts	January 1, 2021	Year ending December 2021	Amendments to accounting treatment for insurance contracts
IAS 1	Presentation of Financial Statements	January 1, 2020	Year ending December 2020	Amendments to definition of "material"
		January 1, 2022	Year ending December 2022	Clarifying classification of liabilities as current or non-current
IAS 8	Accounting Policies, Changes in Accounting Estimates and Errors	January 1, 2020	Year ending December 2020	Amendments to definition of "material"
IAS 39	Financial Instruments Recognition and Measurement	January 1, 2020	Year ending December 2020	Amendments to provide relief from potential effects of the uncertainty caused by interest rate benchmark reform
IFRS 10 IAS 28	Sale or Contribution of Assets between an Investor and its Associate or Joint Venture	Not yet determined	Not yet determined	Amendments to accounting treatment for sale or contribution of assets between an investor and its associate or joint venture

6. Operating Segments

(1) Outline of Reportable Segments

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

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

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

(2) Revenues and Performances of Reportable Segments

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

Year ended December 31, 2018

Millions of yen

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

Year ended December 31, 2019

Millions of yen

	Reportable Segments							
	Domestic Tobacco	International Tobacco	Pharmaceuticals	Processed Food	Total	Other (Note 2)	Elimination	Consolidated
Revenue								
External revenue (Note 3)	**611,494**	**1,310,877**	**88,528**	**158,586**	**2,169,485**	**6,140**	**—**	**2,175,626**
Intersegment revenue	**7,270**	**27,626**	**—**	**1**	**34,897**	**7,333**	**(42,229)**	**—**
Total revenue	**618,764**	**1,338,503**	**88,528**	**158,587**	**2,204,382**	**13,473**	**(42,229)**	**2,175,626**
Segment profit (loss)								
Adjusted operating profit (Note 1)	**187,180**	**340,752**	**15,943**	**5,432**	**549,308**	**(33,478)**	**97**	**515,927**
Other items								
Depreciation and amortization (Note 3)	**59,276**	**108,378**	**5,936**	**7,586**	**181,176**	**2,909**	**(233)**	**183,852**
Impairment losses on other than financial assets	**7,751**	**5,765**	**1,471**	**220**	**15,207**	**917**	**—**	**16,124**
Reversal of impairment losses on other than financial assets	**—**	**91**	**—**	**—**	**91**	**—**	**—**	**91**
Share of profit (loss) in investments accounted for using the equity method	**16**	**4,863**	**—**	**10**	**4,889**	**122**	**—**	**5,011**
Capital expenditures (Note 4)	**34,793**	**78,295**	**6,979**	**6,142**	**126,209**	**5,609**	**(383)**	**131,434**

Reconciliation from "Adjusted operating profit" to "Profit before income taxes"

Year ended December 31, 2018

Millions of yen

	Reportable Segments							
	Domestic Tobacco	International Tobacco	Pharmaceuticals	Processed Food	Total	Other (Note 2)	Elimination	Consolidated
Adjusted operating profit (Note 1)	208,977	384,524	28,438	4,123	626,062	(30,440)	(159)	595,463
Amortization cost of acquired intangibles arising from business acquisitions	(16,245)	(45,527)	—	—	(61,772)	—	—	(61,772)
Adjustment items (income) (Note 5)	9	1,711	—	37	1,757	38,691	—	40,447
Adjustment items (costs) (Note 6)	(288)	(1,195)	(2,141)	(1,240)	(4,864)	(4,290)	—	(9,154)
Operating profit (loss)	192,453	339,514	26,297	2,919	561,183	3,960	(159)	564,984
Financial income								5,754
Financial costs								(39,252)
Profit before income taxes								531,486

Year ended December 31, 2019

Millions of yen

	Reportable Segments							
	Domestic Tobacco	International Tobacco	Pharmaceuticals	Processed Food	Total	Other (Note 2)	Elimination	Consolidated
Adjusted operating profit (Note 1)	**187,180**	**340,752**	**15,943**	**5,432**	**549,308**	**(33,478)**	**97**	**515,927**
Amortization cost of acquired intangibles arising from business acquisitions	**(16,245)**	**(53,378)**	**—**	**—**	**(69,623)**	**—**	**—**	**(69,623)**
Adjustment items (income) (Note 5)	**24**	**8,776**	**61,018**	**461**	**70,278**	**14,189**	**—**	**84,467**
Adjustment items (costs) (Note 6)	**—**	**(22,141)**	**(4,264)**	**(365)**	**(26,770)**	**(1,646)**	**—**	**(28,415)**
Operating profit (loss)	**170,960**	**274,008**	**72,697**	**5,528**	**523,193**	**(20,935)**	**97**	**502,355**
Financial income								**8,402**
Financial costs								**(45,526)**
Profit before income taxes								**465,232**

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

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

(Note 3) Depreciation and amortization of right-of-use assets included in "Depreciation and amortization" is as follows:

Millions of yen

	2019
Domestic Tobacco	**3,649**
International Tobacco	**10,314**
Pharmaceuticals	**456**
Processed Food	**741**
Other	**616**
Depreciation and amortization of right-of-use assets	**15,778**

(Note 4) The increase in right-of-use assets is excluded from the year ended December 31, 2019.

(Note 5) The breakdown of "Adjustment items (income)" is as follows:

Millions of yen

	2018	2019
Gain on transfer of pharmaceutical licenses	—	**60,518**
Restructuring incomes	39,284	**15,197**
Other	1,163	**8,752**
Adjustment items (income)	40,447	**84,467**

Restructuring incomes for the years ended December 31, 2018 and 2019 mainly relate to gains on sale of real estate. The breakdown of restructuring incomes is described in "26. Other Operating Income." Other for the year ended December 31, 2019 mainly relates to gains on fair value adjustment after the measurement period for assets and liabilities acquired in a business combination in the "International Tobacco Business."

(Note 6) The breakdown of "Adjustment items (costs)" is as follows:

Millions of yen

	2018	2019
Restructuring costs	7,934	**26,182**
Other	1,220	**2,233**
Adjustment items (costs)	9,154	**28,415**

Restructuring costs for the year ended December 31, 2018 mainly relate to disposal of real estate, business structure reform in the "Pharmaceutical Business" and rationalization of the production and distribution system in some markets in the "International Tobacco Business." Restructuring costs for the year ended December 31, 2019 mainly relate to business operation transformation in the "International Tobacco Business" and business structure reform in the "Pharmaceutical Business." Restructuring costs included in "Cost of sales" were ¥13 million for the year ended December 31, 2018.

Restructuring costs included in "Selling, general and administrative expenses" were ¥7,921 million and ¥26,182 million for the years ended December 31, 2018 and 2019, respectively. The breakdown of restructuring costs included in "Selling, general and administrative expenses" is described in "27. Selling, General and Administrative Expenses." Other for the year ended December 31, 2018 mainly relates to settlement of the litigation in September 2018. Other for the year ended December 31, 2019 mainly relates to disposal of real estate.

(3) Geographic Information

The regional breakdown of non-current assets as of December 31 is as follows:

Non-current Assets

	Millions of yen	
	2018	2019
Japan	835,386	**812,083**
Overseas	2,452,505	**2,450,772**
Consolidated	3,287,891	**3,262,855**

(Note) Non-current assets, exclusive of financial instruments, deferred tax assets and retirement benefits assets, are segmented by the location of the assets.

The regional breakdown of external revenue for each year is as follows:

External Revenue

	Millions of yen	
	2018	2019
Japan	822,070	**789,279**
Overseas	1,393,892	**1,386,347**
Consolidated	2,215,962	**2,175,626**

(Note) Revenue is segmented by the sales destination.

(4) Major Customers Information

The "International Tobacco Business" of the Group sells products to the Megapolis Group that engages in distribution and wholesale business in Russia and other countries. The external revenues from the Megapolis Group were ¥249,797 million (11.3% of consolidated revenue) for the year ended December 31, 2018 and ¥235,093 million (10.8% of consolidated revenue) for the year ended December 31, 2019.

7. Cash and Cash Equivalents

The breakdown of "Cash and cash equivalents" as of December 31 is as follows:

	Millions of yen	
	2018	2019
Cash and deposits	234,263	**260,908**
Short-term investments	47,800	**96,249**
Total	282,063	**357,158**

Cash and cash equivalents are classified as financial assets measured at amortized cost.

The Group's Iranian subsidiaries' ability to remit funds outside of Iran is restricted mainly due to international sanctions imposed on Iran. "Cash and cash equivalents" include ¥24,772 million as of December 31, 2018 and ¥48,675 million as of December 31, 2019 held by the Group's Iranian subsidiaries.

JTI-Macdonald Corp. (hereinafter referred to as "JTI-Mac"), the Company's Canadian subsidiary, is subject to certain restrictions on the use of funds other than in the ordinary course of business due to the adoption of the "Companies' Creditors Arrangement Act." "Cash and cash equivalents" as of December 31, 2019 includes cash and cash equivalents of ¥19,085 million held by JTI-Mac.

8. Trade and Other Receivables

The breakdown of "Trade and other receivables" as of December 31 is as follows:

	Millions of yen	
	2018	2019
Note and account receivables	449,863	**432,874**
Other	8,378	**28,113**
Allowance for doubtful accounts	(1,650)	**(2,475)**
Total	456,591	**458,513**

Trade and other receivables are presented net of allowance for doubtful accounts in the consolidated statement of financial position.

Trade and other receivables are classified as financial assets measured at amortized cost.

9. Inventories

The breakdown of "Inventories" as of December 31 is as follows:

	Millions of yen	
	2018	2019
Merchandise and finished goods (Note 1)	209,491	**236,233**
Leaf tobacco (Note 2)	364,084	**365,700**
Other	75,662	**75,652**
Total	649,238	**677,586**

(Note 1) For imported tobacco products (merchandise) that are sold by TS Network Co., Ltd., a subsidiary of the Company, commissions solely from wholesale are included in revenue. The amount of imported tobacco products (merchandise) that the company holds as of December 31 of each year is included in inventories and presented as "Merchandise and finished goods."

(Note 2) Leaf tobacco includes those products that will be used after 12 months from the end of each year, but they are included in inventories since they are held within the normal operating cycle.

10. Other Financial Assets

(1) The breakdown of "Other financial assets" as of December 31 is as follows:

	Millions of yen	
	2018	2019
Derivative assets	8,653	**2,564**
Equity securities	64,684	**32,747**
Debt securities	26,816	**18,616**
Time deposits	979	**761**
Other	55,656	**82,757**
Allowance for doubtful accounts	(6,108)	**(5,935)**
Total	150,679	**131,511**
Current assets	35,633	**21,943**
Non-current assets	115,046	**109,568**
Total	150,679	**131,511**

Other financial assets are presented net of allowance for doubtful accounts in the consolidated statement of financial position.

Derivative assets are classified as financial assets measured at fair value through profit or loss excluding those to which hedge accounting is applied, equity securities are classified as financial assets measured at fair value through other comprehensive income, and time deposits and debt securities are classified as financial assets measured at amortized cost.

(2) Names of major securities held as financial assets measured at fair value through other comprehensive income and their fair values as of December 31 are as follows:

Millions of yen

Company name	2018	2019
Seven & i Holdings Co., Ltd.	4,091	**3,424**
DOUTOR・NICHIRES Holdings Co., Ltd.	2,681	**2,892**
Japan Airport Terminal Co.,Ltd.	1,524	**2,436**
Central Japan Railway Company	2,317	**2,200**
KATO SANGYO CO., LTD.	1,709	**2,032**
Mitsubishi Shokuhin Co., Ltd.	1,683	**1,860**
OKAMURA CORPORATION	1,710	**1,343**
West Japan Railway Company	1,032	**1,256**
YOSHIMURA FOOD HOLDINGS K.K.	510	**1,250**
Nippon Express Co., Ltd.	1,059	**1,111**

Equity securities are held mainly for strengthening relationships with investees. Therefore, they are designated as financial assets measured at fair value through other comprehensive income.

In order to pursue the efficiency of assets held and to use them effectively, sales of financial assets measured at fair value through other comprehensive income have been carried out (derecognition).

The fair value at the time of sale and cumulative gain or loss that is recognized in equity through other comprehensive income for each year is as follows:

Millions of yen

	2018	2019
Fair Value	2,241	**30,765**
Cumulative gain or loss recognized in equity as other comprehensive income (Note)	(860)	**(15,883)**

(Note) The figure represents the amount transferred to retained earnings.
The cumulative gain or loss recognized in equity as other comprehensive income is transferred to retained earnings when an equity instrument is sold or the decline in its fair value compared to its acquisition cost is significant.

11. Other Current Assets

The breakdown of "Other current assets" as of December 31 is as follows:

Millions of yen

	2018	2019
Prepaid tobacco excise taxes	308,815	**337,166**
Prepaid expenses	21,262	**22,172**
Consumption tax receivables	17,177	**15,243**
Other	38,618	**35,863**
Total	385,872	**410,443**

12. Non-current Assets Held-for-Sale

The breakdown of "Non-current assets held-for-sale" as of December 31 is as follows:

Breakdown of Major Assets

Millions of yen

	2018	2019
Non-current assets held-for-sale		
Property, plant and equipment	4	**14**
Investment property	6	**—**
Other	—	**17**
Total	10	**30**

"Non-current assets held-for-sale" are mainly idle properties which are currently actively marketed for sale.

With regard to such assets and assets sold, impairment losses of ¥74 million are recognized in "Selling, general and administrative expenses" in the consolidated statement of income for the year ended December 31, 2018.

13. Property, Plant and Equipment

(1) Schedule of Property, Plant and Equipment

The schedules of the carrying amount, acquisition cost, and accumulated depreciation and accumulated impairment losses of "Property, plant and equipment" are as follows:

Millions of yen

Carrying Amount	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	Construction in progress	Total
As of January 1, 2018	363,245	279,088	46,373	56,902	745,607
Individual acquisition	18,972	56,901	14,873	48,735	139,480
Acquisition through business combinations	7,275	8,498	107	21	15,902
Transfer to investment property	(3,211)	(0)	(3)	—	(3,215)
Transfer to non-current assets held-for-sale	(1,945)	(4)	—	—	(1,949)
Depreciation	(16,647)	(50,794)	(14,987)	—	(82,428)
Impairment losses	(1,561)	(3,442)	(86)	(131)	(5,220)
Reversal of impairment losses	248	432	—	12	692
Sale or disposal	(764)	(3,221)	(773)	(82)	(4,841)
Exchange differences on translation of foreign operations	(14,716)	(22,895)	(2,162)	(4,208)	(43,981)
Other	11,691	24,025	991	(37,913)	(1,206)
As of December 31, 2018	362,586	288,587	44,333	63,335	758,841
Cumulative effect of changes in accounting policies	**36,440**	**4,548**	**85**	**—**	**41,073**
As of January 1, 2019, after cumulative effect of changes in accounting policies	**399,027**	**293,135**	**44,418**	**63,335**	**799,914**
Individual acquisition	**29,054**	**47,247**	**15,808**	**41,371**	**133,480**
Transfer to investment property	**(1,095)**	**—**	**(21)**	**—**	**(1,116)**
Transfer to non-current assets held-for-sale	**(14)**	**—**	**—**	**—**	**(14)**
Depreciation	**(28,049)**	**(55,775)**	**(15,196)**	**—**	**(99,021)**
Impairment losses	**(1,930)**	**(9,506)**	**(304)**	**(44)**	**(11,784)**
Reversal of impairment losses	**—**	**91**	**—**	**—**	**91**
Sale or disposal	**(739)**	**(5,148)**	**(2,084)**	**(21)**	**(7,991)**
Exchange differences on translation of foreign operations	**(741)**	**(1,550)**	**(81)**	**(1,280)**	**(3,652)**
Other	**9,461**	**30,172**	**1,357**	**(47,657)**	**(6,668)**
As of December 31, 2019	**404,973**	**298,665**	**43,897**	**55,704**	**803,239**

Millions of yen

Acquisition Cost	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	Construction in progress	Total
As of January 1, 2018	664,779	761,581	156,169	56,902	1,639,431
As of December 31, 2018	671,434	773,836	152,793	63,443	1,661,505
As of December 31, 2019	**734,009**	**826,909**	**156,328**	**55,709**	**1,772,954**

Millions of yen

Accumulated Depreciation and Accumulated Impairment Losses	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	Construction in progress	Total
As of January 1, 2018	301,534	482,493	109,797	—	893,824
As of December 31, 2018	308,847	485,249	108,460	107	902,664
As of December 31, 2019	**329,036**	**528,244**	**112,431**	**5**	**969,715**

(2) Impairment Losses

The grouping of property, plant and equipment for impairment test is the smallest cash-generating unit that independently generates cash inflows.

