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Consolidated Eleven-Year Financial Summary

Japan Tobacco Inc. and Consolidated Subsidiaries / Years ended March 31

	2000	2001	2002	2003
For the year:				
Net sales	¥4,371,250	¥4,501,701	¥4,544,175	¥4,492,264
Tobacco	4,024,487	4,140,270	4,178,034	4,134,466
Japanese domestic	—	—	—	—
International	—	—	—	—
Pharmaceutical	67,790	66,414	61,868	53,927
Food	195,026	210,332	221,197	232,404
Others	83,947	84,685	83,076	71,467
Taxation	—	—	—	—
Net sales excluding excise taxes	—	—	—	—
Adjusted net sales excluding excise taxes (Note 2)	—	—	—	—
EBITDA (Note 3)	¥ 315,132	¥ 312,045	¥ 334,119	¥ 337,296
Tobacco	299,477	296,318	320,969	321,419
Japanese domestic	—	—	—	—
International	—	—	—	—
Pharmaceutical	(790)	(3,105)	(8,519)	(5,110)
Food	(490)	(2,660)	2,259	546
Others	16,093	20,033	19,617	19,674
Elimination/Corporate	842	1,459	(207)	767
Depreciation and Amortization (Note 3)	161,160	172,080	170,314	148,333
Operating income (loss)	¥ 153,972	¥ 139,965	¥ 163,805	¥ 188,963
Tobacco	181,520	165,923	192,114	213,342
Japanese domestic	—	—	—	—
International	—	—	—	—
Pharmaceutical	(11,482)	(12,827)	(18,985)	(13,855)
Food	(14,582)	(17,362)	(11,860)	(13,168)
Others	(1,764)	3,428	1,797	932
Elimination/Corporate	280	803	739	1,712
Net income (loss)	50,792	43,687	36,850	75,302
For the year:				
Net cash provided by operating activities	¥ 288,271	¥ 393,958	¥ 89,727	¥ 258,057
Net cash provided by (used in) investing activities	(899,139)	(90,477)	(40,472)	(74,877)
Net cash provided by (used in) financing activities	472,593	(76,990)	(124,838)	(111,968)
Free cash flow (Note 4)	(786,499)	307,311	31,413	170,372
At year-end:				
Net property, plant and equipment	¥ 770,639	¥ 757,311	¥ 743,712	¥ 733,314
Total assets	3,095,298	3,188,230	3,063,077	2,957,665
Interest-bearing Debt (Note 5)	660,525	606,089	511,738	424,499
Liabilities	1,515,539	1,618,877	1,400,384	1,283,939
Total equity	1,526,583	1,513,846	1,613,105	1,622,654
Ratios:				
Return on equity (ROE)	3.5%	2.9%	2.4%	4.7%
Return on assets (ROA)	—	—	5.4%	6.4%
Operating income margin	3.5%	3.1%	3.6%	4.2%
Total assets turnover (times)	1.64	1.43	1.45	1.49
Equity ratio	49.3%	47.5%	52.7%	54.9%
Debt/Equity ratio (times)	0.43	0.40	0.32	0.26
Current ratio	198.2%	169.7%	196.3%	226.4%
Fixed assets/Long-term capital ratio	72.5%	78.1%	74.9%	69.7%

Notes: 1. Figures stated in U.S. dollars in this report are translated solely for convenience at the rate of ¥93.04 per $1, the rate of exchange as of March 31, 2010.

2. 2005–2008: Excluding imported tobacco in the Japanese domestic tobacco and distribution business in the international tobacco, respectively.
2009–: Excluding the imported tobacco, domestic duty free, the China Division and other miscellaneous items in the Japanese domestic tobacco business, in addition to the distribution, private label, contract manufacturing and other peripheral businesses in the international tobacco business.

3. EBITDA = operating income + depreciation and amortization
Depreciation and amortization = depreciation of tangible fixed assets + amortization of intangible fixed assets + amortization of long-term prepaid expenses + amortization of goodwill

4. FCF = (cash flow from operating activities + cash flow from investing activities) excluding the following items:
From "cash flow from operating activities": Dividends received / interest received and its tax effect / interest paid and its tax effect
From "cash flow from investing activities": Cash outflow from purchase of marketable securities / proceeds from sales of marketable securities / cash outflow from purchases of investment securities / proceeds from sales of investment securities / others (but not business-related investment securities, which are included in the investment securities item)

5. Interest-bearing Debt includes lease obligation after FY 2008.

6. Financial data disclosed herein are basically rounded.

						Millions of yen	Millions of U.S. dollars (Note 1)
2004	2005	2006	2007	2008	2009	**2010**	**2010**
¥4,625,151	¥4,664,514	¥4,637,657	¥4,769,387	¥ 6,409,727	¥6,832,307	**¥6,134,695**	**$65,936**
4,236,920	—	—	—	—	—	**—**	**—**
—	3,491,488	3,405,281	3,416,274	3,362,398	3,200,494	**3,042,836**	**32,705**
—	792,705	881,188	999,658	2,639,969	3,118,319	**2,633,636**	**28,306**
51,242	57,676	49,257	45,452	49,064	56,758	**44,069**	**474**
250,138	265,380	278,378	286,554	336,420	435,966	**394,653**	**4,242**
86,851	57,265	23,553	21,449	21,876	20,770	**19,501**	**209**
2,605,343	2,650,586	2,628,878	2,718,358	3,822,331	4,005,123	**3,620,543**	**38,914**
2,019,807	2,013,927	2,008,780	2,051,029	2,587,396	2,827,184	**2,514,152**	**27,022**
—	1,684,404	1,596,151	1,633,186	2,068,368	2,243,146	**1,980,970**	**21,292**
¥ 373,435	¥ 400,115	¥ 433,391	¥ 464,634	¥ 602,096	¥ 646,217	**¥ 526,702**	**$ 5,661**
343,163	—	—	—	—	—	**—**	**—**
—	296,031	305,753	326,470	306,726	272,280	**257,646**	**2,769**
—	65,462	94,093	112,668	270,757	337,968	**249,869**	**2,686**
(4,426)	5,474	(1,803)	(8,197)	(6,269)	4,890	**(9,651)**	**(104)**
3,300	7,931	11,869	12,018	8,353	17,030	**14,490**	**156**
30,674	26,810	22,140	21,586	22,055	13,150	**13,337**	**143**
724	(1,593)	1,339	89	474	899	**1,011**	**11**
139,401	126,744	126,445	132,643	171,542	282,411	**230,197**	**2,474**
¥ 234,034	¥ 273,371	¥ 306,946	¥ 331,991	¥ 430,554	¥ 363,806	**¥ 296,505**	**$3,187**
238,409	—	—	—	—	—	**—**	**—**
—	215,833	220,095	245,388	222,348	188,259	**203,339**	**2,186**
—	44,458	71,031	81,085	205,360	174,772	**109,127**	**1,173**
(12,840)	1,855	(5,057)	(11,207)	(9,644)	1,020	**(13,593)**	**(146)**
(4,851)	1,948	6,325	6,705	667	(11,451)	**(13,696)**	**(147)**
11,976	10,427	8,673	9,331	10,448	9,695	**10,557**	**113**
1,340	(1,150)	5,879	689	1,375	1,511	**771**	**8**
(7,603)	62,584	201,542	210,772	238,702	123,400	**138,448**	**1,488**
¥ 334,501	¥ 250,840	¥ 150,343	¥ 435,958	¥ 145,030	¥ 275,271	**¥ 320,024**	**$ 3,440**
(228,620)	176,914	(26,358)	(149,692)	(1,668,635)	(65,008)	**(84,057)**	**(903)**
(109,335)	(202,196)	(48,135)	(32,635)	519,001	(217,470)	**(250,398)**	**(2,691)**
269,174	269,459	145,590	223,007	(1,493,717)	240,199	**250,742**	**2,695**
¥ 708,221	¥ 639,655	¥ 596,544	¥ 600,436	¥ 763,332	¥ 668,743	**¥ 679,561**	**$ 7,304**
3,029,084	2,982,056	3,037,379	3,364,663	5,087,214	3,879,803	**3,872,596**	**41,623**
381,203	230,716	216,608	219,269	1,389,296	996,079	**874,330**	**9,397**
1,467,322	1,430,256	1,217,306	1,340,047	2,932,585	2,255,515	**2,149,317**	**23,101**
1,507,937	1,498,204	1,762,512	2,024,616	2,154,629	1,624,288	**1,723,279**	**18,522**
(0.5%)	4.2%	12.4%	11.3%	11.8%	6.8%	**8.6%**	**—**
7.9%	9.2%	10.4%	10.7%	10.5%	8.4%	**7.8%**	**—**
5.1%	5.9%	6.6%	7.0%	6.7%	5.3%	**4.8%**	**—**
1.55	1.55	1.54	1.49	1.52	1.52	**1.58**	**—**
49.8%	50.2%	58.0%	58.3%	40.8%	40.0%	**42.6%**	**—**
0.25	0.15	0.12	0.11	0.67	0.64	**0.53**	**—**
195.3%	202.7%	256.7%	226.4%	96.1%	100.2%	**108.6%**	**—**
69.9%	67.6%	60.7%	61.3%	103.4%	102.5%	**99.3%**	**—**

Management's Discussion and Analysis of Financial Condition and Business Results

• The accounts of most subsidiaries outside Japan that have December 31 fiscal year-ends have been included in consolidated financial statements ended March 31.
• Financial data disclosed herein are basically rounded.