The Group recognized impairment losses of ¥5,220 million in the year ended December 31, 2018, and ¥11,784 million in the year ended December 31, 2019 in "Selling, general and administrative expenses" in the consolidated statement of income.

Impairment losses recognized in the year ended December 31, 2018 represent losses incurred to reduce the carrying amounts to the recoverable amounts for buildings, structures, machinery and vehicles, due to the decision to demolish individual items, etc.

The recoverable amounts of these assets are calculated mainly by their values in use.

Impairment losses recognized in the year ended December 31, 2019 represent losses incurred to reduce the carrying amounts to the recoverable amounts for buildings, structures, machinery and vehicles, due to the decision to dispose of individual items, etc.

The recoverable amounts of these assets are calculated mainly by their values in use, which are estimated at "zero."

14. Goodwill and Intangible Assets

(1) Schedule of Goodwill and Intangible Assets

The schedules of carrying amount, acquisition cost, and accumulated amortization and accumulated impairment losses of "Goodwill" and "Intangible assets" are as follows:

Millions of yen

Carrying Amount	Goodwill	Trademarks	Software	Other	Total
As of January 1, 2018	1,891,210	401,286	23,223	54,666	2,370,385
Individual acquisition	—	188	10,831	8,970	19,990
Acquisition through business combinations	279,606	104,833	163	6,758	391,360
Amortization (Note)	—	(57,539)	(11,242)	(6,888)	(75,669)
Impairment losses	—	—	(17)	(2,389)	(2,406)
Reversal of impairment losses	—	—	0	—	0
Sale or disposal	—	(70)	(124)	(1,556)	(1,750)
Exchange differences on translation of foreign operations	(162,240)	(27,423)	(271)	(1,099)	(191,033)
Other	(161)	—	9,355	(8,579)	615
As of December 31, 2018	2,008,416	421,276	31,919	49,882	2,511,492
Individual acquisition	**—**	**4**	**8,778**	**13,112**	**21,893**
Amortization (Note)	**—**	**(63,380)**	**(11,500)**	**(9,418)**	**(84,298)**
Impairment losses	**—**	**(791)**	**(130)**	**(2,501)**	**(3,423)**
Sale or disposal	**—**	**(6)**	**(300)**	**(83)**	**(389)**
Exchange differences on translation of foreign operations	**(665)**	**3,536**	**(129)**	**121**	**2,863**
Other	**(5,155)**	**3**	**2,934**	**(2,891)**	**(5,109)**
As of December 31, 2019	**2,002,595**	**360,641**	**31,572**	**48,221**	**2,443,029**

(Note) The amortization of intangible assets is included in "Cost of sales" and "Selling, general and administrative expenses" in the consolidated statement of income.

Millions of yen

Acquisition Cost	Goodwill	Trademarks	Software	Other	Total
As of January 1, 2018	1,891,210	1,028,189	142,531	126,263	3,188,192
As of December 31, 2018	2,008,416	1,078,596	157,191	94,698	3,338,901
As of December 31, 2019	**2,002,595**	**1,087,865**	**141,954**	**103,762**	**3,336,175**

Millions of yen

Accumulated Amortization and Accumulated Impairment Losses	Goodwill	Trademarks	Software	Other	Total
As of January 1, 2018	—	626,903	119,308	71,597	817,808
As of December 31, 2018	—	657,320	125,272	44,817	827,409
As of December 31, 2019	**—**	**727,224**	**110,382**	**55,540**	**893,146**

(2) Material Goodwill and Intangible Assets

Goodwill and intangible assets recognized in the consolidated statement of financial position are mainly composed of goodwill and trademarks in the JTIH Group. The carrying amounts of goodwill as of December 31, 2018 and 2019 were ¥1,717,156 million and ¥1,711,335 million, respectively. The carrying amounts of trademarks as of December 31, 2018 and 2019 were ¥305,997 million and ¥261,969 million, respectively.

The majority of goodwill and trademark in the JTIH Group was recognized as a result of the acquisitions of RJR Nabisco's non-U.S. tobacco operations in 1999 and Gallaher in 2007.

Other than the above, goodwill and trademark in Domestic Tobacco business were recognized as a result of the acquisition of Natural American Spirit's non-U.S. tobacco operations in 2016. The carrying amounts of goodwill as of December 31, 2018 and 2019 were ¥265,891 million and ¥265,891 million, respectively. The carrying amounts of trademarks as of December 31, 2018 and 2019 were ¥115,274 million and ¥98,669 million, respectively.

The trademarks are amortized using the straight-line method and the remaining amortization period is mainly from 6 to 7 years.

(3) Impairment Test for Goodwill

For the year ended December 31, 2019, the carrying amount of the majority of goodwill is allocated to the domestic tobacco cash-generating unit of ¥265,891 million (¥265,891 million for the year ended December 31, 2018), the international tobacco cash-generating unit of ¥1,711,335 million (¥1,717,156 million for the year ended December 31, 2018) and the processed food cash-generating unit of ¥25,368 million (¥25,368 million for the year ended December 31, 2018). Details of the result of impairment tests are as follows:

A. Domestic Tobacco Cash-generating Unit

The recoverable amount is calculated by the value in use based on the three-year business plan that was prepared by reflecting past experiences and external information and that was approved by management. After the three-year business plan, given the current domestic tobacco market situation, the Group calculates the value in use by using cash flows with a growth rate of 0% conservatively. For both the current and prior period, the Group's estimated growth rate of 0% is applied only from the fourth year of cash-flows onwards.

The pre-tax discount rate is 4.3% (2018: 4.9%). The value in use sufficiently exceeds the carrying amount of the cash-generating unit. Therefore, even in cases where the discount rate and growth rate used in calculating the value in use fluctuate within reasonable ranges, the Group assumes that the value in use will not become less than the carrying amount.

B. International Tobacco Cash-generating Unit

The recoverable amount is calculated by the value in use based on the three-year business plan that was prepared by reflecting past experiences and external information and that was approved by management. After the three-year business plan, the Group sets a growth rate from 5.7% in the fourth year (2018: 8.1%) to 3.3% in the ninth year (2018: 3.0%), and the same growth rate as the ninth year from the tenth year as a continued growth rate for inflation.

The pre-tax discount rate is 11.0% (2018: 9.9%). The value in use sufficiently exceeds the carrying amount of the cash-generating unit. Therefore, even in cases where the discount rate and growth rate used in calculating the value in use fluctuate within reasonable ranges, the Group assumes that the value in use will not become less than the carrying amount.

C. Processed Food Cash-generating Unit

The recoverable amount is calculated by the value in use based on the three-year business plan that was prepared by reflecting past experiences and external information and that was approved by management. After the three-year business plan, the Group sets a growth rate from 2.5% in the fourth year (2018: 1.2%) to 1.3% in the ninth year (2018: 1.2%), and the same growth rate as the ninth year from the tenth year as a continued growth rate for inflation.

The pre-tax discount rate is 3.8% (2018: 4.0%). The value in use sufficiently exceeds the carrying amount of the cash-generating unit. Therefore, even in cases where the discount rate and growth rate used in calculating the value in use fluctuate within reasonable ranges, the Group assumes that the value in use will not become less than the carrying amount.

(4) Impairment Losses

Goodwill is allocated to cash-generating units that are identified according to locations and types of businesses. The grouping of intangible assets for impairment test is the smallest cash-generating unit that independently generates cash inflow.

The Group recognized impairment losses of ¥2,406 million for the year ended December 31, 2018, and ¥3,423 million for the year ended December 31, 2019 in "Selling, general and administrative expenses" in the consolidated statement of income.

Impairment losses recognized in the year ended December 31, 2018 represent the losses incurred to reduce the carrying amounts to the recoverable amounts of software and other intangible assets since the recoverable amounts were lower than the carrying amounts.

The recoverable amounts of these assets are calculated mainly by their values in use.

Impairment losses recognized in the year ended December 31, 2019 represent the losses incurred to reduce the carrying amounts to the recoverable amounts of trademarks, software and other intangible assets since the recoverable amounts were lower than the carrying amounts.

The recoverable amounts of these assets are calculated mainly by their values in use.

15. Lease Transactions

The Group leases buildings, factory sites, vehicles and other assets as a lessee. Some of the lease contracts have renewal options or escalation clauses. There are no restrictions on additional debt and further leasing imposed by the lease arrangements.

Year ended December 31, 2018

(1) Future Minimum Lease Payments under Non-cancellable Operating Leases

The total of future minimum lease payments under non-cancellable operating leases as of December 31 is as follows:

	Millions of yen
	2018
Not later than 1 year	11,841
Later than 1 year and not later than 5 years	15,870
Later than 5 years	14,696
Total	42,407

(2) Total of Minimum Lease Payments and Contingent Rents

The total of minimum lease payments and contingent rents of operating lease contracts recognized as an expense for each year is as follows:

	Millions of yen
	2018
Total of minimum lease payments	13,445
Contingent rents	1,188

(3) Carrying Amount of Leased Assets from Finance Leases

The breakdown of carrying amount of leased assets from finance leases is as follows:

				Millions of yen
	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	Total
As of December 31, 2018	6,386	5,846	271	12,503

Year ended December 31, 2019

(1) Addition, Depreciation and Carrying Amount of Right-of-use Assets

The breakdown of addition, depreciation and carrying amount of right-of-use assets is as follows:

Year ended December 31, 2019

				Millions of yen
	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	Total
Addition	**14,645**	**9,404**	**72**	**24,121**
Depreciation	**10,449**	**5,210**	**119**	**15,778**

As of December 31, 2019

				Millions of yen
	Land, buildings and structures	Machinery and vehicles	Tools, furniture and fixtures	Total
Carrying amount	**43,772**	**12,813**	**126**	**56,711**

(2) Expense Items Related to Lease

The breakdown of expense items related to lease is as follows:

	Millions of yen
	2019
Financial cost on lease liabilities	**1,506**
Expense relating to short-term lease or leases of low-value assets	**9,440**
Expense relating to variable lease payments	**2,182**
Total cash outflow for leases	**16,003**

16. Investment Property

(1) Schedule of Investment Property

The schedule of the carrying amount of "Investment property" for each year is as follows:

		Millions of yen
	2018	2019
As of January 1	16,700	**17,558**
Expenditure after acquisition	338	**182**
Transfer from property, plant and equipment	3,215	**1,116**
Acquisition by business combination	139	**—**
Transfer to non-current assets held-for-sale	(1,171)	**(403)**
Transfer to property, plant and equipment	(35)	**(370)**
Depreciation	(573)	**(533)**
Impairment losses	(754)	**(917)**
Sale or disposal	(303)	**(34)**
Exchange differences on translation of foreign operations	(6)	**(10)**
Other	7	**—**
As of December 31	17,558	**16,588**
Acquisition cost as of January 1	45,768	**38,355**
Accumulated depreciation and accumulated impairment losses as of January 1	29,068	**20,797**
Acquisition cost as of December 31	38,355	**40,262**
Accumulated depreciation and accumulated impairment losses as of December 31	20,797	**23,674**

(2) Fair Value

The fair value of investment property is determined based on a valuation conducted by an external real estate appraiser. The valuation is made in accordance with the appraisal standards of the country where the investment property is located and based on market evidence of transaction prices for similar assets.

The fair value hierarchy of investment property is categorized from Level 1 to Level 3 as follows:

Level 1: Fair value measured at the quoted price in the active market

Level 2: Fair value that is calculated using the observable price other than categorized in Level 1 directly or indirectly

Level 3: Fair value that is calculated based on valuation techniques which include inputs that are not based on observable market data

The fair value of investment property based on the fair value hierarchy as of December 31 is as follows:

				Millions of yen
				As of December 31, 2018
	Level 1	Level 2	Level 3	Total
Investment property	—	34,678	2,485	37,164

				Millions of yen
				As of December 31, 2019
	Level 1	Level 2	Level 3	Total
Investment property	**—**	**34,788**	**1,416**	**36,204**

(3) Impairment Losses

The grouping of investment properties for impairment test is based on the smallest cash-generating unit that independently generates cash inflows. Impairment tests for idle properties are carried out individually.

The Group recognized impairment losses of ¥754 million for the year ended December 31, 2018, and ¥917 million for the year ended December 31, 2019 in "Selling, general and administrative expenses" in the consolidated statement of income.

Impairment losses recognized for the year ended December 31, 2018 represent the difference between the recoverable amount and the carrying amount for land and buildings as it was decided to demolish certain idle properties. The recoverable amount is calculated based on value in use basis, which is "zero" for buildings due to the decision of demolition, and the recoverable amount of other properties is calculated by the fair value less costs of disposal.

Impairment losses recognized for the year ended December 31, 2019 represent the difference between the recoverable amount and the carrying amount for buildings as it was decided to demolish certain idle properties. The recoverable amounts of these assets are calculated mainly by their values in use, which are estimated at "zero."

17. Income Taxes

(1) Deferred Tax Assets and Deferred Tax Liabilities

The breakdown and schedule of "Deferred tax assets" and "Deferred tax liabilities" by major causes of their occurrence for each year are as follows:

Year ended December 31, 2018

Millions of yen

Deferred Tax Assets	As of January 1, 2018	Recognized in profit or loss	Recognized in other comprehensive income	Other (Note 1)	As of December 31, 2018
Fixed assets (Note 2)	124,709	(10,763)	—	(1,436)	112,509
Retirement benefits	73,621	(1,563)	1,731	(1,543)	72,248
Carryforward of unused tax losses	55,228	(589)	—	(1,513)	53,126
Other	74,433	13,522	(2,043)	(1,697)	84,215
Subtotal	327,991	607	(312)	(6,188)	322,098
Valuation allowance	(65,374)	(1,012)	(1,248)	1,648	(65,986)
Total	262,617	(406)	(1,560)	(4,540)	256,112

Millions of yen

Deferred Tax Liabilities	As of January 1, 2018	Recognized in profit or loss	Recognized in other comprehensive income	Other (Note 1)	As of December 31, 2018
Fixed assets (Note 2)	(84,705)	5,971	—	(12,944)	(91,678)
Retirement benefits	(9,244)	(1,530)	(254)	902	(10,125)
Other	(122,563)	(5,001)	4,337	5,529	(117,697)
Total	(216,511)	(559)	4,083	(6,513)	(219,500)

Year ended December 31, 2019

Millions of yen

Deferred Tax Assets	As of January 1 2019 (Note 3)	Recognized in profit or loss	Recognized in other comprehensive income	Other (Note 1)	As of December 31, 2019
Fixed assets (Note 2)	120,129	(2,528)	—	16	117,616
Retirement benefits	72,248	(3,996)	3,854	(572)	71,534
Carryforward of unused tax losses	53,126	(10,070)	—	(648)	42,409
Other	84,215	2,635	1,103	(22)	87,931
Subtotal	329,717	(13,959)	4,957	(1,225)	319,490
Valuation allowance	(65,986)	15,011	(1,438)	349	(52,064)
Total	263,731	1,053	3,519	(877)	267,426

Millions of yen

Deferred Tax Liabilities	As of January 1 2019 (Note 3)	Recognized in profit or loss	Recognized in other comprehensive income	Other (Note 1)	As of December 31, 2019
Fixed assets (Note 2)	(99,298)	5,824	—	(495)	(93,968)
Retirement benefits	(10,125)	375	(1,708)	(174)	(11,632)
Other	(117,697)	3,938	6,773	(574)	(107,561)
Total	(227,120)	10,137	5,065	(1,243)	(213,160)

(Note 1) "Other" includes exchange differences on translation of foreign operations and acquisition through business combinations.
(Note 2) "Fixed assets" include property, plant and equipment, goodwill, intangible assets and investment property.
(Note 3) According to cumulative effects of changes in accounting policies, "Fixed assets" of "Deferred Tax Assets" and "Deferred Tax Liabilities" have increased ¥7,619 million.