The following discussion of our financial condition and business results should be read in reference to our consolidated financial statements prepared in accordance with Japanese Generally Accepted Accounting Principles ("Japanese GAAP") and other information included in other sections of this annual report. This discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. Actual results may differ materially from those estimated in these statements as a result of a number of factors, including, but not limited to, those described in "Major Risks of Businesses" (See Page 61).

Business Description and Acquisition of Outside Resources

Japan Tobacco Inc. ("JT") is a joint stock corporation (*kabushiki kaisha*) incorporated under the corporate law of Japan (the "Corporate Law") pursuant to the Japan Tobacco Inc. Law (the "JT Law"). JT is primarily engaged in the manufacture and sale of tobacco products in the Japanese domestic and international markets, as one of the largest producers of tobacco products in the world. Sales of cigarettes by JT and its consolidated subsidiaries (the "JT Group" or "Group") in the Japanese domestic market in the fiscal year ended March 31, 2010, amounted to 151.9 billion cigarettes [Note 1], sales in the domestic duty-free market and in the markets in China, Hong Kong and Macau, which are covered by JT's China Division, totaled 3.6 billion cigarettes and sales in other overseas markets stood at 434.9 billion cigarettes [Note 2].

(Note 1) Excluding tobacco products purchased from overseas tobacco manufacturers and sold to retail stores through its distribution subsidiary, TS Network Co., Ltd. ("TS Network")

(Note 2) Including cigars, pipe tobacco and snus, excluding private label and contract manufacturing products.

In the Japanese domestic tobacco market, JT manufactures and sells its tobacco products to retail stores all over the country in accordance with the Tobacco Business Law. This law provides that (1) JT shall be the sole manufacturer of tobacco products in Japan and (2) the maximum wholesale price of each tobacco product manufactured and sold and the retail price of each product sold in Japan, as well as any changes in these prices, shall be subject to approval by the Minister of Finance. The products are transported from its factories to its distribution bases by its subsidiary, JT Logistics Co., Ltd. and then distributed to retail stores by the subsidiary, TS Network. TS Network also acts as the wholesaler of foreign tobacco manufacturers, purchasing and selling their products to retail stores in the Japanese domestic market.

JT greatly expanded its international tobacco business through the acquisition of the non-U.S. tobacco operations of RJR Nabisco, Inc. ("RJR Nabisco") on May 12, 1999. JT paid US$5.0 billion for the non-U.S. tobacco operations of RJR Nabisco, which resulted in US$3.5 billion of goodwill. JT also acquired non-U.S. tobacco-related trademarks and intellectual properties for US$2.7 billion and other assets for US$0.1 billion. The acquisition, worth a total of US$7.8 billion (¥940 billion at the exchange rate effective at that time), was financed by a syndicated loan of US$5.0 billion (¥600 billion at the exchange rate effective at that time) and US$2.8 billion (¥340 billion at the exchange rate effective at that time) in cash. The syndicated loan was later refinanced through domestic and foreign bond issues and long-term loans from banks and insurance companies. JT repaid in full the long-term loans from banks and insurance companies, redeemed the foreign bonds by July 2004 and redeemed the domestic bonds in June 2009. As a result of this acquisition, JT obtained increased access to overseas markets, especially in Europe and Russia, and the rights in almost all countries outside the United States to internationally recognized trademarks such as Winston, Camel and Salem. Since this acquisition, JT's international tobacco business—of which JT International ("JTI") constitutes the core—has consistently maintained strong growth. Although sales and profits of the international tobacco business for the fiscal year ended March 2010 declined due to currency movements, sales and profits at the constant rates of exchange improved.

On April 18, 2007, JT completed the procedures for the acquisition of Gallaher Group Plc to make it a wholly owned subsidiary of JT. The acquisition price was about £7.5 billion (¥1,720 billion at the exchange rate effective at the time), and the total acquisition price including the assumption of net interest-bearing debt was approximately £9.44 billion (¥2,180 billion at the exchange rate effective at the time). This acquisition resulted in goodwill of US$15.1 billion. Of the total value, ¥820 billion was covered by our own funds, ¥450 billion by a loan from Mizuho Bank, Ltd., and £1.9 billion (¥450 billion at the exchange rate effective at the time) by a syndicated loan arranged by Merrill Lynch. Of the funds borrowed from Mizuho Bank, the JT Group repaid a total of ¥150 billion in May and July 2007 out of its own funds and refinanced ¥300 billion through new loans totaling ¥150 billion from other domestic banks and through the issuance of domestic bonds totaling ¥150 billion. It repaid the syndicated loan of £1.9 billion with its own cash, and funds borrowed under a new credit line established outside Japan. As for the domestic bonds, the JT Group is due to redeem ¥50 billion in July 2010, ¥40 billion in July 2011 and ¥60 billion in July 2012.

With the acquisition of Gallaher, we have further strengthened our position as the world's third largest tobacco company. In addition to our strong business foundation in Asia, we now have an increasing presence in Europe and the CIS region. We aim to maintain sustainable growth as a major tobacco company on the strength of our geographically well-balanced operations and our ample growth potential. JT's international tobacco business aims to enhance its role as the driver of the JT Group's profit growth by achieving top-line growth. We count eight brands among our list of global flagship brands ("GFB"): Winston, Camel, Mild Seven, Benson & Hedges, Silk Cut, LD, Sobranie and Glamour. We intend to actively explore opportunities for top-line growth on the strength of these GFB, which form the core of our brand portfolio.

In addition to the tobacco business, the JT Group has been actively engaged in its pharmaceutical and food businesses in order to diversify its source of future profits and cash flows.

In its pharmaceutical business, the JT Group focuses on the research and development of prescription drugs. In the Japanese domestic market, Torii Pharmaceutical Co., Ltd., in which JT acquired a stake of 53.5% for approximately ¥42 billion in December 1998, manufactures and sells prescription drugs through its extensive marketing network. In the overseas market, JT derives revenue principally from royalties on the licensing of its successful anti-HIV drug.

In its food business, the JT Group principally manufactures and sells beverages, processed foods and seasonings in the Japanese domestic market. JT's presence in the beverage market was substantially expanded through the acquisition of a majority stake in Unimat Corporation, a nationwide operator of soft drink vending machines that was later renamed Japan Beverage Inc., for approximately ¥29 billion in a two-stage deal implemented in April and September 1998. In addition, JT acquired the food business of Asahi Kasei Corporation for approximately ¥24 billion in July 1999. In January 2008, the JT Group made Katokichi Co., Ltd. a subsidiary by acquiring additional shares of the company for approximately ¥102 billion, increasing its equity stake in Katokichi from 5% to approximately 94%. Following the acquisition of all voting rights of Katokichi on April 18, 2008, the JT Group channeled its processed food operations, including frozen food operations and seasonings operations, through the Katokichi Group beginning on July 1, 2008. Through this realignment, the Katokichi Group will consolidate its foundation as a unique food manufacturer on the strength of its processed food business—including the frozen food business, which has the eminent scale in Japanese market—and its superior technology for the production of seasonings. Katokichi changed its corporate name to TableMark Co., Ltd. in January 2010.

Under the JT Law, JT must obtain approval from the Minister of Finance with regard to certain matters, such as (1) the issuance of new shares (as well as subscription rights for new shares and bonds with subscription rights for new shares) and (2) resolutions adopted at shareholder meetings for any amendments to the Articles of Incorporation and appropriation of retained earnings. Pursuant to the JT Law, the Japanese government is required to hold one-half or more of the JT shares that were issued upon the company's establishment in 1985, as adjusted for any subsequent stock split or consolidation of shares. The amended JT Law allows JT to issue new shares to the extent that the number of shares held by the government remains at more than one-third of the outstanding shares.

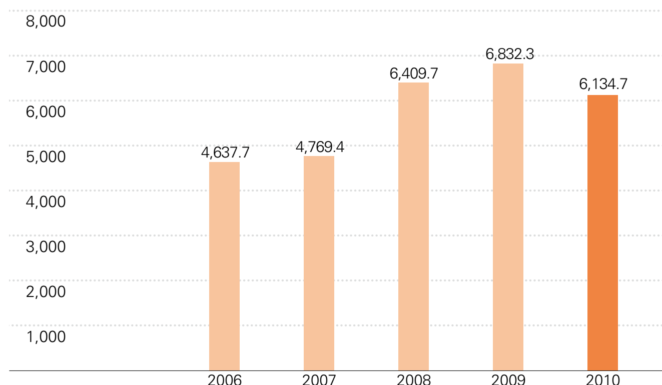
Overview

Our net sales (Note 3) totaled ¥6,134.7 billion for the year ended on March 31, 2010 compared with ¥6,832.3 billion for the year ended March 31, 2009. The Japanese domestic and international tobacco businesses accounted for 49.6% and 42.9%, respectively, of our net sales in the year ended March 31, 2010, compared with 46.8% and 45.6% in the year ended March 31, 2009. Sales for our international tobacco business have become an important component of our total net sales.

Our operating income totaled ¥296.5 billion for the year ended March 31, 2010, compared with ¥363.8 billion for the year ended March 31, 2009. Up to the year ended March 31, 2008 our food business has generated operating income since the year ended March 31, 2005, it posted an operating loss in the year ended March 31, 2009 and in the year ended March 31, 2010. Our pharmaceutical business has posted operating losses every year since the year ended March 31, 1998, when we started to disclose segment-by segment information, with the exception of the year ended March 31, 2005 and the year ended March 31, 2009. As a result, we derive almost all of our operating income from our tobacco business.

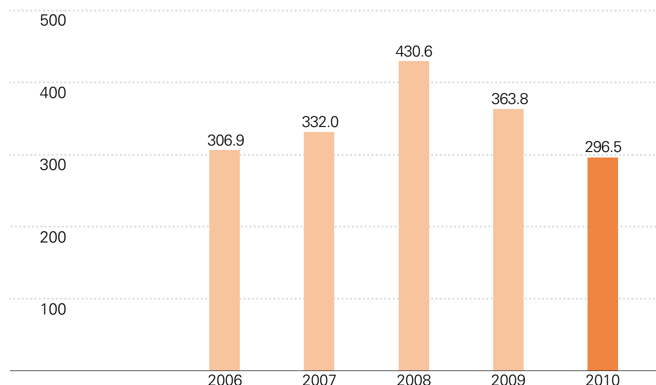
(Note 3) Including tobacco excise taxes.

Net Sales(Note 3)
(Billions of yen)



(Note 3) Including tobacco excise taxes.

Operating Income
(Billions of yen)



Overview of the Japanese Domestic and International Tobacco Businesses

Overall tobacco demand in the Japanese domestic market has been declining due to such factors as the aging of Japanese society, growing awareness about the health risks associated with smoking and the tightening of smoking-related regulations, and we expect this trend to continue. As for overseas markets, too, demand may decline depending on economic conditions and regional factors, although the situation will vary from region to region.

The total tobacco sales of the Japanese domestic tobacco business in the year ended March 31, 2010 fell 5.0% from the previous year to 151.9 billion cigarettes(Note 4) due to the impact of the recession as well as the abovementioned structural factors. Meanwhile, the total tobacco sales of the international tobacco business in the year ended March 31, 2010 declined 2.5% from the previous year to 434.9 billion cigarettes(Note 5), as an increase in sales in Turkey, the UK, Russia and Italy was offset by a decrease in Iran, Ukraine and the Philippines. The table below shows the total tobacco sales of the Japanese domestic and international tobacco businesses for the past two fiscal years.

Year ended March 31	2009	**2010**
Japanese domestic tobacco business (Note 4)	159.9	**151.9**
International tobacco business (Note 5)	445.9	**434.9**
Total	605.8	**586.8**

(Billions of Cigarettes)

(Note 4) Excluding tobacco products purchased from overseas tobacco manufacturers and sold to retail stores through its distribution subsidiary, TS Network Co., Ltd. ("TS Network"), sales volume of domestic duty-free market and in the markets in China, Hong Kong and Macau, which are covered by JT's China Division.

(Note 5) Including cigars, pipe tobacco and snus, excluding private label and contract manufacturing products.

The JT Group regards the Japanese domestic tobacco business as its core source of profits. The business environment is becoming increasingly difficult due to a decline in overall demand in the Japanese domestic market and intensifying competition. To secure a competitive edge, JT will strive to build a strong brand portfolio and also make continuous efforts to enhance added value of its products and improve product quality so as to maximize customer satisfaction and establish a highly cost efficient business framework. In the year ended March 31, 2010, JT strived to enhance the brand portfolio by introducing new products as well as by developing the existing brands, particularly the Mild Seven family and the Seven Stars family, which are our core brands. Specifically, JT launched Mild Seven 100's Box, Mild Seven Lights 100's Box, Seven Stars Black Charcoal Menthol Box, Pianissimo Icene Menthol One and Mild Seven Impact One Menthol Box nationwide and launched Camel Menthol Mini in limited areas. And Seven Stars Black Impact Box was released nationwide in April 2010, which was followed by the nationwide release in June of Winston Lights 6 Box, Winston Extra 3 Box, and Winston Ultra One 100's Box. JT integrated the Icene and Lucia brands into the Pianissimo brand and repackaged 15 major products of the Mild Seven family and renewed all of the 9 brands of the Caster family in April 2010, thereby enhancing the brand of the Pianissimo, Mild Seven and Caster families with a view to achieving sustainable growth. In addition, in May 2010, JT released in limited regions Zerostyle Mint an all-new style of smokeless tobacco which does not require a flame. JT is committed to increasing customer satisfaction by meeting a diverse range of consumer needs including the development of many new tobacco products not limited to cigarettes as well as improving product taste and flavor so that people can enjoy their favorite tobacco products more. Although the Japanese domestic tobacco business suffered a decline in cigarette sales volume, we kept our market share almost unchanged from the previous year through aggressive sales promotion and product launches. Meanwhile, JT closed two domestic tobacco factories at the end of March 2010 as part of our efforts to build an optimum operating structure.

The international tobacco business is actively exploring opportunities for top-line growth by concentrating business resources on GFBs and improving margins through appropriate pricing, so that it can continue to act as the JT Group's profit growth engine. In the year ended March 31, 2010, the total sales volume and the GFB sales volume declined due to such factors as an unstable business environment in Iran, a change in the operating model in the Philippines from the licensing arrangement to contract manufacturing. Despite the impact of those specific events, both the total sales volume and the GFB sales volume grew from the previous year. In the meantime, although the trend of down-trading accelerated in many key markets in the year ended March 31, 2010 due to the recession and sharp tobacco tax increases, our international tobacco business achieved market share growth in almost all key markets, including Russia, France, Italy, Spain, the UK and Turkey because of its well-balanced brand portfolio, which is strong in the sub-premium and mid-price segments, and its efforts to enhance brand equity and strengthen sales promotion activities. We also believe that our continued active investments in enhancing brand equity in each market made significant contributions to the increases in many market shares.

Market shares in the Japanese domestic and overseas tobacco markets may fluctuate in the short term due to temporary factors, such as the launch of new products by the JT Group and other tobacco manufacturers, and special sales promotion activities. Local market shares may also be affected by a number of other factors, including competition, pricing strategies, changes in consumer preferences, brand recognition and regional economic conditions.

Such factors may lead to a decrease in the JT Group's market share. In addition, there is a risk that the measures adopted by the JT Group to counter the decrease in market share may entail additional costs, reducing its profits. The profitability of the Japanese domestic and international tobacco businesses may fluctuate due to various factors, including the following:

- Health concerns relating to the use of tobacco product;
- Legal or regulatory developments and changes, including, without limitation, tax increases and restrictions on the sale, marketing and usage of tobacco products, and governmental investigations

and privately imposed smoking restriction;
- Litigation in Japan and elsewhere;
- Our ability to successfully expand internationally and make investments outside of Japan;
- Competition and changing consumer preferences;
- The impact of any acquisitions;
- Local and global economic conditions; and
- Fluctuations in foreign exchange rates and the cost of raw materials.

Please refer to "Major Risks of Businesses" (Page 61) for the details.