The deferred tax assets are recognized for the amount considered to be recoverable on deductible temporary differences, carryforward of unused tax losses and tax credits by taking taxable temporary differences and future taxable profits plan into account. The carryforward of unused tax losses, for which the deferred tax assets are not recognized, was ¥44,610 million (including ¥15,696 million, for which the carryforward expires after five years) as of December 31, 2018, and ¥31,555 million (including ¥19,252 million, for which the carryforward expires after five years) as of December 31, 2019. Tax credits, for which the deferred tax assets are not recognized, were ¥5,417 million (including ¥5,183 million, for which the carryforward expires after five years) as of December 31, 2018, and ¥4,201 million (including ¥3,931 million, for which the carryforward expires after five years) as of December 31, 2019.

(2) Income Taxes

The breakdown of "Income taxes" for each year is as follows:

Millions of yen

	2018	2019
Current income taxes	143,090	114,799
Deferred income taxes	965	(11,189)
Total income taxes	144,055	103,609

Deferred income taxes increased by ¥96 million and decreased by ¥4,498 million for the years ended December 31, 2018 and 2019, respectively, due to the effect of changes in tax rates in Japan and other countries.

(3) Reconciliation of the Effective Tax Rate

The breakdown of major items that caused differences between the effective statutory tax rate and the average actual tax rate for each year is as follows:

The Company is subject mainly to corporate tax, inhabitant tax and enterprise tax, and the effective statutory tax rate is calculated based on these taxes. The effective statutory tax rates were 30.66% and 30.43% for the years ended December 31, 2018 and 2019, respectively. Foreign subsidiaries are subject to income taxes at their locations.

%

	2018	2019
Effective statutory tax rate	30.66	30.43
Different tax rates applied to foreign subsidiaries	(9.57)	(9.08)
Non-deductible expenses	1.13	1.48
Dividend income	0.45	2.04
Valuation allowance	0.95	(2.90)
Tax credits	(0.62)	(1.66)
Withholding tax in foreign countries	1.50	1.79
Tax contingencies	2.32	1.21
Other	0.28	(1.05)
Average actual tax rate	27.10	22.27

18. Trade and Other Payables

The breakdown of "Trade and other payables" as of December 31 is as follows:

	Millions of yen	
	2018	2019
Accounts payable	197,426	**229,914**
Other payables	68,246	**69,439**
Other	114,844	**109,245**
Total	380,516	**408,597**

Trade and other payables are classified as financial liabilities measured at amortized cost.

19. Bonds and Borrowings (Including Other Financial Liabilities)

(1) Breakdown of Financial Liabilities

The breakdown of "Bonds and borrowings" and "Other financial liabilities" as of December 31 is as follows:

	Millions of yen		
	2018	2019	Due
Derivative liabilities	3,176	**7,739**	—
Short-term borrowings	165,985	**192,581**	—
Commercial paper	72,038	**—**	—
Current portion of long-term borrowings	12,443	**11,554**	—
Current portion of bonds (Note)	—	**80,000**	—
Long-term borrowings	116,870	**103,743**	2021–2028
Bonds (Note)	610,444	**586,623**	—
Lease liabilities	9,807	**53,705**	—
Other	1,570	**1,479**	—
Total	992,334	**1,037,425**	
Current liabilities	254,953	**305,997**	
Non-current liabilities	737,381	**731,428**	
Total	992,334	**1,037,425**	

(Note) The summary of the issuing conditions of the bonds is as follows:

Company	Name of bond	Date of issuance	Millions of yen As of December 31, 2018	**As of December 31, 2019**	% Interest rate	Collateral	Date of maturity
Japan Tobacco Inc.	8th domestic straight bond	December 9, 2010	20,000	**20,000 (20,000)**	1.300	Yes	December 9, 2020
Japan Tobacco Inc.	9th domestic straight bond	July 15, 2015	60,000	**60,000 (60,000)**	0.217	Yes	July 15, 2020
Japan Tobacco Inc.	10th domestic straight bond	July 15, 2015	30,000	**30,000**	0.358	Yes	July 15, 2022
Japan Tobacco Inc.	11th domestic straight bond	July 15, 2015	25,000	**25,000**	0.599	Yes	July 15, 2025
Japan Tobacco Inc.	12th domestic straight bond	September 10, 2018	60,000	**60,000**	0.110	Yes	September 8, 2023
Japan Tobacco Inc.	13th domestic straight bond	September 10, 2018	30,000	**30,000**	0.355	Yes	September 8, 2028
Japan Tobacco Inc.	14th domestic straight bond	September 10, 2018	10,000	**10,000**	0.758	Yes	September 10, 2038
Japan Tobacco Inc.	Straight bond in USD	April 13, 2016	83,116 [USD 750 mil.]	**82,095 [USD 750 mil.]**	2.000	Yes	April 13, 2021
Japan Tobacco Inc.	Straight bond in USD	April 13, 2016	55,268 [USD 500 mil.]	**54,580 [USD 500 mil.]**	2.800	Yes	April 13, 2026
JT International Financial Services B.V.	Straight bond in USD	September 28, 2018	57,871 [USD 525 mil.]	**57,198 [USD 525 mil.]**	3.500	No	September 28, 2023
JT International Financial Services B.V.	Straight bond in USD	September 28, 2018	54,827 [USD 500 mil.]	**54,172 [USD 500 mil.]**	3.875	No	September 28, 2028
JT International Financial Services B.V.	Straight bond in EUR	September 28, 2018	69,134 [EUR 550 mil.]	**66,772 [EUR 550 mil.]**	1.125	No	September 28, 2025
JT International Financial Services B.V.	Straight bond in EUR	November 26, 2019	—	**60,639 [EUR 500 mil.]**	1.000	No	November 26, 2029
JT International Financial Services B.V.	Straight bond in GBP	September 28, 2018	55,228 [GBP 400 mil.]	**56,168 [GBP 400 mil.]**	2.750	No	September 28, 2033
Total			610,444 (—)	**666,623 (80,000)**			

(Note 1) The figure in parentheses ( ) represents the amount of the current portion of the bond.
(Note 2) The figure in parentheses [ ] represents the amount of foreign currency-denominated bond.

Derivative liabilities are classified as financial liabilities measured at fair value through profit or loss excluding those to which hedge accounting is applied, and bonds and borrowings are classified as financial liabilities measured at amortized cost.

There are no financial covenants that have a significant impact on the bonds and borrowings of the Group.

(2) Assets Pledged as Collateral for Liabilities

A. Pursuant to the provisions of Article 6 of the Japan Tobacco Inc. Act, the Company's properties are pledged as general collateral for bonds issued by the Company. Bondholders are entitled to claim satisfaction in preference to unsecured creditors of the Company properties (with the exception of national and local taxes and certain other statutory obligations).

B. Assets pledged as collateral by some subsidiaries are ¥2,138 million and ¥2,060 million as of December 31, 2018 and 2019, respectively. Their corresponding debt is ¥71 million as of December 31, 2018.

20. Provisions

The breakdown and schedule of "Provisions" for each year are as follows:

Year ended December 31, 2018

Millions of yen

	Asset retirement provisions	Restructuring provisions	Provisions for sales rebates	Other provisions	Total
As of January 1, 2018	3,463	7,074	3,312	3,185	17,033
Provisions	157	1,657	3,668	657	6,138
Interest cost associated with passage of time	29	—	—	—	29
Provisions used	(70)	(7,590)	(3,312)	(309)	(11,280)
Provisions reversed	—	(686)	—	(1,058)	(1,744)
Exchange differences on translation of foreign operations	—	(133)	—	(185)	(318)
As of December 31, 2018	3,579	322	3,668	2,289	9,858
Current liabilities	—	309	3,668	2,101	6,078
Non-current liabilities	3,579	12	—	189	3,780
Total	3,579	322	3,668	2,289	9,858

Year ended December 31, 2019

Millions of yen

	Asset retirement provisions	Restructuring provisions	Provisions for sales rebates	Other provisions	Total
As of January 1, 2019	**3,579**	**322**	**3,668**	**2,289**	**9,858**
Provisions	**2**	**25,393**	**4,000**	**4,564**	**33,960**
Interest cost associated with passage of time	**29**	**—**	**—**	**—**	**29**
Provisions used	**(9)**	**(2,874)**	**(3,668)**	**(990)**	**(7,540)**
Provisions reversed	**(4)**	**(95)**	**—**	**(699)**	**(798)**
Exchange differences on translation of foreign operations	**—**	**490**	**—**	**34**	**524**
As of December 31, 2019	**3,598**	**23,236**	**4,000**	**5,199**	**36,033**
Current liabilities	**—**	**7,565**	**4,000**	**5,004**	**16,570**
Non-current liabilities	**3,598**	**15,671**	**—**	**194**	**19,463**
Total	**3,598**	**23,236**	**4,000**	**5,199**	**36,033**

A. Asset Retirement Provisions

In order to settle the obligation of restoring and of removing hazardous substances from plant facilities and premises that the Group uses, the probable amount to be paid in the future is recognized based on past performances. These expenses are expected to be paid after one year or more; however, they may be affected by future business plans.

B. Restructuring Provisions

These provisions are mainly related to business integration and measures for the rationalization of the "International Tobacco Business." The timing of the payment may be affected by future business plans.

C. Provisions for Sales Rebates

These provisions are for contracts which reward the customers with discounts when the sales volume or sales amount in a given period exceeds a specified volume or amount and correspond to "Refund liabilities" in IFRS 15 "Revenue from Contracts with Customers." They are expected to be paid within one year.

21. Other Liabilities

The breakdown of "Other current liabilities" and "Other non-current liabilities" as of December 31 is as follows:

Millions of yen

	2018	2019
Tobacco excise tax payables	297,728	**302,965**
Tobacco special excise tax payables	10,562	**10,060**
Tobacco local excise tax payables	163,704	**163,387**
Consumption tax payables	95,781	**124,693**
Bonus to employees	38,977	**49,473**
Employees' unused paid vacations liabilities	19,130	**19,488**
Other	269,582	**186,752**
Total	895,464	**856,818**
Current liabilities	716,190	**701,050**
Non-current liabilities	179,274	**155,768**
Total	895,464	**856,818**

22. Employee Benefits

(1) Post-employment Benefits

The Group sponsors funded or unfunded defined benefit plans and defined contribution plans as employee retirement benefit plans. The benefits of defined benefit plans are predetermined based on conditions, such as points employees have gained in compensation for each year of service, the payment rate, years of service, and average salaries in their final years of service before retirement.

The Company is obligated to bear pension costs for a mutual assistance association incurred with respect to services in or before June 1956 (prior to enforcement of the Act on the Mutual Aid Association of Public Corporation Employees). Such obligations are recognized as liabilities at their present value using the actuarial valuation method and are included in retirement benefit liabilities.

Special termination benefits may be provided to employees on their early retirements under certain circumstances.

The Company and its subsidiary transferred a portion of their pension plans from a defined benefit plan to a defined contribution plan as of April 1, 2018.

The funded defined benefit plans are administrated by the Group or the fund that is legally separated from the Group in accordance with statutory requirements. The Group, or the board of the pension fund and the trustee of the plan, are required by law to act in the best interests of the plan participants, and are responsible for managing the plan assets in accordance with the designated investment strategy.

The Group's main defined benefit plans expose the Group to actuarial risks, such as investment risk, interest rate risk, inflation risk, and longevity risk.

(i) Investment risk

The present value of the defined benefit obligations is calculated using a discount rate set with reference to a yield on high quality corporate bonds or government bonds. If the return on the plan assets is below this yield, there is a possibility that the plan is underfunded.

(ii) Interest rate risk

A decrease in a yield on high quality corporate bonds or government bonds will increase the present value of the defined benefit obligations. However, this will be partially offset by an increase in the fair value of the debt instruments (plan assets).

(iii) Inflation risk

The level of benefit for certain defined benefit plans of the Group is linked to inflation. Accordingly, a rise in inflation will increase the present value of the defined benefit obligations.

(iv) Longevity risk

Some defined benefit plans of the Group provide a lifetime annuity, and the Group is obligated to provide pension benefits to the plan participants for the rest of their lives after their retirements. The present value of the defined benefit obligations is calculated by reference to the best estimate of the mortality of plan participants during or after employment. An increase in average life expectancy of the plan participants will increase the defined benefit obligations.

A. Schedule of Defined Benefit Obligations

The schedule of the defined benefit obligations is as follows:

Millions of yen

	Japan (Note 3)	Overseas	Total
As of January 1, 2018 (Notes 1, 2)	249,972	530,415	780,386
Current service cost	10,214	9,348	19,562
Past service cost and settlement	(26,868)	450	(26,418)
Interest expense	1,049	10,646	11,695
Contributions by plan participants	—	1,675	1,675
Remeasurement gains and losses:			
Actuarial gains and losses arising from changes in demographic assumptions	(249)	(1,189)	(1,438)
Actuarial gains and losses arising from changes in financial assumptions	(85)	(9,860)	(9,946)
Actuarial gains and losses arising from experience adjustments	3,350	1,255	4,605
Benefits paid	(21,159)	(23,942)	(45,101)
Exchange differences on translation of foreign operations	—	(34,097)	(34,097)
Other	—	263	263
As of December 31, 2018 (Notes 1, 2)	216,223	484,964	701,187
Current service cost	**9,940**	**9,099**	**19,039**
Past service cost and settlement	**—**	**(4,190)**	**(4,190)**
Interest expense	**1,000**	**10,287**	**11,288**
Contributions by plan participants	**—**	**1,727**	**1,727**
Remeasurement gains and losses:			
Actuarial gains and losses arising from changes in demographic assumptions	**1,135**	**(4,668)**	**(3,533)**
Actuarial gains and losses arising from changes in financial assumptions	**(1,282)**	**46,336**	**45,053**
Actuarial gains and losses arising from experience adjustments	**(2,914)**	**(2,463)**	**(5,378)**
Benefits paid	**(23,507)**	**(21,110)**	**(44,617)**
Exchange differences on translation of foreign operations	**—**	**(284)**	**(284)**
Other	**—**	**(608)**	**(608)**
As of December 31, 2019 (Notes 1, 2)	**200,595**	**519,089**	**719,684**

(Note 1) The Group's weighted-average duration of the defined benefit obligations is 6.9 years for Japan and 15.5 years for overseas (2018: 7.1 years for Japan and 15.1 years for overseas).
(Note 2) The Group's breakdown of the defined benefit obligation by plan participant is as follows:

Millions of yen

	As of December 31, 2018			**As of December 31, 2019**		
	Japan	Overseas	Total	Japan	Overseas	Total
Active members	140,274	158,329	298,603	**135,200**	**172,637**	**307,837**
Deferred members	13,158	74,678	87,836	**10,427**	**76,190**	**86,617**
Pensioners	62,792	251,957	314,748	**54,968**	**270,263**	**325,230**
Total	216,223	484,964	701,187	**200,595**	**519,089**	**719,684**

(Note 3) The schedule of mutual pension benefits obligations included in the category of Japan is as follows:

Millions of yen

	2018	**2019**
As of January 1	42,284	**36,675**
Interest expense	127	**110**
Remeasurement gains and losses	(875)	**(1,661)**
Benefits paid	(4,861)	**(4,034)**
As of December 31	36,675	**31,090**

B. Schedule of Plan Assets

The schedule of the plan assets is as follows:

Millions of yen

	Japan	Overseas	Total
As of January 1, 2018	89,998	411,004	501,002
Interest income	322	8,460	8,782
Decrease due to settlement	(22,481)	—	(22,481)
Remeasurement gains and losses:			
Return on plan assets (excluding amounts included in interest income)	(31)	(11,420)	(11,451)
Contributions by the employer (Notes 1, 2)	1,159	10,885	12,044
Contributions by plan participants	—	1,675	1,675
Benefits paid	(6,180)	(19,163)	(25,343)
Exchange differences on translation of foreign operations	—	(27,738)	(27,738)
As of December 31, 2018	62,788	373,702	436,489
Interest income	**296**	**8,207**	**8,503**
Remeasurement gains and losses:			
Return on plan assets (excluding amounts included in interest income)	**1,064**	**30,122**	**31,185**
Contributions by the employer (Notes 1, 2)	**959**	**6,465**	**7,424**
Contributions by plan participants	**—**	**1,727**	**1,727**
Benefits paid	**(7,114)**	**(16,402)**	**(23,516)**
Exchange differences on translation of foreign operations	**—**	**4,634**	**4,634**
As of December 31, 2019	**57,992**	**408,455**	**466,447**

(Note 1) Pursuant to laws and regulations, the Group and the pension fund review the financial condition of the pension plan regularly and recalculate contributions for allocating future benefit and keeping the balance of the pension financing when the plan is underfunded.
(Note 2) The Group plans to pay contributions of ¥6,462 million in the year ending December 31, 2020.