Impact of Exchange Rate Fluctuations

The JT Group has become more prone than before to exchange rate fluctuations as a result of an expansion of its international tobacco business. While JT itself makes consolidated financial statements in terms of the Japanese yen, overseas subsidiaries and affiliates of the JT Group do so in terms of foreign currencies. Consequently, the business results, assets and liabilities of the overseas subsidiaries and affiliates are converted into yen terms when they are reflected in JT's consolidated financial statements. Therefore, JT's financial statements are affected by the fluctuations of the foreign currencies used by the overseas subsidiaries and affiliates against the Japanese yen. JT International Holding B.V. (JT's consolidated subsidiary in the Netherlands; hereinafter referred to as "JTIH"), which is responsible for consolidating the financial results of the JT Group's international tobacco business, uses the U.S. dollar for its financial accounting. However, JTIH does business through consolidated subsidiaries and affiliates around the world, some of which use foreign currencies other than the U.S. dollar. This means that the JT Group's consolidated results are affected not only by exchange rate fluctuations between the Japanese yen and the U.S. dollar but also by those between the U.S. dollar and other foreign currencies used by the consolidated subsidiaries and affiliates for their financial accounting. However, the impact of such exchange rate fluctuations does not significantly affect the business fundamentals.

A substantial portion of the JT Group's international transactions is conducted in currencies other than the Japanese yen, and that portion is affected by exchange rate fluctuations. Although JT partially hedges its exposure to foreign exchange risks related to transactions conducted in foreign currencies, the JT Group's exchange risks cannot be fully offset. Therefore, the possibility cannot be ruled out that the JT Group's business performance will be negatively affected by exchange rate fluctuations.

Consolidated Business Results and Results by Industry Segment

Consolidated Income Statement

		Millions of yen		Millions of U.S. dollars
For years ended March 31	2008	2009	**2010**	**2010**
Net sales	¥6,409,727	¥6,832,307	**¥6,134,695**	**$65,936**
Cost of sales	5,228,926	5,554,399	**5,022,637**	**53,984**
Gross profit	1,180,801	1,277,908	**1,112,058**	**11,952**
Selling, general and administrative expenses	750,247	914,102	**815,553**	**8,765**
Operating income	430,554	363,806	**296,505**	**3,187**
Other income (expenses), net	(57,940)	(101,662)	**(20,450)**	**(220)**
Income before income taxes and minority interests	372,614	262,144	**276,055**	**2,967**
Income taxes	128,379	134,973	**131,304**	**1,411**
Income before minority interests	244,235	127,171	**144,751**	**1,556**
Minority interests	5,533	3,771	**6,303**	**68**
Net income	¥ 238,702	¥ 123,400	**¥ 138,448**	**$ 1,488**
Net income before goodwill amortization	¥ 242,585	¥ 228,912	**¥ 235,875**	**$ 2,535**

Results by Industry Segment

For years ended March 31	2008	2009	2010	2010
			Millions of yen	Millions of U.S. dollars
Net sales (Note 6)	¥6,409,727	¥6,832,307	**¥6,134,695**	**$65,936**
Tobacco				
Japanese domestic	3,362,398	3,200,494	**3,042,836**	**32,705**
International	2,639,969	3,118,319	**2,633,636**	**28,306**
Pharmaceutical	49,064	56,758	**44,069**	**474**
Food	336,420	435,966	**394,653**	**4,242**
Others	21,876	20,770	**19,501**	**209**

(Note 6) Including tobacco tax

For years ended March 31	2008	2009	2010	2010
			Millions of yen	Millions of U.S. dollars
Adjusted net sales excluding excise taxes (Note 7)	—	¥2,243,147	**¥1,980,970**	**$21,292**
Tobacco				
Japanese domestic	—	648,830	**615,991**	**6,621**
International	—	1,080,821	**906,756**	**9,746**
Pharmaceutical	—	56,758	**44,069**	**474**
Food	—	435,966	**394,653**	**4,242**
Others	—	20,770	**19,501**	**209**

(Note 7) Japanese domestic tobacco; excluding excise tax and revenue from the imported tobacco, domestic duty free, the China Division, and other miscellaneous. International tobacco; excluding excise taxes and revenue from distribution, private label, contract manufacturing and other peripheral business.

For years ended March 31	2008	2009	2010	2010
			Millions of yen	Millions of U.S. dollars
Operating income	¥430,554	¥363,806	**¥296,505**	**$3,187**
Tobacco				
Japanese domestic	222,348	188,259	**203,339**	**2,186**
International	205,360	174,772	**109,127**	**1,173**
Pharmaceutical	(9,644)	1,020	**(13,593)**	**(146)**
Food	667	(11,451)	**(13,696)**	**(147)**
Others	10,448	9,695	**10,557**	**113**
Elimination/Corporate	1,375	1,511	**771**	**8**

For years ended March 31	2008	2009	2010	2010
			Millions of yen	Millions of U.S. dollars
EBITDA	¥602,096	¥646,217	**¥526,702**	**$5,661**
Tobacco				
Japanese domestic	306,726	272,280	**257,646**	**2,769**
International	270,757	337,968	**249,869**	**2,686**
Pharmaceutical	(6,269)	4,890	**(9,651)**	**(104)**
Food	8,353	17,030	**14,490**	**156**
Others	22,055	13,150	**13,337**	**143**
Elimination/Corporate	474	899	**1,011**	**11**

Year Ended March 31, 2010 Compared with Year Ended March 31, 2009

Net Sales

Net sales for the year ended March 31, 2010 decreased by ¥697.6 billion, or 10.2% from the previous year to ¥6,134.7 billion. The net sales amounts indicated below represent the amounts excluding inter-segment transactions.

• Japanese Domestic Tobacco Business

Net sales in our Japanese domestic tobacco business are comprised of domestic sales of tobacco products manufactured by the JT Group within and outside Japan (including domestic duty-free sales and sales of imported tobaccos) (Note 8), domestic sales of products manufactured by foreign tobacco manufacturers and distributed by our subsidiaries as wholesalers and sales in the China, Hong Kong and Macau markets, which are covered by JT's China Division. Net sales for our Japanese domestic tobacco business totaled ¥3,042.8 billion in the year ended March 31, 2010, a decrease of ¥157.7 billion, or 4.9%, from the previous year. Adjusted net sales excluding tax declined by ¥32.8 billion, or 5.1%, from the previous year to ¥616.0 billion. The sales volume of JT's tobacco products in Japan decreased by 8.1 billion cigarettes, or 5.0%, from the previous year to 151.9 billion cigarettes (Note 9).

The sales volume declined due to the continued decrease in total cigarette demand caused by factors such as: the aging Japanese population, growing consciousness of health risks associated with smoking, tightened smoking regulations and the economic recession. Our market share came to 64.9%, almost unchanged compared with the previous year. Net sales excluding excise tax per 1,000 cigarettes remained almost unchanged from the previous year for ¥4,056.

(Note 8) The margin on the sales of imported tobacco products for the Japanese domestic tobacco business is substantially smaller than on the margin on the sales of JT products, as the JT Group's involvement is limited to the distribution operation.

(Note 9) In addition, 3.6 billion cigarettes sold in domestic duty-free markets and in the China, Hong Kong and Macau markets, which are covered by JT's China Division accounted for domestic sales volume.

• International Tobacco Business

Net sales for our international tobacco business totaled ¥2,633.6 billion, a decline of ¥484.7 billion, or 15.5%, from the previous year, while adjusted net sales excluding taxes decreased by ¥174.1 billion, or 16.1%, to ¥906.8 billion. The sales volume of our international tobacco business dropped by 11.0 billion cigarettes, or 2.5%, to 434.9 billion cigarettes, as robust sales growth of Winston in Italy, France and Turkey and of Camel in Italy and Ukraine were offset by the negative impact of an unstable business environment in Iran and a shift in the operating model in the Philippines from the licensing arrangement to contract manufacturing. The GFB sales volume dropped 2.1 billion cigarettes, or 0.9%, from the previous year to 243.4 billion cigarettes. Sales denominated in local currencies are first converted into the U.S. dollar terms and then into yen terms based on the average exchange rate for the relevant accounting period. Despite the decline in the sales volume, U.S. dollar-based net sales increased at constant rates of exchange as a result of favorable pricing in many markets. However, yen-based net sales declined as a result of the depreciation of the local currencies against the U.S. dollar and the dollar's depreciation against the yen.

The average exchange rates of the major local currencies converted into dollar terms were: $1=31.77 ruble, $1=0.65 pound, $1=0.73 euro for the year ended March 31, 2010, compared with $1=24.84 ruble, $1=0.53 pound and $1=0.68 euro for the year ended March 31, 2009. The 12-month average exchange rate between the Japanese yen and the U.S. dollar that was used for the conversion of sales for the year ended March 31, 2010 was ¥93.65 to $1.00, compared with ¥103.48 to $1.00 for the year ended March 31, 2009.