C. Reconciliation of Defined Benefit Obligations and Plan Assets

The reconciliation of the defined benefit obligations and plan assets to the net defined benefit liabilities (assets) recognized in the consolidated statement of financial position as of December 31 is as follows:

As of December 31, 2018

Millions of yen

	Japan	Overseas	Total
Present value of the funded defined benefit obligations	60,453	343,304	403,757
Fair value of the plan assets	(62,788)	(373,702)	(436,489)
Subtotal	(2,334)	(30,398)	(32,732)
Present value of the unfunded defined benefit obligations	155,770	141,660	297,430
Net defined benefit liabilities (assets) recognized in the consolidated statement of financial position	153,435	111,262	264,697
Retirement benefit liabilities	158,297	163,541	321,838
Retirement benefit assets	(4,861)	(52,279)	(57,140)
Net defined benefit liabilities (assets) recognized in the consolidated statement of financial position	153,435	111,262	264,697

As of December 31, 2019

Millions of yen

	Japan	Overseas	Total
Present value of the funded defined benefit obligations	**53,201**	**366,845**	**420,046**
Fair value of the plan assets	**(57,992)**	**(408,455)**	**(466,447)**
Subtotal	**(4,791)**	**(41,610)**	**(46,401)**
Present value of the unfunded defined benefit obligations	**147,394**	**152,244**	**299,638**
Net defined benefit liabilities (assets) recognized in the consolidated statement of financial position	**142,603**	**110,635**	**253,237**
Retirement benefit liabilities	**148,915**	**171,699**	**320,614**
Retirement benefit assets	**(6,312)**	**(61,064)**	**(67,377)**
Net defined benefit liabilities (assets) recognized in the consolidated statement of financial position	**142,603**	**110,635**	**253,237**

D. Major Breakdown of Plan Assets

The breakdown of plan assets by major category as of December 31 is as follows:

Japan

Millions of yen

	As of December 31, 2018			**As of December 31, 2019**		
	Market price in an active market			Market price in an active market		
	Quoted	Unquoted	Total	Quoted	Unquoted	Total
Cash and cash equivalents	7,183	—	7,183	**7,794**	**—**	**7,794**
Equity instruments	3,052	—	3,052	**3,078**	**—**	**3,078**
Japan	1,530	—	1,530	**1,509**	**—**	**1,509**
Overseas	1,523	—	1,523	**1,569**	**—**	**1,569**
Debt instruments	10,388	—	10,388	**8,819**	**—**	**8,819**
Japan	9,147	—	9,147	**7,572**	**—**	**7,572**
Overseas	1,242	—	1,242	**1,247**	**—**	**1,247**
General account of life insurance companies [Note]	—	40,309	40,309	**—**	**36,496**	**36,496**
Other	1,208	646	1,855	**785**	**1,019**	**1,804**
Total	21,832	40,956	62,788	**20,477**	**37,515**	**57,992**

Overseas

Millions of yen

	As of December 31, 2018			**As of December 31, 2019**		
	Market price in an active market			Market price in an active market		
	Quoted	Unquoted	Total	Quoted	Unquoted	Total
Cash and cash equivalents	15,269	—	15,269	**15,622**	**—**	**15,622**
Equity instruments	47,856	—	47,856	**59,536**	**0**	**59,537**
United Kingdom	3,871	—	3,871	**4,242**	**—**	**4,242**
North America	17,539	—	17,539	**23,397**	**—**	**23,397**
Other	26,445	—	26,445	**31,897**	**0**	**31,897**
Debt instruments	277,109	5,134	282,242	**294,759**	**5,334**	**300,093**
United Kingdom	195,193	—	195,193	**210,452**	**—**	**210,452**
North America	39,583	0	39,583	**33,186**	**—**	**33,186**
Other	42,333	5,134	47,466	**51,122**	**5,334**	**56,456**
Real estate	11,581	65	11,646	**13,060**	**66**	**13,126**
Other	8,206	8,482	16,688	**10,395**	**9,683**	**20,078**
Total	360,021	13,681	373,702	**393,372**	**15,083**	**408,455**

Total

Millions of yen

	As of December 31, 2018			**As of December 31, 2019**		
	Market price in an active market			Market price in an active market		
	Quoted	Unquoted	Total	Quoted	Unquoted	Total
Cash and cash equivalents	22,452	—	22,452	**23,416**	**—**	**23,416**
Equity instruments	50,908	—	50,908	**62,614**	**0**	**62,615**
Debt instruments	287,497	5,134	292,631	**303,578**	**5,334**	**308,913**
Real estate	11,581	65	11,646	**13,060**	**66**	**13,126**
General account of life insurance companies [Note]	—	40,309	40,309	**—**	**36,496**	**36,496**
Other	9,414	9,129	18,543	**11,180**	**10,702**	**21,882**
Total	381,852	54,637	436,489	**413,849**	**52,598**	**466,447**

(Note) A certain interest rate and principal for the general account of life insurance are guaranteed by life insurance companies.

The investment strategy for the Group's major plans is as follows:

(Japan)

The Company's pension fund is managed in accordance with the internal policy for securing stable profits in the middle- and long-term in order to ensure the redemption of the plan liability. Concretely, by setting a target rate of return and composition ratio of plan assets by asset category within the risk tolerance that is annually assessed, the Company invests plan assets consistently with the composition ratio. When reviewing the composition ratio, the Company considers introducing an asset investment which has a high correlation with the liability.

When an unexpected situation occurs in the market environment, it is temporarily allowed to make a weighted adjustment to the risk assets, complying with company policy.

(Overseas)

The investment strategy for the foreign subsidiaries' funded pension plans is decided properly by the trustee of the plan and the management of overseas subsidiaries according to local legislation. The Company's objective for the foreign subsidiaries' funded pension plans is to manage risks arising from its defined benefit obligation, and meanwhile to achieve a return on assets in excess of the movement in the value of the defined benefit obligation.

The majority of the plan assets have been allocated to liability matching bonds and the remaining parts of the plan assets are mainly invested in equities targeting long-term return.

E. Matters Related to Actuarial Assumptions

The major items of actuarial assumptions as of December 31 are as follows:

%

	As of December 31, 2018		**As of December 31, 2019**	
	Japan	Overseas	Japan	Overseas
Discount rate	0.5	2.2	**0.6**	**1.5**
Inflation rate	—	2.4	**—**	**2.3**

As of December 31, 2018

Years

	Japan		Overseas	
	Males	Females	Males	Females
Average life expectancy at retirement [Note 1]				
Current pensioners	23.6 [Note 2]	29.3 [Note 2]	22.0 [Note 3]	24.2 [Note 3]
Future pensioners			23.4 [Note 4]	25.5 [Note 4]

As of December 31, 2019

	Japan		Overseas	Years
	Males	Females	Males	Females
Average life expectancy at retirement (Note 1)				
Current pensioners	23.6 (Note 2)	29.3 (Note 2)	21.8 (Note 3)	24.0 (Note 3)
Future pensioners			23.1 (Note 4)	25.3 (Note 4)

(Note 1) The average life expectancies underlie the values of the defined benefit obligations on major plans. Assumptions regarding future mortality rate are based on published statistics and mortality tables.
(Note 2) Life expectancy for a pensioner currently aged 60. Regardless of the plan participant's current age, the Group performs actuarial calculations based on the assumption that life expectancy remains the same.
(Note 3) Life expectancy for a pensioner currently aged 65.
(Note 4) Life expectancy at the age of 65 for an active member currently aged 50.
(Note 5) The valuation of defined benefit obligations reflects a judgment on uncertain future events. The sensitivities of defined benefit obligations due to changes in major assumptions as of December 31 are as follows. Each of these sensitivities assumes that other variables remain fixed; however, in fact, they do not always change independently. Negative figures represent a decrease in pension plan obligations, while positive figures represent an increase.

		As of December 31, 2018		As of December 31, 2019	Millions of yen
	Change in assumptions	Japan	Overseas	Japan	Overseas
Discount rate	Increase by 0.5%	(7,192)	(34,758)	**(6,438)**	**(38,101)**
	Decrease by 0.5%	7,711	38,496	**6,917**	**42,460**
Inflation rate	Increase by 0.5%	—	23,889	**—**	**25,757**
	Decrease by 0.5%	—	(22,326)	**—**	**(24,052)**
Mortality rate	Extended 1 year	4,420	16,812	**3,834**	**20,155**
	Shortened 1 year	(4,267)	(16,915)	**(3,696)**	**(19,764)**

F. Breakdown of Defined Benefit Cost

The breakdown of defined benefit cost for each year is as follows:

Year ended December 31, 2018

	Japan	Overseas	Millions of yen Total
Current service cost	10,214	9,348	19,562
Past service cost and gains and losses on settlement	(4,388)	450	(3,937)
Interest expense (income)	727	2,186	2,913
Defined benefit cost through profit or loss	6,553	11,985	18,538
Actuarial gains and losses arising from changes in demographic assumptions	(249)	(1,189)	(1,438)
Actuarial gains and losses arising from changes in financial assumptions	(85)	(9,860)	(9,946)
Actuarial gains and losses arising from experience adjustments	3,350	1,255	4,605
Return on plan assets (excluding amounts included in interest income)	31	11,420	11,451
Defined benefit cost through other comprehensive income	3,047	1,626	4,673
Total of defined benefit cost	9,600	13,611	23,210

Year ended December 31, 2019

	Japan	Overseas	Millions of yen Total
Current service cost	**9,940**	**9,099**	**19,039**
Past service cost and gains and losses on settlement	**—**	**(4,190)**	**(4,190)**
Interest expense (income)	**704**	**2,080**	**2,785**
Defined benefit cost through profit or loss	**10,645**	**6,989**	**17,634**
Actuarial gains and losses arising from changes in demographic assumptions	**1,135**	**(4,668)**	**(3,533)**
Actuarial gains and losses arising from changes in financial assumptions	**(1,282)**	**46,336**	**45,053**
Actuarial gains and losses arising from experience adjustments	**(2,914)**	**(2,463)**	**(5,378)**
Return on plan assets (excluding amounts included in interest income)	**(1,064)**	**(30,122)**	**(31,185)**
Defined benefit cost through other comprehensive income	**(4,126)**	**9,083**	**4,957**
Total of defined benefit cost	**6,519**	**16,072**	**22,591**

(Note 1) The net amount of interest expense and interest income is included in "Financial costs." Other expenses are included in "Cost of sales" and "Selling, general and administrative expenses."
(Note 2) Contributions to the defined contribution plans were ¥11,517 million for the year ended December 31, 2018 and ¥9,269 million for the year ended December 31, 2019 and were not included in the table above.

(2) Other Employee Benefit Expenses

The employee benefit expenses other than post-employment benefits that are included in the consolidated statement of income for each year are as follows:

	2018	Millions of yen 2019
Remuneration and salary	236,971	**239,305**
Bonus to employees	67,379	**80,973**
Legal welfare expenses	44,535	**44,607**
Welfare expenses	39,086	**38,620**
Termination benefits	(304)	**24,541**

23. Equity and Other Equity Items

(1) Share Capital and Capital Surplus

A. Authorized Shares

The number of authorized shares as of December 31, 2018 and 2019 is 8,000,000 thousand ordinary shares.

B. Fully Paid Issued Shares

The schedule of the number of issued shares and share capital is as follows:

	Thousands of shares		Millions of yen
	Number of ordinary issued shares	Share capital	Capital surplus
As of January 1, 2018	2,000,000	100,000	736,400
Increase (decrease)	—	—	—
As of December 31, 2018	2,000,000	100,000	736,400
Increase (decrease)	—	—	—
As of December 31, 2019	**2,000,000**	**100,000**	**736,400**

(Note) The shares issued by the Company are non-par value ordinary shares that have no restriction on any content of rights.

(2) Treasury Shares

The schedule of the number of treasury shares and its amount as of each year end is as follows:

	Thousands of shares	Millions of yen
	Number of shares	Amount
As of January 1, 2018	208,957	443,636
Increase (decrease) (Note 2)	(380)	(807)
As of December 31, 2018	208,577	442,829
Increase (decrease) (Note 2)	17,620	49,640
As of December 31, 2019	**226,197**	**492,469**

(Note 1) The Company adopts share option plans and utilizes treasury shares for delivery of shares due to its exercise. Contract conditions and amounts are described in "33. Share-based Payments."

(Note 2) The number of treasury shares purchased based on the resolution made by the Board of Directors is 17,788 thousand shares and the total purchase cost is ¥50,000 million for the year ended December 31, 2019. Purchases of shares less than one unit are 0 thousand shares for the year ended December 31, 2018 and 0 thousand shares for the year ended December 31, 2019. The number of shares delivered upon exercise of share options is 380 thousand shares for the year ended December 31, 2018 and 168 thousand shares for the year ended December 31, 2019.

(3) Other Components of Equity

A. Subscription Rights to Shares

The Company adopts share option plans and issues subscription rights to shares based on the Companies Act. Contract conditions and amount are described in "33. Share-based Payments."

B. Exchange Differences on Translation of Foreign Operations

Exchange differences on translation of foreign operations are composed of foreign currency translation difference that occurs when consolidating financial statements of foreign subsidiaries prepared in foreign currencies, and the effective portion of net gain (loss) on the hedging instruments designated as hedge of net investment.

C. Net Gain (Loss) on Derivatives Designated as Cash Flow Hedges

The Group uses derivatives for hedging to avoid the risk of fluctuation in future cash flows. This is the effective portion of changes in the fair value of hedging instruments designated as cash flow hedges.

D. Net Gain (Loss) on Revaluation of Financial Assets Measured at Fair Value through Other Comprehensive Income

This is the valuation difference in the fair value of financial assets measured at fair value through other comprehensive income.

E. Remeasurements of Defined Benefit Plans

Remeasurements of defined benefit plans comprise actuarial gains and losses, the return on plan assets excluding amounts included in interest income, and any change in the effect of the asset ceiling excluding amounts included in interest income. In addition, actuarial gains and losses are the effects of differences between the actuarial assumptions at the beginning of the year and what has actually occurred, and the effects of changes in actuarial assumptions. Remeasurements are recognized as other comprehensive income when they occur and are transferred immediately from other components of equity to retained earnings.

24. Dividends

Dividends paid for each year are as follows:

Year ended December 31, 2018

	Class of shares	Millions of yen Total dividends	Yen Dividends per share	Basis date	Effective date
(Resolution)					
Annual Shareholders' Meeting (March 27, 2018)	Ordinary shares	125,373	70	December 31, 2017	March 28, 2018
Board of Directors (August 1, 2018)	Ordinary shares	134,351	75	June 30, 2018	September 3, 2018

Year ended December 31, 2019

	Class of shares	Millions of yen Total dividends	Yen Dividends per share	Basis date	Effective date
(Resolution)					
Annual Shareholders' Meeting (March 20, 2019)	**Ordinary shares**	**134,357**	**75**	**December 31, 2018**	**March 22, 2019**
Board of Directors (July 31, 2019)	**Ordinary shares**	**136,579**	**77**	**June 30, 2019**	**September 2, 2019**

Dividends for which the effective date falls in the following year are as follows:

Year ended December 31, 2018

	Class of shares	Millions of yen Total dividends	Yen Dividends per share	Basis date	Effective date
(Resolution)					
Annual Shareholders' Meeting (March 20, 2019)	Ordinary shares	134,357	75	December 31, 2018	March 22, 2019

Year ended December 31, 2019

	Class of shares	Millions of yen Total dividends	Yen Dividends per share	Basis date	Effective date
(Resolution)					
Annual Shareholders' Meeting (March 19, 2020)	**Ordinary shares**	**136,583**	**77**	**December 31, 2019**	**March 23, 2020**

25. Revenue

(1) Disaggregation of Revenue

The disaggregation of "Revenue" for each year is as follows. The amounts are presented after eliminations of intercompany transactions.

Year ended December 31, 2018

Millions of yen

	Reportable Segments					
	Domestic Tobacco (Note 2)	International Tobacco (Note 3)	Pharmaceuticals	Processed Food	Other	Consolidated
Core revenue from tobacco business (Note 1)	582,379	1,250,719	—	—	—	1,833,098
Other	39,047	61,622	113,992	161,387	6,815	382,864
Total	621,426	1,312,342	113,992	161,387	6,815	2,215,962

Year ended December 31, 2019

Millions of yen

	Reportable Segments					
	Domestic Tobacco (Note 2)	International Tobacco (Note 3)	Pharmaceuticals	Processed Food	Other	Consolidated
Core revenue from tobacco business (Note 1)	**568,880**	**1,253,022**	**—**	**—**	**—**	**1,821,902**
Other	**42,614**	**57,855**	**88,528**	**158,586**	**6,140**	**353,724**
Total	**611,494**	**1,310,877**	**88,528**	**158,586**	**6,140**	**2,175,626**

(Note 1) The "Domestic Tobacco Business" does not include revenue related to imported tobacco delivery charges. In addition, the "International Tobacco Business" does not include revenue related to the distribution business and contract manufacturing.

(Note 2) Revenues from RRP in core revenue from the "Domestic Tobacco Business" were ¥64,611 million and ¥60,932 million for the year ended December 31, 2018 and 2019, respectively. RRP represents Reduced-Risk Products with potential to reduce the health risks associated with smoking.

(Note 3) Core revenue by cluster from the "International Tobacco Business" is as follows:

	2018	Millions of yen 2019
South and West Europe	222,964	**216,653**
North and Central Europe	233,103	**236,210**
CIS+	311,897	**309,646**
Rest-of-the-World	482,756	**490,513**
Total	1,250,719	**1,253,022**

South and West Europe includes France, Italy and Spain. North and Central Europe includes Germany and the United Kingdom. CIS+ includes Romania and Russia. Rest-of-the-World includes Iran, Taiwan and Turkey.

A. Domestic and International Tobacco Businesses

Domestic and international tobacco businesses engage in the sale of tobacco products.

Revenue from sales of products is recognized upon delivery of the products because the customer obtains control of the products upon delivery, by which the Group evaluates that the performance obligation is satisfied. Revenue is measured at the consideration promised in a contract with a customer, less discounts, rebates and taxes, including consumption tax. In addition, where the Group makes payments to the customer, except the case when consideration payable to the customer is a payment for a distinct product or service from the customer, revenue is measured at the amount which is consideration promised with the customer, less consideration payable to the customer.

Considerations for transactions are received mainly within one year from satisfying their performance obligations and includes no significant financing components.

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

B. Pharmaceutical Business

Pharmaceutical business mainly engages in the sale of prescription drugs and licensing.

Revenue from sales of products is recognized upon delivery of the products because the customer obtains control of the products upon delivery, by which the Group evaluates that the performance obligation is satisfied. Revenue is measured at the consideration promised in a contract with a customer, less discounts, rebates and taxes, including consumption tax. In addition, where the Group makes payments to the customer, except the case when consideration payable to the customer is a payment for a distinct product or service from the customer, revenue is measured at the amount which is consideration promised with the customer, less consideration payable to the customer.

Revenue from licensing is generated by licensing out the rights to develop and market of each compound to licensees in the development stage, and the Group receives upfront income, milestone revenue and sales-based royalties. Upfront income is recognized at the time the customer obtains control of the license. Milestone revenue is recognized at the time the milestone agreed between the parties such as the progress of development is achieved. Sales-based royalties are measured based on the Group's licensees' sales, and recognized by taking into consideration the timing of occurrence.

Considerations for transactions are received mainly within one year from satisfying their performance obligations and includes no significant financial component.

C. Processed Foods Business

Processed foods business engages in the sale of frozen and ambient processed foods, bakery products and seasonings.

Revenue from sales of products is recognized upon delivery of the products because the customer obtains control of the products upon delivery, by which the Group evaluates that the performance obligation is satisfied. Revenue is measured at the consideration promised in a contract with a customer, less discounts, rebates and taxes, including consumption tax. In addition, where the Group makes payments to the customer, except the case when consideration payable to the customer is a payment for a distinct product or service from the customer, revenue is measured at the amount which is consideration promised with the customer, less consideration payable to the customer.

Considerations for transactions are received mainly within one year from satisfying their performance obligations and includes no significant financial component.

Transactions in which the Group is involved as an agency are excluded from revenue. The inflow of economic benefits after deducting these transactions is presented as "Revenue" in the consolidated statement of income.

(2) Transaction Price Allocated to the Remaining Performance Obligations

The Group uses the practical expedient and does not disclose information on the remaining performance obligations because it has no significant transactions with initial expected contractual terms exceeding one year. There are no significant amounts of considerations from contracts with customers that are not included in transaction prices.

(3) Gross Turnover

The reconciliation from "Gross turnover" to "Revenue" for each year is as follows:

	2018	Millions of yen 2019
Gross turnover	7,532,248	**7,581,071**
Tobacco excise taxes and agency transaction amount	(5,316,285)	**(5,405,446)**
Revenue	2,215,962	**2,175,626**

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

Gross turnover is an item that the Group discloses voluntarily and is not "Revenue" as defined by IFRS.

26. Other Operating Income

The breakdown of "Other operating income" for each year is as follows:

	2018	Millions of yen 2019
Gain on transfer of pharmaceutical licenses	—	**60,518**
Gain on sale of property, plant and equipment, intangible assets and investment property (Notes 1, 2)	39,402	**15,605**
Other (Note 2)	9,129	**19,603**
Total	48,532	**95,725**

(Note 1) The amount of gain on sale for the year ended December 31, 2018 mainly relates to the sale of the old plant sites.
(Note 2) The amount of restructuring incomes included in each account is as follows:

	2018	Millions of yen 2019
Gain on sale of property, plant and equipment, intangible assets and investment property	38,559	**14,626**
Other	725	**571**
Total	39,284	**15,197**

27. Selling, General and Administrative Expenses

The breakdown of "Selling, general and administrative expenses" for each year is as follows:

	2018	Millions of yen 2019
Advertising expenses	29,111	**33,467**
Promotion expenses	106,199	**102,095**
Commission	52,749	**55,469**
Employee benefit expenses (Note 2)	268,956	**309,623**
Research and development expenses (Note 1)	65,377	**64,079**
Depreciation and amortization	87,926	**106,094**
Impairment losses on other than financial assets (Note 2)	8,454	**16,124**
Losses on sale and disposal of property, plant and equipment, intangible assets, and investment property (Note 2)	8,845	**9,432**
Other (Note 2)	142,790	**135,324**
Total	770,407	**831,707**

(Note 1) All research and development expenses are included in "Selling, general and administrative expenses."

(Note 2) The amount of restructuring costs included in each account is as follows:

	2018	2019
		Millions of yen
Employee benefit expenses	24	**24,378**
Impairment losses on other than financial assets	3,105	**411**
Losses on sale and disposal of property, plant and equipment, intangible assets, and investment property	3,262	**329**
Other	1,530	**1,064**
Total	7,921	**26,182**

28. Financial Income and Financial Costs

The breakdown of "Financial income" and "Financial costs" for each year is as follows:

Financial Income	2018	2019
		Millions of yen
Dividend income		
Financial assets measured at fair value through other comprehensive income		
Investments derecognized during the year	185	**1,275**
Investments held at the end of the year	1,871	**654**
Interest income		
Financial assets measured at amortized cost		
Deposits and bonds	3,695	**6,014**
Other	2	**459**
Total	5,754	**8,402**

Financial Costs	2018	2019
		Millions of yen
Interest expenses		
Financial liabilities measured at amortized cost		
Bonds and borrowings (Note 2)	16,267	**26,019**
Other	77	**1,538**
Foreign exchange losses (Note 1)	15,974	**13,297**
Employee benefit expenses (Note 3)	2,913	**2,785**
Other	4,022	**1,887**
Total	39,252	**45,526**

(Note 1) Valuation gain (loss) of currency derivatives is included in foreign exchange losses.
(Note 2) Valuation gain (loss) of interest rate derivatives is included in interest expenses.
(Note 3) The employee benefit expenses are the net amount of interest cost and interest income related to employee benefits.

29. Other Comprehensive Income

Amount arising during the year, reclassification adjustments to profit or loss and tax effects for each component of "Other comprehensive income" for each year are as follows:

Year ended December 31, 2018

	Amount arising	Reclassification adjustments	Before tax effects	Tax effects	Net of tax effects
					Millions of yen
Items that will not be reclassified to profit or loss					
Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income	(11,703)	—	(11,703)	3,488	(8,215)
Remeasurements of defined benefit plans	(4,673)	—	(4,673)	1,478	(3,195)
Total of items that will not be reclassified to profit or loss	(16,375)	—	(16,375)	4,965	(11,410)
Items that may be reclassified subsequently to profit or loss					
Exchange differences on translation of foreign operations	(244,898)	(230)	(245,128)	(2,603)	(247,731)
Net gain (loss) on derivatives designated as cash flow hedges	1,138	236	1,374	(363)	1,012
Total of items that may be reclassified subsequently to profit or loss	(243,760)	6	(243,754)	(2,965)	(246,719)
Total	(260,135)	6	(260,129)	2,000	(258,129)

Year ended December 31, 2019

	Amount arising	Reclassification adjustments	Before tax effects	Tax effects	Net of tax effects
					Millions of yen
Items that will not be reclassified to profit or loss					
Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income	**(2,209)**	**—**	**(2,209)**	**(274)**	**(2,484)**
Remeasurements of defined benefit plans	**(4,957)**	**—**	**(4,957)**	**2,146**	**(2,811)**
Total of items that will not be reclassified to profit or loss	**(7,166)**	**—**	**(7,166)**	**1,871**	**(5,295)**
Items that may be reclassified subsequently to profit or loss					
Exchange differences on translation of foreign operations	**7,521**	**2,591**	**10,112**	**(233)**	**9,879**
Net gain (loss) on derivatives designated as cash flow hedges	**(882)**	**320**	**(561)**	**171**	**(391)**
Total of items that may be reclassified subsequently to profit or loss	**6,639**	**2,911**	**9,550**	**(62)**	**9,489**
Total	**(527)**	**2,911**	**2,384**	**1,810**	**4,194**

30. Earnings per Share

(1) Basis of Calculating Basic Earnings per Share

A. Profit Attributable to Ordinary Shareholders of the Parent Company

	2018	2019
		Millions of yen
Profit for the period attributable to owners of the parent company	385,677	**348,190**
Profit not attributable to ordinary shareholders of the parent company	—	**—**
Profit for the period used for calculation of basic earnings per share	385,677	**348,190**

B. Weighted-average Number of Ordinary Shares Outstanding During the Period

		Thousands of shares
	2018	**2019**
Weighted-average number of shares during the period	1,791,296	**1,776,782**

(2) Basis of Calculating Diluted Earnings per Share

A. Profit Attributable to Diluted Ordinary Shareholders

		Millions of yen
	2018	**2019**
Profit for the period used for calculation of basic earnings per share	385,677	**348,190**
Adjustment	—	**—**
Profit for the period used for calculation of diluted earnings per share	385,677	**348,190**

B. Weighted-average Number of Diluted Ordinary Shares Outstanding During the Period

		Thousands of shares
	2018	**2019**
Weighted-average number of ordinary shares during the period	1,791,296	**1,776,782**
Increased number of ordinary shares under subscription rights to shares	863	**857**
Weighted-average number of diluted ordinary shares during the period	1,792,159	**1,777,639**

31. Non-cash Transactions

Significant Non-cash Transactions

The amount of assets acquired under finance leases was ¥1,041 million for the year ended December 31, 2018. In addition, starting from this year, increase in right-of-use assets has been described in "15. Lease Transactions" following the application of IFRS16.

32. Reconciliation of Liabilities Arising from Financing Activities

Reconciliation of liabilities arising from financing activities for each year is as follows:

Year ended December 31, 2018

			Non-cash changes				Millions of yen
	As of January 1, 2018	Cash flows	Acquisition through business combinations	Foreign exchange movement	Fair value changes	Other	As of December 31, 2018
Short-term borrowings and commercial paper	341,041	(133,849)	49,137	(19,586)	—	1,280	238,023
Long-term borrowings (Note 1)	71,854	56,425	1,795	(764)	—	2	129,313
Bonds (Note 1)	332,242	285,136	—	(7,346)	—	413	610,444
Lease liabilities	10,667	(1,637)	—	(264)	—	1,041	9,807
Derivatives (Note 2)	(2,490)	2,294	—	—	196	—	—
Total	753,314	208,370	50,932	(27,960)	196	2,736	987,588

Year ended December 31, 2019

			Non-cash changes				Millions of yen
	As of January 1, 2019 (Note 3)	Cash flows	Acquisition through business combinations	Foreign exchange movement	Fair value changes	Other	**As of December 31, 2019**
Short-term borrowings and commercial paper	**238,023**	**(44,976)**	**—**	**(1,563)**	**—**	**1,097**	**192,581**
Long-term borrowings (Note 1)	**129,313**	**(11,568)**	**—**	**(2,475)**	**—**	**27**	**115,297**
Bonds (Note 1)	**610,444**	**59,435**	**—**	**(3,579)**	**—**	**324**	**666,623**
Lease liabilities	**48,840**	**(14,294)**	**—**	**(394)**	**—**	**19,552**	**53,705**
Total	**1,026,621**	**(11,403)**	**—**	**(8,011)**	**—**	**21,000**	**1,028,206**

(Note 1) Current portion is included.
(Note 2) Derivatives are held for the purpose of hedging bonds.
(Note 3) According to cumulative effects of changes in accounting policies, lease liabilities have increased ¥39,033 million.

33. Share-based Payments

The Company and Torii Pharmaceutical adopt share option plans. Share options are granted by the resolutions of the Board of Directors based on the approvals at the Annual Shareholders' Meeting.

The outline of the share option plan of the Company is as follows:

(1) Share Option Contract Conditions of the Company

Positions of persons granted	: Directors and Executive Officers
Settlement	: Issuance of shares
Effective period of granted share option	: 30 years after the date of grant
Vesting conditions	: None

Conditions related to the exercise of share options are as follows:

A. The subscription rights to shares become exercisable when a holder of a subscription right to shares no longer holds a position as a director, an audit & supervisory board member or an executive officer. In the subscription rights to shares allocation contract with holders of such rights, it is provided for that the rights become exercisable from the date following the date on which they no longer hold their positions.