• Pharmaceutical Business

Net sales for our pharmaceutical business dropped by ¥12.7 billion, or 22.4%, from the previous year to ¥44.1 billion in the year ended March 31, 2010. While net sales for Torii Pharmaceutical increased, the consolidated net sales declined after the previous year's sales were boosted by the receipt of an upfront fee for the licensing of anti-osteoporosis oral compound JTT-305 to Merck of the United States in September 2008 and a milestone revenue associated with progress in the development of the JTT-705 compound for the treatment of dyslipidemia, which was licensed to Roche in October 2004.

• Food business

Net sales for our food business declined by ¥41.3 billion, or 9.5%, from the previous year to ¥394.7 billion. Sales of beverage products declined by ¥1.2 billion, or 0.6%, to ¥186.1 billion. Sales of processed foods fell by ¥40.1 billion, or 16.1%, from the previous year to ¥208.5 billion, as a result of the withdrawal from the chilled processed food business and the exclusion of some subsidiaries from the consolidated results due to the change in ownership.

Cost of Sales (Note 10)

Cost of sales in the year ended March 31, 2010 decreased by ¥531.8 billion, or 9.6%, from the previous year to ¥5,022.6 billion. Despite the increase of the production cost due to the price hike of foreign leaf tobacco, the decrease in the sales volume of the Japanese domestic tobacco business and the adverse currency movements in the international tobacco business contributed to the decrease in the cost of sales.

(Note 10) The cost of sales includes tobacco excise taxes

Selling, General and Administrative Expenses

Selling, general and administrative expenses in the year ended March 31, 2010 decreased by ¥98.5 billion, or 10.8%, from the previous year to ¥815.6 billion. This was attributable to the effects of exchange rate fluctuations on the conversion of the selling, general and administrative expenses of the international tobacco business into yen terms and the completion of the amortization of some trademark rights in the Japanese domestic tobacco business.

EBITDA (Note 11) and Operating Income

As a result of the above factors, EBITDA in the year ended March 31, 2010 declined by ¥119.5 billion, or 18.5%, from the previous year to ¥526.7 billion, while operating income dropped by ¥67.3 billion, or 18.5%, to ¥296.5 billion. EBITDA and operating income by business segment were as follows:

(Note 11) In the mid-term management plan "JT-11," we use EBITDA for the profit index that committed to our stakeholders and for the key performance indicators. EBITDA as defined by the JT Group is operating income plus the amortization cost (the cost of the depreciation of tangible fixed assets and amortization of intangible fixed assets, long-term prepaid expenses and goodwill). The cost of the amortization of some tangible assets is included in the cost of sales while that of other tangible assets is included in the general and administrative expenses.

• Japanese Domestic Tobacco Business

EBITDA for our Japanese domestic tobacco business in the year ended March 31, 2010 decreased by ¥14.6 billion, or 5.4%, from the previous year to ¥257.6 billion due to a decline in net sales caused by a fall in the sales volume. Operating income increased by ¥15.1 billion, or 8.0%, to ¥203.3 billion. The reduced net sales was offset by a drop in the depreciation cost following the completion of the amortization of some trademark rights.

• International Tobacco Business

EBITDA for our international tobacco business in the year ended March 31, 2010 declined by ¥88.1 billion, or 26.1%, from the previous year to ¥249.9 billion and operating income dropped by ¥65.6 billion, or 37.6%, to ¥109.1 billion. This was due to a net sales decline attributable to the depreciation of the local currencies of major markets against the U.S. dollar, the dollar's depreciation against the Japanese yen and a rise in the manufacturing cost due to increased leaf tobacco prices.

• Pharmaceutical Business

Our pharmaceutical business recorded an negative EBITDA of ¥9.7 billion in the year ended March 31, 2010, representing a deterioration of ¥14.5 billion from the previous year, and an operating loss of ¥13.6 billion, a deterioration of ¥14.6 billion from the previous year. Although net sales and profits for Torii Pharmaceutical increased, the consolidated EBITDA and operating loss deteriorated after the previous year's results that were boosted by the receipt of an upfront fee for the licensing of anti-osteoporosis oral compound JTT-305 to Merck in September 2008 and a milestone revenue associated with progress in the development of the JTT-705 compound for the treatment of dyslipidemia, which was licensed to Roche in October 2004.

• Food business

EBITDA for our food business in the year ended March 31, 2010 declined by ¥2.5 billion, or 14.9%, from the previous year to ¥14.5 billion as a result of a reduced net sales and one-time factors such as losses in the fishery business despite cost reduction.

It posted an operating loss of ¥13.7 billion, a deterioration of ¥2.2 billion from the previous year. This was due to the impact of the amortization of goodwill related to TableMark Co. Ltd.'s acquisition of additional shares in Green Foods Co., Ltd., a subsidiary, in June 2009, as well as the reduced EBITDA.

• Others

EBITDA for our other businesses in the year ended March 31, 2010 increased by ¥0.2 billion, or 1.4%, from the previous year to ¥13.3 billion, while operating income increased by ¥0.9 billion, or 8.9%, to ¥10.6 billion.

Other Expenses/Income (on a net basis)

We booked other expenses totaling ¥20.5 billion (on a net basis) in the year ended March 31, 2010, a decrease of ¥81.2 billion from the previous year. This was attributable to a decline in interest payments due to reduced borrowings, redemption of bonds and lower interest rates, a drop in exchange losses, the elimination of some expenses incurred in the previous year, including: expenses related to a change in the operating model in the Philippines; expenses associated with the demolition of company housing; and the cost of introducing vending machines with the adult identification function, and a gain from the reversal of liability on a fine levied under the UK competition law, which outweighed a decrease in the profits from the sale of fixed assets.

Income before Income Taxes and Minority Interests

As a result of the above factors, income before income taxes and minority interests in the year ended March 31, 2010 increased by ¥13.9 billion, or 5.3%, from the previous year to ¥276.1 billion mainly due to changes in the business.

Income Taxes

Income taxes in the year ended March 31, 2010 declined by ¥3.7 billion, or 2.7%, from the previous year to ¥131.3 billion. The actual effective tax rate in the year ended March 31, 2010 decreased by 3.9 points to 47.6%.

Income before Minority Interests

Income before minority interests in the year ended March 31, 2010 increased by ¥17.6 billion, or 13.8%, from the previous year to ¥144.8 billion. Minority interests in the year ended March 31, 2010 increased by ¥2.5 billion, or 67.1%, from the previous year to ¥6.3 billion mainly due to changes in the business.

Net Income

As a result of the above factors, net income in the year ended March 31, 2010 increased by ¥15.0 billion, or 12.2%, from the previous year to ¥138.4 billion.

Net Profit before Goodwill Amortization

Since April 2008, we have booked the cost of goodwill amortization of all segments in accordance with the "standard accounting treatments to the accounting of overseas subsidiaries in the consolidated financial statements" (a report by the Accounting Standards Board of Japan). In the year ended March 31, 2010, the cost of goodwill amortization [Note 12] came to ¥97.4 billion, and net income before goodwill amortization increased by ¥7.0 billion, or 3.0%, to ¥235.9 billion.

(Note 12) The cost of goodwill amortization is included in the selling, general and administrative expenses.

Year Ended March 31, 2009 Compared with Year Ended March 31, 2008

Net Sales

Net sales [Note 13] for the year ended March 31, 2009 increased by ¥422.6 billion, or 6.6% from the previous year to ¥6,832.3 billion. The net sales amounts indicated below represent the amounts excluding inter-segment transactions.

(Note 13) Including tobacco excise taxes

• Japanese Domestic Tobacco Business

Net sales in our Japanese domestic tobacco business are comprised of domestic sales (including duty-free sales) of tobacco products manufactured by the JT Group in and outside Japan, domestic sales of products manufactured by foreign tobacco manufacturers and distributed by our subsidiaries as wholesalers and sales in the China, Hong Kong and Macau markets, which are covered by JT's China Division. Net sales for our Japanese domestic tobacco business totaled ¥3,200.5 billion in the year ended March 31, 2009, a decrease of ¥161.9 billion, or 4.8%, from the previous year. The sales volume of JT's tobacco products in Japan decreased by 7.8 billion cigarettes, or 4.7%, from the previous year to 159.9 billion cigarettes [Note 14].

The sales volume declined due to the continued decrease in total cigarette demand caused by factors such as: the aging Japanese population, growing consciousness of health risks associated with smoking, tightened smoking regulations, and revision of retail prices based on a hike in the tobacco excise tax implemented in July 2006.