B. In the case where any holders of subscription rights to shares waive such rights, they cannot exercise them.

(2) Changes in the Number of Share Options of the Company

						Shares
			2018			**2019**
	Directors	Executive Officers	Total	Directors	Executive Officers	Total
Balance as of January 1	328,800	702,400	1,031,200	**195,400**	**634,000**	**829,400**
Granted	68,800	109,400	178,200	**126,000**	**187,200**	**313,200**
Exercised	—	(380,000)	(380,000)	**—**	**(168,000)**	**(168,000)**
Transferred	(202,200)	202,200	—	**39,600**	**(39,600)**	**—**
Balance as of December 31	195,400	634,000	829,400	**361,000**	**613,600**	**974,600**
Exercisable balance as of December 31	—	239,600	239,600	**—**	**153,400**	**153,400**

(Note 1) The number of share options is presented as the number of underlying shares.
(Note 2) All share options are granted with an exercise price of ¥1 per share.
(Note 3) Share options are granted to 5 directors and 18 executive officers for the year ended December 31, 2018, and 6 directors and 20 executive officers for the year ended December 31, 2019.
"Transferred" included in the "Changes in the Number of Share Options" represents the number of share options for persons granted whose management position changed during the period.
(Note 4) The weighted-average fair values per share of share options granted during the period were ¥1,500 and ¥940 for the years ended December 31, 2018 and 2019, respectively.
(Note 5) The weighted-average share prices of share options at the time of exercise during the period were ¥3,086 and ¥2,544 for the years ended December 31, 2018 and 2019, respectively.
(Note 6) The weighted-average remaining contract years of unexercised share options at the end of each period were 25.4 years and 26.4 years for the years ended December 31, 2018 and 2019, respectively.

(3) Method of Measuring Fair Value of Share Options Granted During the Period of the Company

A. Valuation Model

Black-Scholes Model

B. Main Assumptions and Estimation

	2018	2019
Share price	¥3,013	**¥2,401**
Volatility of share price (Note 1)	31.7%	**31.2%**
Estimated remaining period (Note 2)	15 years	**15 years**
Estimated dividends (Note 3)	¥140/share	**¥150/share**
Risk free interest rate (Note 4)	0.26%	**0.07%**

(Note 1) Calculated based on daily share prices quoted for the past 15 years.
(Note 2) Because of the difficulty of a reasonable estimation due to insufficient data, the remaining period is estimated based on the assumption that share option rights would be exercised at a midpoint of the exercise period.
(Note 3) Based on the latest dividends paid.
(Note 4) The yield on government bonds for a period of the expected remaining period.

(4) Share-based Payment Expenses

The costs for share options included in "Selling, general and administrative expenses" in the consolidated statement of income were ¥275 million and ¥291 million for the years ended December 31, 2018 and 2019, respectively.

34. Financial Instruments

(1) Capital Management

The Group's management principle is pursuit of the "4S" model: balancing the interests of consumers, shareholders, employees and wider society, and fulfilling our responsibilities towards them, aiming to exceed their expectations.

The Group believes that sustainable profit growth in the mid- to long-term based on this principle will increase the Group's value in the mid- to long-term, and is consequently in the best interest of all stakeholders, including our shareholders.

For that reason, as its financial policy, the Group maintains a strong financial base that secures stability in the case of changes in business environment such as economic crises, and flexibility enabling expeditious responses to business investment opportunities.

The Group manages net interest-bearing debt, where cash and cash equivalents are deducted from interest-bearing debt, and capital (the part attributable to the owners of the parent company). The amounts as of December 31 are as follows:

		Millions of yen
	2018	2019
Interest-bearing debt (Note)	987,588	**974,502**
Cash and cash equivalents	(282,063)	**(357,158)**
Net interest-bearing debt	705,526	**617,344**
Capital (equity attributable to owners of the parent company)	2,630,594	**2,662,696**

(Note) Lease liabilities are excluded from the year ended December 31, 2019.

There are specific rules for shares of the Company under the Japan Tobacco Inc. Act, as follows:

The Japanese government shall hold more than one-third of all of the shares issued by the Company (excluding the type of shares, for which it is stipulated that voting rights may not be exercised on any matters that can be resolved by the Annual Shareholders' Meeting) (Article 2 (1)).

In cases where the Company intends to solicit persons to subscribe for shares to be issued or subscription rights to shares or where the Company intends to deliver shares (excluding treasury shares), subscription rights to shares (excluding its own subscription rights to shares) or bonds with subscription rights to shares (excluding its own bonds with subscription rights to shares) when exchanging with shares, the Company shall obtain the approval of the Minister of Finance (Article 2 (2)).

Disposal of shares owned by the Japanese government shall be within the limits on the number of shares decided by the Diet in the relevant annual budget (Article 3).

The Group monitors financial indicators in order to maintain a well-balanced capital structure that ensures an appropriate return on equity and a stable and flexible financial condition for future investment. We monitor credit ratings for financial stability and flexibility, and ROE (return on equity) for profitability, while focusing on changes in the domestic and overseas environment.

(2) Financial Risk Management

The Group is exposed to financial risks (credit risk, liquidity risk, foreign exchange risk, interest rate risk, and market price fluctuation risk) in the process of its management activities and it manages risks based on a specific policy in order to avoid or reduce said risks. The results of risk management are regularly reported by the Treasury Division to the president and the Board of Directors of the Company.

The Group policy limits derivatives to transactions for the purpose of mitigating risks from transactions based on actual demand. Therefore, we do not transact derivatives for speculation purposes or trading purposes.

(3) Credit Risk

Receivables, such as note and account receivables, acquired from the operating activities of the Group are exposed to customer credit risk.

The Group holds mainly debt securities for surplus investment and equity securities of customers and suppliers to strengthen relationships with them; those securities are exposed to the issuer's credit risk.

In addition, through derivative transactions that the Group conducts in order to hedge foreign exchange fluctuation risks and interest rate fluctuation risks, we are exposed to the credit risk of the financial institutions which are counterparties to these transactions.

In principle, the Group sets credit lines or transaction conditions with respect to trade receivables for counterparties based on the Credit Management Guidelines in order to control the credit risk relating to counterparties. In addition, the receivable balances of counterparties with high credit risk are monitored. The Treasury Division of the Company regularly monitors the status of the occurrence and collection of bad debts, and reports them to the president and the Board of Directors of the Company.

With regard to the investment of cash surpluses and derivatives, the Group invests in debt securities and other financial instruments with a certain credit rating and transacts with financial institutions with a high credit rating in principle in order to prevent credit risks from occurring and based on the Group Financial Operation Basic Policy. In addition, the Treasury Division of the Company regularly monitors the performance of these transactions and reports the results to the president and the Board of Directors of the Company.

The maximum exposure pertaining to credit risks for financial assets is the carrying amount after considering impairment in the consolidated financial statements.

There is no excessive concentration of the credit risks to certain counterparties.

The Group reviews collectability of trade receivables depending on the credit conditions of counterparties and recognizes allowance for doubtful accounts. The schedule of the allowance for doubtful accounts is as follows.

					Millions of yen
	Trade receivables	Other financial assets			
		Measured at an amount equal to the 12-month expected credit losses	Measured at an amount equal to the full lifetime expected credit losses		
			Non-credit-impaired financial assets	Credit-impaired financial assets	Total
As of January 1, 2018	23,589	—	317	6,252	30,158
Addition	228	—	13	906	1,147
Decrease (intended use)	(19,537)	—	(3)	(117)	(19,656)
Decrease (reversal)	(591)	—	(58)	(979)	(1,628)
Other	(2,040)	—	—	(223)	(2,263)
As of December 31, 2018	1,650	—	269	5,839	7,758
Addition	**1,163**	**—**	**18**	**1**	**1,182**
Decrease (intended use)	**(218)**	**—**	**—**	**(0)**	**(219)**
Decrease (reversal)	**(20)**	**—**	**(57)**	**(78)**	**(155)**
Other	**(100)**	**—**	**—**	**(56)**	**(156)**
As of December 31, 2019	**2,475**	**—**	**230**	**5,705**	**8,409**

(Note) There is no significant change in the carrying amounts of financial assets which affects the change in the allowance for doubtful accounts.

(4) Liquidity Risk

The Group raises funds by borrowings, commercial paper and bonds; however, these liabilities are exposed to the liquidity risk that we would not be able to repay liabilities on the due date due to the deterioration of the financing environment.

In accordance with the Group Financial Operation Basic Policy, the Group establishes a finance plan based on the annual business plan and the Treasury Division of the Company regularly monitors and collects information on the balance of liquidity-in-hand and interest-bearing debt and reports it to the president and the Board of Directors of the Company. In addition, the Group keeps necessary credit facilities to manage liquidity risk by having commitment lines with several financial institutions.

The financial liability balance (including derivative financial instruments) by maturity as of December 31 is as follows:

As of December 31, 2018

Millions of yen

	Carrying amount	Contractual cash flow	Due within one year	Due after one year through two years	Due after two years through three years	Due after three years through four years	Due after four years through five years	Due after five years
Non-derivative financial liabilities								
Trade and other payables	380,516	380,516	380,516	—	—	—	—	—
Short-term borrowings	165,985	165,985	165,985	—	—	—	—	—
Commercial paper	72,038	72,150	72,150	—	—	—	—	—
Current portion of long-term borrowings	12,443	12,443	12,443	—	—	—	—	—
Long-term borrowings	116,870	117,006	—	11,956	11,608	41,610	11,576	40,257
Bonds	610,444	613,773	—	80,000	83,250	30,000	118,275	302,248
Lease liabilities	9,807	13,401	1,305	1,130	992	700	483	8,790
Subtotal	1,368,104	1,375,273	632,399	93,086	95,849	72,309	130,334	351,295
Derivative financial liabilities								
Foreign exchange forward contract	3,176	3,176	3,176	—	—	—	—	—
Subtotal	3,176	3,176	3,176	—	—	—	—	—
Total	1,371,280	1,378,449	635,575	93,086	95,849	72,309	130,334	351,295

As of December 31, 2019

Millions of yen

	Carrying amount	Contractual cash flow	Due within one year	Due after one year through two years	Due after two years through three years	Due after three years through four years	Due after four years through five years	Due after five years
Non-derivative financial liabilities								
Trade and other payables	**408,597**	**408,597**	**408,597**	—	—	—	—	—
Short-term borrowings	**192,581**	**192,581**	**192,581**	—	—	—	—	—
Current portion of long-term borrowings	**11,554**	**11,554**	**11,554**	—	—	—	—	—
Long-term borrowings	**103,743**	**103,847**	—	**11,209**	**41,211**	**11,175**	**20,064**	**20,187**
Current portion of bonds	**80,000**	**80,000**	**80,000**	—	—	—	—	—
Bonds	**586,623**	**590,133**	—	**82,170**	**30,000**	**117,519**	—	**360,444**
Lease liabilities	**53,705**	**58,189**	**15,289**	**10,985**	**6,482**	**4,183**	**2,751**	**18,497**
Subtotal	**1,436,804**	**1,444,901**	**708,022**	**104,364**	**77,694**	**132,877**	**22,815**	**399,128**
Derivative financial liabilities								
Foreign exchange forward contract	**7,739**	**7,739**	**7,739**	—	—	—	—	—
Subtotal	**7,739**	**7,739**	**7,739**	—	—	—	—	—
Total	**1,444,543**	**1,452,640**	**715,761**	**104,364**	**77,694**	**132,877**	**22,815**	**399,128**

The total of commitment lines and withdrawal as of December 31 are as follows:

Millions of yen

	2018	2019
Total committed line of credit	478,531	**470,411**
Withdrawing	—	—
Unused balance	478,531	**470,411**

(5) Foreign Exchange Risk

The Group operates businesses globally and, therefore, is exposed to the following risks due to foreign exchange fluctuation:

(i) The risk where the profit or loss and cash flow in each functional currency of the Group is influenced by foreign exchange fluctuation as a result of external transactions and intergroup transactions, including the payment and receipt of dividends, in currencies that are different from each functional currency of the Group.

(ii) The risk that the equity of the Group is influenced by foreign exchange fluctuation when equity denominated in each functional currency of the Group is translated into Japanese yen and consolidated.

(iii) The risk that the profit or loss of the Group is influenced by foreign exchange fluctuation when profit or loss denominated in each functional currency of the Group is translated into Japanese yen and consolidated.

The Group hedges against risk (i) using derivatives or foreign currency-denominated interest-bearing debts for example, when future cash flow is projected or when receivables and payables are fixed, and some of them are designated as cash flow hedges. The Group hedges against risk (ii) using foreign currency-denominated interest-bearing debts for example, and part of these are designated as net investment hedges. The Group does not hedge against risk (iii) in principle.

In order to mitigate risks mentioned above resulting from the foreign exchange fluctuation, in accordance with the Group Financial Operation Basic Policy, and under the supervision of the Financial Risk Management Committee of the Company, the Group establishes and implements a foreign currency hedge policy, taking into consideration the impact on the Group's performance and the current conditions of the foreign exchange market in a comprehensive manner. The Treasury Division of the Company regularly reports the performances to the president and the Board of Directors of the Company.

Foreign Exchange Sensitivity Analysis

In cases where each currency other than the functional currency that denominates the financial instruments held by the Group as of each year end increases by 10% in value against the functional currency, the impact on profit before income taxes in the consolidated statement of income is as follows:

The impact from the translation of functional currency-denominated financial instruments, and assets, liabilities, income and expenses of foreign operations into Japanese yen is not included. Also, it is based on the assumption that currencies other than the currencies used for the calculation do not fluctuate.

Millions of yen

	2018	2019
Profit before income taxes	(2,725)	**(1,594)**

(6) Interest Rate Risk

Interest rate risk within the Group arises from interest-bearing debts after deducting cash equivalents. Borrowings and bonds with floating rates are exposed to interest rate fluctuation risk.

In order to reduce the interest rate fluctuation risk related to borrowings and bonds, in accordance with the Group Financial Operation Basic Policy, and under the supervision of the Financial Risk Management Committee of the Company, the Group establishes and implements an interest rate hedging policy, taking into consideration the impact on the Group's performance and the current condition of the interest rates in a comprehensive manner. The Treasury Division of the Company reports the performances to the president and the Board of Directors of the Company.

Interest Rate Sensitivity Analysis

In cases where the interest rate of financial instruments held by the Group as of each year end increases by 100bp, the impact on profit before income taxes in the consolidated statement of income is as follows:

The analysis is subject to financial instruments affected by interest rate fluctuation and based on the assumption that other factors, including the impacts of foreign exchange fluctuation, are constant.

Millions of yen

	2018	2019
Profit before income taxes	(955)	**(566)**

(7) Hedging Transactions

The Group's policy for hedging transactions is stated in "3. Significant Accounting Policies."

A. Cash Flow Hedges

The details of hedging instruments designated as cash flow hedges are as follows:

As of December 31, 2018

	Contract amount	Over one year	Carrying amount (Note) (Millions of yen) Assets	Carrying amount (Note) (Millions of yen) Liabilities	Average rate, etc.
Foreign exchange risk					
Foreign exchange forward contract					
JPY/USD	USD 638 mil.	USD —	1,329	613	¥109.21
JPY/CNY	CNY 49 mil.	CNY —	—	8	¥15.92

As of December 31, 2019

	Contract amount	Over one year	Carrying amount (Note) (Millions of yen) Assets	Liabilities	Average rate, etc.
Foreign exchange risk					
Foreign exchange forward contract					
JPY/USD	**USD 187 mil.**	**USD —**	**41**	**227**	**¥106.67**

(Note) Carrying amounts of derivatives are presented as "Other financial assets" or "Other financial liabilities" in the consolidated statement of financial position, and the portion with over one year maturity is classified as "Non-current assets" or "Non-current liabilities."

The schedule of net gains (losses) on hedging instrument designated as cash flow hedges is as follows:

	Millions of yen Effective portion of changes in the fair value of cash flow hedges Foreign exchange risk	Interest rate risk	Total
As of January 1, 2018	(195)	106	(88)
Other comprehensive income			
Amount arising (Note 1)	1,334	(196)	1,138
Reclassification adjustments (Note 2)	194	42	236
Tax effects	(410)	47	(363)
Other	(480)	—	(480)
As of December 31, 2018	443	—	443
Other comprehensive income			
Amount arising (Note 1)	**(882)**	**—**	**(882)**
Reclassification adjustments (Note 2)	**320**	**—**	**320**
Tax effects	**171**	**—**	**171**
Other	**(185)**	**—**	**(185)**
As of December 31, 2019	**(132)**	**—**	**(132)**

(Note 1) The change in value of the hedged item used as the basis for recognizing hedge ineffectiveness approximates the change in fair value of the hedging instrument.
(Note 2) The amount, which is reclassified when the hedged item affects profit or loss, is recognized in "Revenue," "Financial income" or "Financial costs" in the consolidated statement of income. The amount of hedge ineffectiveness is immaterial.