Our market share increased by 0.2 percentage points compared with the previous year, to 65.1%, marking the second consecutive year of market share increase. Net sales excluding excise tax per 1,000 cigarettes remained unchanged from the previous year at ¥4,057.

(Note 14) In addition, 3.6 billion cigarettes sold in domestic duty-free markets and in the China, Hong Kong and Macau markets, which are covered by JT's China Division accounted for domestic sales volume.

• International Tobacco Business

Net sales for our international tobacco business totaled ¥3,118.3 billion, an increase of ¥478.4 billion, or 18.1%, from the previous year.

The sales volume of our international tobacco business increased by 66.7 billion cigarettes, or 17.3%, to 452.3 billion cigarettes, thanks mainly to Winston's sales growth in Russia, Turkey, Ukraine and Spain; Camel' sales growth in Italy, Russia and Spain; and Mild Seven's sales growth in Korea, Taiwan, Russia and Malaysia. The sales volume of GFB grew 42.3 billion cigarettes, or 20.8%, to 245.5 billion cigarettes. Sales denominated in foreign currencies are first converted into dollar terms and then into yen terms based on the average exchange rate for the relevant accounting period. Sales in dollar terms increased due to an expansion in the sales volume of GFB as well as the inclusion of the full-year results of Gallaher. However, sales in yen terms increased despite negative effects from the yen's appreciation against the dollar.

The 12-month average exchange rate between the Japanese yen and the U.S. dollar that was used for the conversion of sales for the year ended March 31, 2009 was ¥103.48 to $1.00, compared with ¥117.85 to $1.00 for the year ended March 31, 2008.

• Pharmaceutical Business

Net sales for our pharmaceutical business increased by ¥7.7 billion, or 15.7%, from the previous year to ¥56.8 billion in the year ended March 31, 2009. A decrease in net sales for Torii Pharmaceutical was more than offset by an upfront payment for the licensing of anti-osteoporosis oral compound JTT-305 to Merck in September 2008 and a milestone revenue associated with progress in the development of the JTT-705 compound for the treatment of dyslipidemia, which was licensed to Roche in October 2004.

• Food business

Net sales for our food business increased by ¥99.5 billion, or 29.6%, from the previous year to ¥436.0 billion. Sales of beverage products declined by ¥7.6 billion, or 3.9%, to ¥187.4 billion. Sales of processed foods increased by ¥107.1 billion, or 75.7%, from the previous year to ¥248.6 billion, as the consolidation of the Katokichi Group outweighed the impact of the frozen food products contamination, and negative effects of unfavorable weather conditions and increased competition in the beverages business as well as a slump in general consumption caused by the recent severe economic downturn.

Cost of Sales [Note 15]

Cost of sales in the year ended March 31, 2009 increased by ¥325.5 billion, or 6.2%, from the previous year to ¥5,554.4 billion, mainly as a result of the inclusion of the full-year results of Gallaher and the Katokichi Group. This and other favorable factors were partially offset by a decrease in the sales volume of the Japanese domestic tobacco business.

(Note 15) The cost of sales includes tobacco excise taxes.

Selling, General and Administrative Expenses

Selling, general and administrative expenses in the year ended March 31, 2009 increased by ¥163.9 billion, or 21.8%, from the previous year to ¥914.1 billion. This was attributable to the inclusion of the cost of the goodwill amortization related to the international tobacco business following a revision of the accounting standards and the inclusion of the full-year cost of the amortization of the goodwill of the Katokichi Group as well as the inclusion of the full-year results of Gallaher and the Katokichi Group.

EBITDA (Note 16) and Operating Income

As a result of the above factors, EBITDA in the year ended March 31, 2009 increased by ¥44.1 billion, or 7.3%, from the previous year to ¥646.2 billion. However, operating income declined by ¥66.7 billion, or 15.5%, from the previous year to ¥363.8 billion, mainly as a result of the start of goodwill amortization following a revision of accounting standards applied to the international tobacco business. Operating income by business segment was as follows:

(Note 16) In the mid-term management plan "JT-11," we use EBITDA for the key performance indicators. EBITDA as defined by the JT Group is operating income plus the amortization cost (the cost of the depreciation of tangible fixed assets and amortization of intangible fixed assets, long term prepaid expenses and goodwill). The cost of the amortization of some tangible assets is included in the cost of sales while that of other tangible assets is included in the general and administrative expenses.

• Japanese Domestic Tobacco Business

EBITDA for our Japanese domestic tobacco business in the year ended March 31, 2009 declined by ¥34.4 billion, or 11.2%, from the previous year, to ¥272.3 billion, while operating income decreased by ¥34.1 billion, or 15.3%, from the previous year to ¥188.3 billion. The decrease was attributable mainly to a decline in the sales volume and an increase in sales promotion expenses.

• International Tobacco Business

EBITDA for our international tobacco business in the year ended March 31, 2009 grew by ¥67.2 billion, or 24.8%, to ¥338.0 billion due to an increase in the sales volume, mainly of GFBs, and the inclusion of the full-year results of Gallaher. However, operating income decreased by ¥30.6 billion, or 14.9%, from the previous year to ¥174.8 billion, mainly due to the start of the goodwill amortization following the revision of accounting standards. A rise in the exchange rate of the Japanese yen against the U.S. dollar contributed to the decrease in operating income in yen terms.

• Pharmaceutical Business

Our pharmaceutical business recorded an EBITDA of ¥4.9 billion, an improvement of ¥11.2 billion from the previous year, in the year ended March 31, 2009, while it posted an operating income of ¥1.0 billion, representing an improvement of ¥10.7 billion in the operating balance from the previous year.

A decrease in net sales for Torii Pharmaceutical was more than offset by an upfront payment for the licensing of anti-osteoporosis oral compound JTT-305 to Merck in September 2008 and a milestone revenue associated with progress in the development of the JTT-705 compound for the treatment of dyslipidemia, which was licensed to Roche in October 2004.

• Food business

EBITDA for our food business increased by ¥8.7 billion, or 103.9%, from the previous year, to 17.0 billion as a result of an increase in the depreciation cost due to a revision of the leasing accounting standards. However, the food business posted an operating loss of ¥11.5 billion in the year ended March 31, 2009, representing a deterioration of ¥12.1 billion in the operating balance compared with the previous year. This was attributable to a rise in general expenses, an increase in raw materials costs and the inclusion of the full-year cost of the amortization of the goodwill of the Katokichi Group following the consolidation of the group.

• Others

EBITDA for our other businesses in the year ended March 31, 2009 declined by ¥8.9 billion, or 40.4%, from the previous year to ¥13.1 billion, while operating income decreased by ¥0.8 billion or 7.2% from the previous year to ¥9.7 billion.

Other Expenses/Income (on a net basis)

We booked other expenses totaling ¥101.7 billion (on a net basis) in the year ended March 31, 2009, an increase of ¥43.7 billion from the previous year. This reflected the inclusion of full-year interest payments related to additional debts and corporate bonds associated with the acquisition of Gallaher, a decline in profits from the sale of fixed assets, losses related to the demolition of company-owned residences for employees, expenses incurred by the international tobacco business in relation to a revision of the business model in the Philippines market and the cost of reorganizing the Katokichi Group's business operations.

Income before Income Taxes and Minority Interests

As a result of the above factors, income before income taxes and minority interests in the year ended March 31, 2009 decreased by ¥110.5 billion, or 29.6%, from the previous year to ¥262.1 billion.

Income Taxes

Income taxes in the year ended March 31, 2009 increased by ¥6.6 billion, or 5.1%, from the previous year to ¥135.0 billion. The actual effective tax rate in the year ended March 31, 2009 increased by 17.03 points to 51.49%, mainly due to the impact of the cost of the goodwill amortization that was not covered by the deferred tax accounting.

Income before Minority Interests

Income before minority interests in the year ended March 31, 2009 declined by ¥117.1 billion, or 47.9%, from the previous year to ¥127.2 billion. Minority interests in the year ended March 31, 2009 decreased by ¥1.8 billion, or 31.8%, from the previous year to ¥3.8 billion.

Net Income

As a result of the above factors, net income in the year ended March 31, 2009 decreased by ¥115.3 billion, or 48.3%, from the previous year to ¥123.4 billion.

Net Income before Goodwill Amortization

Since April 2008, we have booked the cost of goodwill amortization in accordance with the "standard accounting treatments to the accounting of overseas subsidiaries in the consolidated financial statements" (a report by the Accounting Standards Board of Japan). In the year ended March 31, 2009, the cost of goodwill amortization (Note 17) came to ¥105.5 billion, and net income before goodwill amortization totaled ¥228.9 billion.

(Note 17) The cost of goodwill amortization is included in the selling, general and administrative expenses.