B. Hedge of Net Investment in Foreign Operations

The details of hedging instruments designated as hedge of net investment are mainly as follows:

As of December 31, 2018

	Contract amount	Over one year	Carrying amount (Note) (Millions of yen) Assets	Liabilities	Average rate, etc.
Bonds in USD	USD 1,250 mil.	USD 1,250 mil.	—	138,384	¥109.41
Bonds in GBP	GBP 400 mil.	GBP 400 mil.	—	55,216	$1.32
Foreign exchange forward contract					
EUR / RUB	RUB 19,973 mil.	RUB —	516	338	€0.012
USD / TWD	TWD 6,113 mil.	TWD —	67	—	$0.033

As of December 31, 2019

	Contract amount	Over one year	Carrying amount (Note) (Millions of yen) Assets	Liabilities	Average rate, etc.
Bonds in USD	**USD 1,250 mil.**	**USD 1,250 mil.**	**—**	**136,675**	**¥109.41**
Bonds in EUR	**EUR 567 mil.**	**EUR 567 mil.**	**—**	**69,132**	**$1.11**
Bonds in GBP	**GBP 400 mil.**	**GBP 400 mil.**	**—**	**56,089**	**$1.32**
Foreign exchange forward contract					
EUR / RUB	**RUB 29,502 mil.**	**RUB —**	**—**	**930**	**€0.014**
JPY / USD	**USD 400 mil.**	**USD —**	**—**	**749**	**¥106.68**
USD / TWD	**TWD 7,518 mil.**	**TWD —**	**—**	**399**	**$0.033**
GBP / USD	**USD 245 mil.**	**USD —**	**15**	**395**	**£0.77**
EUR / USD	**USD 183 mil.**	**USD —**	**—**	**358**	**€0.89**

(Note) Carrying amounts of bonds are presented as "Bonds and borrowings" in the consolidated statement of financial position, and the portion with over one year maturity is classified as "Non-current liabilities." Carrying amounts of derivatives are presented as "Other financial assets" or "Other financial liabilities" in the consolidated statement of financial position, and the portion with over one year maturity is classified as "Non-current assets" or "Non-current liabilities."

The schedule of net gains (losses) on hedging instrument designated as hedge of net investment in foreign operations is as follows:

	Millions of yen 2018	2019
As of January 1	10,793	**17,842**
Other comprehensive income		
Amount arising (Note 1)	9,652	**(7,271)**
Tax effects	(2,603)	**(233)**
As of December 31 (Note 2)	17,842	**10,338**

(Note 1) The change in value of the hedged item used as the basis for recognizing hedge ineffectiveness approximates the change in fair value of the hedging instrument.
(Note 2) Net gain arising from the hedging instruments for which hedge accounting is discontinued were ¥17,505 million and ¥14,683 million as of December 31, 2018 and 2019 respectively those which are included in the exchange differences on translation of foreign operations.

(8) Market Price Fluctuation Risk

With respect to securities, the Group regularly assesses the fair value and financial conditions of the issuers, and each relevant department reviews the portfolio held by taking into account the relationship with counterparty entities as necessary.

(9) Fair Value of Financial Instruments

The fair value hierarchy of financial instruments is categorized from Level 1 to Level 3 as follows:

Level 1: Fair value measured at the quoted price in the active market
Level 2: Fair value that is calculated using the observable price other than categorized in Level 1 directly or indirectly
Level 3: Fair value that is calculated based on valuation techniques which include inputs that are not based on observable market data

A. Financial Instruments Measured at Amortized Cost

The carrying amount and fair value hierarchy of financial instruments measured at amortized cost as of December 31 are as follows:

As of December 31, 2018

	Carrying amount	Millions of yen Fair value Level 1	Level 2	Level 3	Total
Long-term borrowings (Note)	129,313	—	—	129,978	129,978
Bonds	610,444	606,495	—	—	606,495

As of December 31, 2019

					Millions of yen
					Fair value
	Carrying amount	Level 1	Level 2	Level 3	Total
Long-term borrowings (Note)	**115,297**	**—**	**116,804**	**—**	**116,804**
Bonds (Note)	**666,623**	**683,650**	**—**	**—**	**683,650**

(Note) Current portion is included.

With regard to short-term financial assets and short-term financial liabilities measured at amortized cost, their fair value approximates the carrying amount.

The fair value of long-term borrowings is calculated based on the present value which is obtained by discounting the total of the principal and interest by the interest rate assumed in a case where the same loan is newly made.

B. Financial Instruments Measured at Fair Value

The fair value hierarchy of financial instruments measured at fair value as of December 31 is as follows:

As of December 31, 2018

				Millions of yen
	Level 1	Level 2	Level 3 (Note)	Total
Derivative assets	—	8,653	—	8,653
Equity securities	58,847	—	5,837	64,684
Other	401	11,025	4,514	15,940
Total	59,248	19,677	10,351	89,277
Derivative liabilities	—	3,176	—	3,176
Total	—	3,176	—	3,176

As of December 31, 2019

				Millions of yen
	Level 1	Level 2	Level 3 (Note)	Total
Derivative assets	**—**	**2,564**	**—**	**2,564**
Equity securities	**25,829**	**—**	**6,919**	**32,747**
Other	**442**	**17,673**	**5,008**	**23,123**
Total	**26,270**	**20,238**	**11,927**	**58,435**
Derivative liabilities	**—**	**7,739**	**—**	**7,739**
Total	**—**	**7,739**	**—**	**7,739**

(Note) The schedule of financial instruments that are classified in Level 3 is as follows:

		Millions of yen
	2018	2019
As of January 1	9,342	**10,351**
Total gain (loss)		
Profit or loss (Note 1)	(341)	**209**
Other comprehensive income (Note 2)	(1003)	**(182)**
Purchases	2,270	**1,660**
Sales	(81)	**(140)**
Other	164	**29**
As of December 31	10,351	**11,927**

(Note 1) Gains and losses included in profit or loss for the years ended December 31, 2018 and 2019 are related to financial assets measured at fair value through profit or loss as of the year end. These gains and losses are included in "Financial income" and "Financial costs."

(Note 2) Gains and losses included in other comprehensive income for the years ended December 31, 2018 and 2019 are related to financial assets measured at fair value through other comprehensive income as of the year end. These gains and losses are included in "Net gain (loss) on revaluation of financial assets measured at fair value through other comprehensive income."

35. Related Parties

Based on the Japan Tobacco Inc. Act, the Japanese government shall hold more than one-third of all of the shares issued by the Company (excluding the type of shares, for which it is stipulated that voting rights may not be exercised on any matters that can be resolved by Annual Shareholders' Meeting). As of December 31, 2019, the Japanese government held 33.35% of all outstanding shares of the Company.

(1) Related-party Transactions

Related-party transactions are conducted under the same conditions as regular business transactions.

The Group's revenue from CJSC TK Megapolis, the local Russian distribution affiliate, was ¥216,913 million and ¥202,780 million for the years ended December 31, 2018 and 2019, respectively. The Group held trade receivables of ¥44,436 million and ¥38,640 million from CJSC TK Megapolis as of December 31, 2018 and 2019, respectively.

(2) Remuneration for Directors and Audit and Supervisory Board Members

Remuneration for directors and audit and supervisory board members for each year is as follows:

		Millions of yen
	2018	2019
Remuneration and bonuses	795	**673**
Share-based payments	109	**115**
Total	904	**788**

36. Subsidiaries, Associates and Others

(The composition of the Group)

The composition of the Group by reportable segment as of December 31 is as follows:

	2018		2019	
Reportable Segments	Number of subsidiaries	Number of entities accounted for using the equity method (Note)	Number of subsidiaries	Number of entities accounted for using the equity method (Note)
Domestic Tobacco	13	1	**13**	**1**
International Tobacco	166	5	**171**	**7**
Pharmaceuticals	2	—	**2**	**—**
Processed Food	29	3	**28**	**3**
Other	14	2	**17**	**2**
Total	224	11	**231**	**13**

(Note) No associates or joint ventures are considered to be material to the Group.

There is no significant change in the composition of the Group for the year ended December 31, 2019.

Regarding the restrictions on the ability to use the assets of the Group, please refer to "7. Cash and Cash Equivalents."

37. Commitments

(1) Commitments for the Acquisition of Assets

Commitments for the acquisition of assets as of December 31 are as follows:

		Millions of yen
	2018	2019
Acquisition of property, plant and equipment	54,030	**35,747**
Acquisition of intangible assets	3,127	**1,602**
Total	57,157	**37,348**

(2) Procurement of Domestic Leaf Tobacco

With regard to the procurement of domestic leaf tobacco by the Company, based on the Tobacco Business Act, the Company enters into purchase contracts with domestic leaf tobacco growers every year, and the contracts determine the area under cultivation by type of tobacco and the prices by type and quality of tobacco leaf. Under the contracts, the Company is obligated to purchase all domestic leaf tobacco produced pursuant to such contracts, except for any domestic leaf tobacco not suited for the manufacture of tobacco products.

38. Contingencies

Contingent Liabilities

The Company and some of its subsidiaries are defendants in legal proceedings. Provisions are not accounted for in matters where it is not practicable to reasonably estimate the final outcomes.

The Company and some of its subsidiaries, who are defendants in such legal proceedings, believe that our defenses asserted in these proceedings are based on substantial evidence and implement the system for the response to action with the assistance of external lawyers.

(1) Smoking and Health Related Litigation

The Company and some of its subsidiaries are defendants in lawsuits filed by plaintiffs seeking damages for harm allegedly caused by smoking, the marketing of tobacco products, or exposure to tobacco smoke. As of December 31, 2019, there were a total of 20 smoking and health related cases pending in which one or more members of the Group were named as a defendant or for which the Company may have certain indemnity obligations pursuant to the agreement such as for the Company's acquisition of RJR Nabisco Inc.'s overseas (non-U.S.) tobacco operations.

The major ongoing smoking and health related cases are as follows:

On March 8, 2019, JTI-Macdonald Corp. (hereinafter referred to as "JTI-Mac"), the Company's Canadian subsidiary, filed for protection from its creditors under the Companies' Creditors Arrangement Act (CCAA). The Ontario Superior Court has granted the CCAA application and extended protection in favor of JTI-Mac (hereinafter referred to as "CCAA Proceedings"). All of the below Canadian matters against JTI-Mac have been stayed by the CCAA Proceedings, under which JTI-Mac carries on business in the ordinary course.

A. Individual Claim

There is one individual case brought against the Company's indemnitee in South Africa.

South Africa Individual Claim (Joselowitz):

The individual claim was brought against the Company's indemnitee in South Africa in October 2000. Plaintiff seeks compensatory and punitive damages, alleging that the Company's indemnitee marketed products which it knew to be dangerous to health, manipulated nicotine content to foster addiction, failed to comply with South African labeling requirements and participated in a clandestine worldwide operation to encourage children to smoke. This case has been dormant since February 2001.

In addition, there is one individual case (which is currently dormant) brought against the Company's subsidiary in Ireland.

B. Class Actions

There are eight ongoing class actions in Canada against the Company's subsidiary and/or indemnitees.

Canada Quebec Class Action (Cecilia Letourneau):

This class action was brought in September 1998 against three Canadian tobacco manufacturers including JTI-Mac. Plaintiffs were seeking a total of approximately ¥384.7 billion (approximately CAD 4.6 billion) in compensatory damages, an amount for which all the defendants are jointly and severally liable, and a total amount of approximately ¥384.7 billion (approximately CAD 4.6 billion) in punitive damages, to be divided among all the defendants based on their respective market shares.

The Quebec Superior Court published the first instance judgment in favor of the plaintiffs in June 2015. In June 2015, JTI-Mac and other tobacco manufacturers appealed the judgment to the Quebec Court of Appeal, and the appeal on the merits was heard and concluded in November 2016.

In March 2019, the Quebec Court of Appeal dismissed the appeal of defendants by substantively upholding the first instance judgment and ordering a punitive damage award against the appellants of approximately ¥13.5 billion (approximately CAD 161 million), in which the share of the total damage award against JTI-Mac is approximately ¥1.3 billion (approximately CAD 15 million). The time limit for seeking leave to appeal the decision to the Supreme Court of Canada is suspended during the CCAA Proceedings. Enforcement of the judgement is stayed by the CCAA Proceedings.

Canada Quebec Class Action (Conseil Québécois sur le tabac et la santé):

This class action was brought in November 1998 against three Canadian tobacco manufacturers including JTI-Mac. Plaintiffs were seeking a total of approximately ¥1,042.2 billion (approximately CAD 12.4 billion) in compensatory damages, an amount for which all the defendants are jointly and severally liable, and a total amount of approximately ¥67.9 billion (approximately CAD 0.8 billion) in punitive damages, to be divided among all the defendants based on their respective market shares.

The Quebec Superior Court published the first instance judgment in favor of the plaintiffs in June 2015. In June 2015, JTI-Mac and other tobacco manufacturers appealed the judgment to the Quebec Court of Appeal, and the appeal on the merits was heard and concluded in November 2016.

In March 2019, the Quebec Court of Appeal dismissed the appeal of the defendants by substantively upholding the first instance judgment and ordering a compensatory damage award jointly and severally against the defendants of approximately ¥1,133.6 billion (approximately CAD 13.5 billion), in which the share of the total damage award against JTI-Mac is approximately ¥147.4 billion (approximately CAD 1.8 billion), and a punitive damage award of approximately ¥3 million (approximately CAD 0.04 million) per defendants. The time limit for seeking leave to appeal the decision to the Supreme Court of Canada is suspended during the CCAA Proceedings. Enforcement of the judgement is stayed by the CCAA Proceedings.

The Quebec Court of Appeal rendered one judgment for both class actions against the defendants and ordered them to make an initial deposit of approximately ¥97.3 billion (approximately CAD 1.2 billion), in which the share of JTI-Mac is approximately ¥12.2 billion (approximately CAD 145 million). The obligation to pay the initial deposit is stayed by the CCAA Proceedings.

Canada Saskatchewan Class Action (Adams):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2009. Plaintiffs are seeking unspecified compensatory and punitive damages on behalf of class members who allege to be or have been addicted to nicotine contained in cigarettes manufactured by the defendants. The preliminary motions are pending. The case was dormant and is currently stayed by the CCAA Proceedings.

Canada Manitoba Class Action (Kunta):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2009. Plaintiffs are seeking unspecified compensatory and punitive damages on behalf of class members who allege to be or have been addicted to nicotine contained in cigarettes manufactured by the defendants. The statement of claim was served on the Company's indemnitees but not on JTI-Mac. The case was dormant and is currently stayed by the CCAA Proceedings.

Canada Nova Scotia Class Action (Semple):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2009. Plaintiffs are seeking unspecified compensatory and punitive damages on behalf of class members who allege to be or have been addicted to nicotine contained in cigarettes manufactured by the defendants. The statement of claim was served on the Company's indemnitees but not on JTI-Mac. The case was dormant and is currently stayed by the CCAA Proceedings.

Canada British Columbia Class Action (Bourassa):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2010. Plaintiffs are seeking unspecified compensatory and punitive damages for class members. The preliminary motions are pending. The case was dormant and is currently stayed by the CCAA Proceedings.

Canada British Columbia Class Action (McDermid):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2010. Plaintiffs are seeking unspecified compensatory and punitive damages for class members. The preliminary motions are pending. The case was dormant and is currently stayed by the CCAA Proceedings.

Canada Ontario Class Action (Jacklin):

This class action was brought against tobacco industry members including JTI-Mac and the Company's indemnitees in June 2012. Plaintiffs are seeking unspecified compensatory and punitive damages for class members. The preliminary motions are pending. The case was dormant and is currently stayed by the CCAA Proceedings.

C. Health-Care Cost Recovery Litigation

There are 10 ongoing health-care cost recovery cases in Canada pending against the Company's subsidiary and indemnitees brought by all the Canadian provinces (except three Canadian territories). These provinces filed lawsuits under their own provincial legislation which was enacted exclusively for the purpose of authorizing the provincial government to file a direct action against tobacco manufacturers to recoup the health-care costs the government has allegedly incurred and will incur, resulting from "tobacco related wrongs."