Results by Geographic Segment

We divide our operations into three geographic segments based on the business territories of the JT Group's main business entities: Japan, Western Europe (including Switzerland, France and Germany) and other regions. Our "other regions" segment comprises primarily Asia (excluding Japan but including China, Hong Kong and Macau), Canada, Russia and the other Commonwealth of Independent States nations, the Middle East and Africa.

Table Results by Geographic Segment

For years ended March 31	Millions of yen 2008	2009	2010	Millions of U.S. dollars 2010
Net sales (Note 18)	¥6,409,727	¥6,832,307	**¥6,134,695**	**$65,936**
Japan	3,711,763	3,672,004	**3,482,548**	**37,430**
Western Europe	1,678,770	2,038,028	**1,677,755**	**18,033**
Other	1,019,194	1,122,275	**974,392**	**10,473**

(Note 18) including tobacco excise taxes

For years ended March 31	Millions of yen 2008	2009	2010	Millions of U.S. dollars 2010
Operating income (loss)	¥430,554	¥363,806	**¥296,505**	**$3,187**
Japan	222,340	186,439	**184,553**	**1,983**
Western Europe	55,936	(24,188)	**(40,289)**	**(433)**
Other	151,398	199,633	**150,496**	**1,618**
Elimination/Corporate	880	1,922	**1,745**	**19**

Japan: Net sales in Japan in the year ended March 31, 2010 decreased by ¥189.5 billion, or 5.2%, from the previous year to ¥3,482.5 billion, due to a decline in the sales volume of the Japanese domestic tobacco business. Operating income in the year ended March 31, 2010 declined by ¥1.9 billion, or 1.0%, from the previous year to ¥184.6 billion. This was due to the reduced net sales, which was partially offset by a drop in the depreciation cost following the completion of the amortization of some trademark rights.

Net sales in Japan in the year ended March 31, 2009 declined by ¥39.8 billion, or 1.1%, from the previous year to ¥3,672.0 billion as a result of a decrease in the sales volume for the Japanese domestic tobacco business. Operating income in the year ended March 31, 2009 dropped by ¥35.9 billion, or 16.1%, from the previous year to ¥186.4 billion because of the reduced sales volume for the Japanese domestic tobacco business and the inclusion of the full-year cost of the amortization of the goodwill of the Katokichi Group.

Western Europe: Net sales in Western Europe in the year ended March 31, 2010 decreased by ¥360.3 billion, or 17.7%, from the previous year to ¥1,677.8 billion, due to the negative forex impact of depreciation of local currency in the main markets like the UK in the international tobacco business. Operating losses in the year ended March 31, 2010 totaled ¥40.2 billion, a deterioration of ¥40.3 billion from the previous year, because of the negative forex impact as well as the cost of goodwill amortization.

Net sales in Western Europe in the year ended March 31, 2009 grew by ¥359.3 billion, or 21.4% from the previous year to ¥2,038.0 billion as a result of the inclusion of the full-year results of Gallaher, which has a large market share in the United Kingdom and Ireland, where cigarette prices are high. Operating losses in the year ended March 31, 2009 totaled ¥24.1 billion, a deterioration of ¥80.1 billion from the previous year, because of the cost of goodwill amortization.

Other Regions: Net sales in other regions in the year ended March 31, 2010 declined by ¥147.9 billion, or 13.2%, from the previous year to ¥974.4 billion. This was due to the negative forex impact of depreciation of local currency in the main markets like Russia in the international tobacco business. Operating income in the year ended March 31, 2010 decreased by ¥49.1 billion, or 24.6%, from the previous year to ¥150.5 billion.

Net sales in other regions in the year ended March 31, 2009 grew by ¥103.1 billion, or 10.1%, from the previous year to ¥1,122.3 billion as a result of an increase in international sales by JT International, particularly in countries such as Russia and Turkey. Operating income in the year ended March 31, 2009 increased by ¥48.2 billion, or 31.9% from the previous year to ¥199.6 billion.

Liquidity and Capital Resources

In our financial management, we strive to maintain a stable financial base that enables the implementation of capital expenditures, the acquisition of outside resources, and R&D activities in a cost-efficient manner, in order to achieve business expansion without being affected by short-term fluctuations in revenues. We raise the necessary funds principally from cash flows provided by operations, borrowing from financial institutions and the issuance of long-term bonds.

Cash Flows

• Overview:

As of March 31, 2009 and March 31, 2010, cash and cash equivalents totaled ¥167.3 billion and ¥154.4 billion, respectively.

	Millions of yen			Millions of U.S. dollars
For years ended March 31	2008	2009	**2010**	**2010**
Net cash provided by operating activities	¥ 145,030	¥ 275,271	**¥ 320,024**	**$ 3,440**
Net cash used in investing activities	(1,668,635)	(65,008)	**(84,057)**	**(903)**
Net cash provided by (used in) financing activities	519,001	(217,470)	**(250,398)**	**(2,691)**
Effect of exchange rate changes and other	40,091	(39,591)	**1,542**	**15**
Net decrease in cash and cash equivalents	(964,513)	(46,798)	**(12,889)**	**(139)**
Cash and cash equivalents at beginning of the period	1,179,522	215,009	**167,258**	**1,798**
Decrease in cash and cash equivalents resulting from exclusion of subsidiaries from consolidation	—	(953)	**—**	**—**
Cash and cash equivalents at end of the period	¥ 215,009	¥ 167,258	**¥ 154,369**	**$ 1,659**

Year Ended March 31, 2010 Compared with Year Ended March 31, 2009

Net cash generated by operating activities in the year ended March 31, 2010 came to ¥320.0 billion compared with ¥275.3 billion in the year ended March 31, 2009, as an increase in inventories due to a rise in leaf tobacco prices and increased procurement in the international tobacco business was offset by stable cash flow from the tobacco business. Net cash used in investment activities in the year ended March 31, 2010 was ¥84.1 billion compared with ¥65.0 billion for the year ended March 31, 2009. It was mainly due to the expenditures on the acquisition of fixed assets.

Net cash used for financing activities in the year ended March 31, 2010 was ¥250.4 billion compared with ¥217.5 billion in net cash used for such activities in the year ended March 31, 2009. This was mainly due to the payment of dividends and the redemption of corporate bonds and the repayment of borrowings despite of the net cash provided from issuance of commercial paper and corporate bonds.

Year Ended March 31, 2009 Compared with Year Ended March 31, 2008

Net cash generated by operating activities in the year ended March 31, 2009 came to ¥275.3 billion compared with ¥145.0 billion in the year ended March 31, 2008, as an increase in the working capital was more than offset by the creation of stable cash flow by the tobacco

business, including the cash flow generated by the inclusion of the full-year results of Gallaher. In the year ended March 31, 2009, we paid 12 months' worth of tobacco excise tax compared with the 13 months' worth paid in the previous year, when there was a onetime factor related to a bank holiday. Net cash used in investment activities in the year ended March 31, 2009 was ¥65.0 billion compared with ¥1,668.6 billion for the year ended March 31, 2008. Cash was used mainly for the acquisition of additional shares in Katokichi Co. and shares in Fuji Foods Corporation.

Net cash used for financing activities in the year ended March 31, 2009 was ¥217.5 billion, compared with ¥519.0 billion in net cash generated from such activities in the year ended March 31, 2008. This was mainly due to the payment of dividends and the redemption of corporate bonds and the repayment of borrowings by a foreign subsidiary.

Liquidity and Fund Needs

We need liquidity mainly for capital expenditures, working capital, acquisition of outside resources and debt repayments, as well as payments of interest, dividends and income taxes.

• Capital Expenditures

Capital expenditures include outlays on machinery and equipment for factories, trademarks and other tangible and intangible assets necessary for enhancing the productivity of our factories and other facilities, strengthening our competitiveness, and operating in various business fields.

	Millions of yen			Millions of U.S. dollars
For years ended March 31	2008	2009	**2010**	**2010**
Capital expenditures	¥129,555	¥134,273	**¥137,134**	**$1,474**

In the year ended March 31, 2010, capital expenditures totaled ¥137.1 billion. In our Japanese domestic tobacco business, we spent ¥45.8 billion, mainly on measures to streamline manufacturing processes, strengthen our ability to respond flexibly to supply and demand fluctuations with regard to an increasingly diverse range of products and develop new products. In our international tobacco business, we invested ¥64.6 billion for the purpose of expanding our production capacity. In our pharmaceutical business, we spent ¥3.0 billion on the construction of production and research facilities, while we invested ¥23.4 billion in our food business, mainly for enhancing production facilities. In our other businesses, capital expenditures were ¥0.3 billion.