Canada British Columbia Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of British Columbia in January 2001 against tobacco industry members including JTI-Mac and the Company's indemnitees based on its provincial legislation, the "Tobacco Damages and Health-Care Costs Recovery Act." The claim amount is unspecified. In 2001, several defendants challenged the legislation's constitutionality, which was ultimately rejected by the Supreme Court of Canada in September 2005. The action remains pending in the first instance. The case is stayed by the CCAA Proceedings.

Canada New Brunswick Health-Care Cost Recovery Litigation:

This health-care cost recovery litigation was filed by the Province of New Brunswick in March 2008 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The case is stayed by the CCAA Proceedings.

Canada Ontario Health-Care Cost Recovery Litigation:
This health-care cost recovery litigation was filed by the Province of Ontario in September 2009 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The statement of claim contains allegations of joint and several liabilities among all the defendants but does not specify any individual amount or percentages within the total claimed amount of ¥27,650.7 billion (CAD 330 billion). The case is stayed by the CCAA Proceedings.

Canada Newfoundland and Labrador Health-Care Cost Recovery Litigation:
This health-care cost recovery litigation was filed by the Province of Newfoundland and Labrador in February 2011 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The case is stayed by the CCAA Proceedings.

Canada Manitoba Health-Care Cost Recovery Litigation:
This health-care cost recovery litigation was filed by the Province of Manitoba in May 2012 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The case is stayed by the CCAA Proceedings.

Canada Quebec Health-Care Cost Recovery Litigation:
This health-care cost recovery litigation was filed by the Province of Quebec in June 2012 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The statement of claim contains allegations of joint and several liabilities among all the defendants but does not specify any individual amount or percentages within the total amount of the claim approximately ¥5,082.5 billion (approximately CAD 60.7 billion). The case is stayed by the CCAA Proceedings.

Canada Alberta Health-Care Cost Recovery Litigation:
This health-care cost recovery litigation was filed by the Province of Alberta in June 2012 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The statement of claim contains allegations of joint and several liabilities among all the defendants but does not specify any individual amount or percentages within the total claimed amount of at least ¥837.9 billion (CAD 10.0 billion). The case is stayed by the CCAA Proceedings.

Canada Saskatchewan Health-Care Cost Recovery Litigation:
This health-care cost recovery litigation was filed by the Province of Saskatchewan in June 2012 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The case is stayed by the CCAA Proceedings.

Canada Prince Edward Island Health-Care Cost Recovery Litigation:
This health-care cost recovery litigation was filed by the Province of Prince Edward Island in September 2012 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The case is stayed by the CCAA Proceedings.

Canada Nova Scotia Health-Care Cost Recovery Litigation:
This health-care cost recovery litigation was filed by the Province of Nova Scotia in January 2015 against tobacco industry members including JTI-Mac and the Company's indemnitees based on legislation similar to that introduced in the Province of British Columbia. The claim amount is unspecified. The claim amount is unspecified. The case is stayed by the CCAA Proceedings.

(2) Other Legal Proceedings
The Company and some of its subsidiaries are also engaged in other legal proceedings such as commercial and tax disputes.

(Note) The amount of damages sought denominated in foreign currencies is translated into Japanese yen at the rates as of December 31, 2019.

39. Subsequent Events

The Company entered into loan agreements with banks as follows:

(1) Lenders: Mizuho Bank, Ltd., MUFG Bank, Ltd., Sumitomo Mitsui Banking Corporation and Sumitomo Mitsui Trust Bank, Limited

(2) Aggregate amount of borrowings: ¥100 billion

(3) Interest rates: Floating rates (TIBOR plus spread)

(4) Drawdown date: January 31, 2020

(5) Repayment date: January 31, 2080
The Company may, at its option, repay early all or a portion of the principal on any Interest Payment Date on or after the Interest Payment Date of January 2025.

(6) Collateral/Guarantee: None

(7) Use of proceeds: Repayment of existing debts and working capital

(8) Other borrowing terms:

a. Interest deferral clause
The Company may, at its option, defer the payment of interest.

b. Subordination clause
The lenders shall have subordinated claim rights subordinated to senior debts in liquidation proceedings, bankruptcy proceedings, reorganization proceedings, civil rehabilitation proceedings or any other equivalent proceedings other than those under the laws of Japan.
No terms and conditions of the Subordinated Loan Agreement may be amended in a manner detrimental in any way to any creditors of the Company other than the creditors of the subordinated receivables.

c. Replacement restrictions
There is no contractual provision on replacement restrictions.
Provided, when making a prepayment of the Subordinated Loan, the Company intends to replace it with the funds raised by common stock or financial instruments that have equity credit attributes approved by rating agencies to be equal to or higher than the Subordinated Loan within twelve months prior to the prepayment date. However, the Company may decide not to replace the Subordinated Loan with the approved funds that have equal or higher equity credit attributes, if predefined financial requirements are met.

Others

A. Quarterly Information for the Year ended December 31, 2019

Millions of yen

	Q1 January 1, 2019 to March 31, 2019	Q2 January 1, 2019 to June 30, 2019	Q3 January 1, 2019 to September 30, 2019	2019 January 1, 2019 to December 31, 2019
Revenue	505,422	1,058,549	1,633,748	2,175,626
Profit before income taxes for the period (year)	172,727	290,618	411,564	465,232
Profit attributable to owners of the parent company for the period (year)	120,840	226,451	316,148	348,190
Basic earnings per share for the period (year) (yen)	67.66	127.23	177.83	195.97

	Q1 January 1, 2019 to March 31, 2019	Q2 April 1, 2019 to June 30, 2019	Q3 July 1, 2019 to September 30, 2019	2019 October 1, 2019 to December 31, 2019
Basic earnings per share for the quarter (yen)	67.66	59.54	50.57	18.06

B. Significant Lawsuits
The significant lawsuits of the Group are as stated in "38. Contingencies" in the notes to consolidated financial statements.

Deloitte.

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of Japan Tobacco Inc.:

We have audited the accompanying consolidated statement of financial position of Japan Tobacco Inc. and its consolidated subsidiaries as of December 31, 2019, and the related consolidated statements of income, comprehensive income, changes in equity, and cash flows for the fiscal year from January 1, 2019 to December 31, 2019, and notes to consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Japan Tobacco Inc. and its consolidated subsidiaries as of December 31, 2019, and the consolidated results of their operations and their cash flows for the fiscal year then ended in accordance with International Financial Reporting Standards.

Deloitte Touche Tohmatsu LLC

March 19, 2020

Member of
Deloitte Touche Tohmatsu Limited

Glossary of Terms

Unless otherwise stated, terms and numbers reported in this glossary are in accordance with IFRS.

Adjusted Operating Profit: Operating profit + Amortization cost of acquired intangibles arising from business acquisitions + Adjusted items (income and costs).*

* Adjusted items (income and costs) = Impairment losses on goodwill ± restructuring income and costs ± others

ALP: Agricultural labor practices.

BnU: Billion Units.

CDP: Headquartered in London, CDP is the leading international non-profit organization that accelerates action to achieve a sustainable economy, assessing disclosure and impacts by corporations from around the world.

Constant Exchange Rates (Constant FX): Constant exchange rates are computed by restating current year results at the previous year's foreign currency exchange (FX) rate. Results at constant rates of exchange should be considered in addition to, not as a substitute for, results reported in accordance with IFRS.

Contraband: Genuine products smuggled from abroad that are diverted from the legitimate supply chain and sold in a country other than the intended retail market without payment of domestic duty in that country.

Core Revenue (International Tobacco Business): Includes revenue from waterpipe tobacco and Reduced-Risk Products, but excludes revenue from distribution, contract manufacturing and other peripheral businesses.

Core Revenue (Japanese Domestic Tobacco Business): Excludes revenue from distribution of imported tobacco in the Japanese domestic tobacco business, among others, but includes revenue from domestic duty free, the China business, little cigars and Reduced-Risk Products such as Ploom TECH devices and capsules.

Counterfeit: Fake products appearing to be genuine brand products protected by intellectual property rights. Counterfeit products are manufactured without authorization from the rights' owners and with the intent to copy the genuine brand to deceive the consumer. They are also sold without duties being paid.

DJSI (Dow Jones Sustainability Indices): The DJSI is a collaborative initiative by S&P Dow Jones Indices of the United States and RobecoSAM of Switzerland. It assesses the sustainability performance of companies, based on economic, environmental and social criteria.

FCF (Free Cash Flow): FCF is sum of cash flows from operating activities and investing activities, but excludes the following items:
- From operating CF: depreciation from lease transactions, interest received, dividends received, interest paid and income taxes related to these items excluding lease transactions
- From investing CF: purchase of investment securities (both short-term and long-term), payments into time deposits, proceeds from sale or redemption of investment securities (both short-term and long-term), proceeds from withdrawal of time deposits and other investing activities not for business operation purposes

Fine Cut: Fine Cut represents tobacco products which are packed in a loose, fine-cut form in pouches and are also known as rolling tobacco, used for both RYO "roll-your-own" cigarettes (made using rolling papers) and MYO "make-your-own" cigarettes (made by filling a filter tube with cut tobacco).

GFB: Global Flagship Brands (Winston, Camel, MEVIUS, LD).

GHG emissions: Greenhouse gas emissions.

GHG Scope 1: Direct GHG emissions from corporate activities, such as burning of fossil fuels at factories.

GHG Scope 2: Indirect GHG emissions from consumption of purchased electricity, heat or steam.

GHG Scope 3: Other indirect emissions, including from manufacture of products bought from other companies.

IFRS: International Financial Reporting Standards.

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

JPY BN: Billion Japanese yen.

JT Cigarette Sales Volume (Japanese Domestic Tobacco Business): Excludes sales volume of domestic duty free, the China business and Reduced-Risk Products.

Profit: Profit attributable to owners of the parent.

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

Restated: See "Constant Exchange Rates."

Revenue: Excluding tobacco excise taxes and revenue from agent transactions.

RMC: Ready-Made Cigarettes.

Science Based Targets (SBT): SBT is a joint initiative that enables businesses to take swift climate action by setting ambitious emission reduction targets.

SDGs: The Sustainable Development Goals (SDGs) were adopted by all United Nations Member States in 2015 as a universal call to action to end poverty, protect the planet and ensure that all people enjoy peace and prosperity by 2030.

TableMark: References to "TableMark" are to TableMark Co., Ltd.

Total Shipment Volume (International Tobacco Business): The shipment volume of tobacco-based products which includes Fine Cut, cigars, pipe tobacco, snus, kretek and T-Vapor but excludes contract manufactured products, waterpipe tobacco and E-Vapor.

USD MM: Million U.S. dollars.

Awards and Recognition

Dow Jones Sustainability Indices

We are a member of the Dow Jones Sustainability Asia Pacific Index, and we were recognized with SAM Bronze Class 2020 ranking and as a SAM Industry Mover 2020 for the first time.

JT Group press release
September 2019
The Sustainability Yearbook 2020

FTSE Blossom Japan

We have been selected as a member of FTSE Blossom Japan Index every year since 2017. FTSE Blossom Index (selected by GPIF as a core ESG benchmark) is designed to measure the performance of Japanese companies that demonstrate strong sustainability practices.

FTSE Blossom Japan
February 2020

CDP A List and Supplier Engagement Leader

Achieving a place on CDP "A List" for climate change (press release in January 2020) and water security (press release in February 2020). We are also recognized as a global leader for engaging our supply chain in climate change activities.

Learn more on JT.com.

Science Based Targets

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

JT Group press release
February 2019

Global Child Forum

We were recognized as a "leader" by the Global Child Forum, as part of their 2019 Global Corporate Sector and Children's Rights Benchmark Report "The State of Children's Rights and Business: From Promise to Practice."

Final score card
November 2019

PRIDE Index

In the PRIDE Index, which highlights the most LGBT-friendly companies, JT achieved Gold status, the highest ranking, for the fourth consecutive year.

work with Pride – PRIDE index –
October 2019

Platinum Kurumin Certification

JT is certified as a childcare-supporting company by the Japanese Ministry of Health, Labor and Welfare.

Platinum Kurumin Certification (in Japanese)
2019

Top Employer

Our international tobacco business was certified as a Global Top Employer for the sixth consecutive year.

Top Employer
February 2020

Nadeshiko Brand

JT was selected as a "Nadeshiko Brand" that encourages women's success in the workplace.

Nadeshiko Brand
March 2020

Equal Salary Employer

In January 2019, the headquarters of JTI became the first Geneva-based multinational headquarters to be certified as an equal salary employer by the EQUAL-SALARY Foundation.

White 500

JT was selected as a Certified Health and Productivity Management Organization (White 500) for our outstanding health-conscious management.

White 500
March 2020

Shareholder Information

As of December 31, 2019

Common Stock

Authorized:	8,000,000,000
Issued:	2,000,000,000
Number of shareholders:	515,211

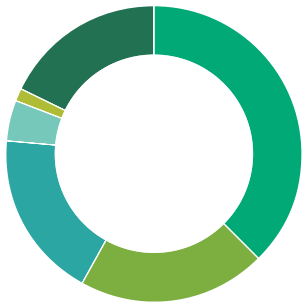
Share Registrar

Mitsubishi UFJ Trust and Banking Corporation
4-5, Marunouchi 1-chome, Chiyoda-ku, Tokyo

Listing

Tokyo Stock Exchange: First Section

Composition of Shareholders (excluding treasury stock)



Principal Shareholders

Name	Shares held
Minister of Finance	666,926,200
The Master Trust Bank of Japan, Ltd. (Trust Account)	88,722,600
Japan Trustee Services Bank, Ltd. (Trust Account)	54,377,600
SMBC Nikko Securities Inc.	29,357,000
Trust & Custody Services Bank, Ltd. as trustee for Mizuho Bank, Ltd. Retirement Benefit Trust Account re-entrusted by Mizuho Trust and Banking Co., Ltd.	23,660,000
Japan Trustee Services Bank, Ltd. (Trust Account 5)	23,508,500
JP Morgan Chase Bank 385151 (Standing proxy: Mizuho Bank, Ltd., Settlement Sales Department)	22,262,535
JP Morgan Chase Bank 380055 (Standing proxy: Mizuho Bank, Ltd., Settlement Sales Department)	21,612,342
State Street Bank West Client-Treaty 505234 (Standing proxy: Mizuho Bank, Ltd., Settlement Sales Department)	21,561,341
Japan Trustee Services Bank, Ltd. (Trust Account 9)	18,737,300

Government Offerings of JT Shares

1st Offering

Method	Offering by Bids	Offering by non-Bids
Offer price (Pricing date)	Bid price: From ¥1,362,000 to ¥2,110,000 Weighted average price: ¥1,438,000 (August 29, 1994)	¥1,438,000 (August 31, 1994)
Number of shares offered	229,920 shares	164,356 shares
Offer term	From August 15 to 18, 1994	From September 2 to 8, 1994

Note:
Listing date: October 27, 1994
Exchange: First Section of Tokyo Stock Exchange

2nd and 3rd, 4th Offering

	2nd Offering	3rd Offering	4th Offering
Method	Offering by Book-Building formula	Offering by Book-Building formula	Offering by Book-Building formula
Offer price (Pricing date)	¥815,000 (June 17, 1996)	¥843,000 (June 7, 2004)	¥2,949 (March 11, 2013)
Number of shares offered	Japan: 237,390 shares, International: 35,000 shares (Total: 272,390 shares)	Japan: 198,334 shares, International: 91,000 shares (Total: 289,334 shares)	Japan: 145,625,500 shares, International: 107,636,300 shares (Total: 253,261,800 shares)
Offer term	From June 18 to 19, 1996	From June 8 to 10, 2004	From March 12 to 13, 2013

Corporate Data

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8, rue Kazem Radjavi
1202 Geneva, Switzerland
Tel: +41 (0)22-703-0777
Fax: +41 (0)22-703-0789
URL: https://www.jti.com/

Date of Establishment
April 1, 1985

Paid-in Capital
100 billion yen