In the year ended March 31, 2009, capital expenditures totaled ¥134.3 billion. In our Japanese domestic tobacco business, we spent ¥46.5 billion, mainly on measures to streamline manufacturing processes, strengthen our ability to respond flexibly to supply and demand fluctuations with regard to an increasingly diverse range of products and develop new products. In our international tobacco business, we invested ¥59.8 billion for the purpose of expanding our production capacity. In our pharmaceutical business, we spent ¥3.4 billion on the construction of production and research facilities, while we invested ¥23.2 billion in our food business, mainly for enhancing production facilities. In our other businesses, capital expenditures were ¥1.1 billion, mainly for real estate development.

In the year ended March 31, 2008, capital expenditures totaled ¥129.6 billion. In our Japanese domestic tobacco business, we spent ¥57.2 billion, mainly on measures to streamline manufacturing processes, strengthen our ability to respond flexibly to supply and demand fluctuations with regard to an increasingly diverse range of products, develop new products and replace vending machines. In our international tobacco business, we invested ¥48.4 billion for the purpose of expanding our production capacity. In our pharmaceutical business, we spent ¥4.3 billion on the construction of production and research facilities, while we invested ¥6.0 billion in our food business, mainly for enhancing production facilities. In our other businesses, capital expenditures were ¥14.8 billion, mainly for real estate development.

For the year ending March 31, 2011, we are planning for capital expenditures to total approximately ¥172.0 billion. In our Japanese domestic tobacco business, we plan to invest approximately ¥62.0 billion to improve productivity and reduce costs, while in our international tobacco business, we plan to spend approximately ¥68.0 billion to increase production capacity. We have earmarked approximately ¥2.5 billion in investment for our pharmaceutical business to improve R&D, approximately ¥35.0 billion for our food business to enhance production facilities and approximately ¥4.5 billion for our other businesses.

Our actual capital expenditures may differ significantly from the planned figures as a result of a number of factors including, but not limited to, those discussed in the "Major Risks of Businesses."

• Working Capital

We need working capital mainly for purchasing raw materials, including leaf tobacco and other inventory items, the payment of salaries and wages, sales expenses, advertising and promotion expenses, tax payments and R&D expenses.

• Acquisition of Outside Resources

As necessary, we may invest in or acquire companies deemed to have the potential to help us diversify our cash flow sources and improve our profitability.

• Dividends

We need sufficient liquidity to make our scheduled dividend payments. As our basic dividend policy, we aim to achieve a consolidated dividend payout ratio of 30% in the medium term under the Medium-Term Management Plan "JT-11," with the impact of goodwill amortization excluded from the net income used as a basis for calculating the payout ratio. We will continue to provide a competitive level of return to shareholders in light of the implementation status of our mid- to long-term growth strategies and the outlook of our consolidated financial results, with a view to increasing our dividend payments further. The dividend payout ratio based on consolidated net income before goodwill amortization for the year ended March 31, 2010 was 23.6%.

• Stock Repurchases

A repurchase of our own shares requires cash outlays. In order to repurchase our own shares in a flexible manner, we amended the Articles of Incorporation at the general shareholders' meeting held on June 24, 2004 so that we could make repurchases based on a resolution made by the Board of Directors. As of March 31, 2010, we held 419,903 shares of common stock as treasury stock. We may continue to hold the repurchased shares as treasury stock or use them for share retirement or for other purposes. Stock repurchases provide our management with an additional option for increasing flexibility and speed in capital management in order to adapt to a rapidly changing business environment. We will determine the timing, scale and manner of any further repurchase in an appropriate manner in light of our business needs and market trends.

Capital Resources and Use

We have historically had, and expect to continue to have, significant cash flows from operating activities. Cash provided by operating activities was ¥275.3 billion in the year ended March 31, 2009 and ¥320.0 billion in the year ended March 31, 2010. We expect that cash generated by operating activities will continue to cover capital expenditures and debt repayments.

For substantial capital needs related to the acquisition of outside resources, we may utilize debt financing, primarily borrowings from financial institutions or the issuance of bonds, as needed. (Please see "Long and Short-term Debt" below.)

Equity financing, including warrants and bonds with warrants, requires the approval of the Minister of Finance under the Japan Tobacco Inc. Law. Revisions to the Japan Tobacco Inc. Law that took effect on April 19, 2002 provide us with the flexibility to issue new shares upon the approval of the Minister of Finance to the extent that the Japanese government retains more than one-third of the outstanding shares in JT. In the future, we may choose to raise capital through stock issuance, which would dilute the value of existing shareholders' equity holdings.

Long and Short-term Debt

• Long-term Debt

Our long-term liabilities consist mainly of long-term debt and liabilities for retirement benefits. As of March 31, 2010, long-term debt was ¥646.1 billion, of which bonds accounted for ¥459.4 billion. Our remaining long-term debt (including the current portion) consisted of ¥172.6 billion loans from banks and life insurance companies and ¥14.1 billion long-term lease obligations. Annual interest rates applicable to yen-denominated long-term bank loans outstanding as of March 31, 2009 and 2010 ranged from 0.77% to 5.30% and from 0.90% to 5.30%, respectively. Annual interest rates for long-term loans denominated in other currencies ranged from 2.35% to 8.00% for those outstanding as of March 31, 2009 and from 0.97% to 8.75% for those outstanding as of March 31, 2010.

Maturities of long-term debt (including the current portion) as of March 31, 2010 were as follows:

For years ended March 31	Millions of yen	Millions of U.S. dollars
2011	¥306,525	$3,295
2012	172,228	1,851
2013	166,974	1,795
2014	59,149	636
2015	168,558	1,812
2016 and thereafter	873	8
Total	¥874,307	$9,397

As of March 31, 2010, our long-term debt was rated Aa3 by Moody's Investors Service, Inc., A+ by Standard & Poor's Ratings Services and AA by Rating and Investment Information, Inc. (R&I). These ratings are among the highest ratings for international tobacco companies. By maintaining high credit ratings, we can finance large sums of capital at relatively low cost from third parties as needed. Our ability to maintain high ratings is affected by a number of factors such as developments in our major business markets, the quality of execution of our business strategies, and general economic trends that are beyond our control. The credit ratings are not recommendations for purchasing, selling or holding securities.

The ratings could be withdrawn or revised at any time. Each rating should be evaluated separately from other ratings. Under the JT Law, bonds issued by JT are secured by statutory preferential rights to the property of JT. These rights give bondholders precedence over unsecured creditors in seeking repayment, with the exception of national and local taxes and other statutory obligations.

• Short-term Debt

We take in short-term loans from banks and other financial institutions. Short-term loans totaled ¥113.2 billion as of March 31, 2009, including ¥61.8 billion in foreign currency-denominated loans, and ¥228.3 billion as of March 31, 2010, including ¥60.3 billion in foreign currency-denominated loans. Annual interest rates applicable to yen

denominated short-term bank loans ranged from 0.216% to 2.750% as of March 31, 2009 and from 0.090% to 3.500% as of March 31, 2010. Annual interest rates applicable to short-term loans denominated in other currencies ranged from 0.130% to 83.000% as of March 31, 2009 and from 1.040% to 27.250% as of March 31, 2010. Annual interest rates applicable to commercial paper ranged from 0.106% to 0.145% as of March 31, 2010.

As a Japanese commercial custom, short-term and long-term bank loans are extended under general agreements stipulating that, under certain circumstances, collateral or guarantees for present and future debts should be provided upon the request of the bank, and that the bank shall have the right, as the debt obligations become due or in the event of default, to offset cash deposits against debts due to it. We have never been requested to provide such collateral or guarantees.

Derivative Transactions

We are exposed to market risks principally from changes in interest rates, foreign exchange rates and equity and debt security prices. Our interest rate risk exposures primarily relate to financing activities.

Our foreign currency exposures relate to buying, selling and financing in currencies other than the local currencies of our operations. In order to reduce foreign exchange rate risk and interest rate risk, we use derivative financial instruments including interest rate swaps, interest rate cap option contracts, foreign currency forward contracts, currency swaps and currency option contracts. We do not hedge against price fluctuations of debt and equity securities.

We have risk management policies and procedures designed to mitigate the risks arising from the use of derivative financial instruments.

We utilize derivatives solely for risk management purposes, and no derivatives are held or issued for trading purposes. As part of our risk management procedures, we identify the specific risks and transactions to be hedged and the appropriate hedging instruments to be used to reduce the risk, and assess the correlation between the hedged risks and the hedging instruments. The effectiveness of our hedging activities is assessed in accordance with our risk management policies and practice manual for hedging transactions.

We are exposed to credit-related risk in the event of default by counterparties to derivative financial instruments. However, we strive to mitigate this risk by limiting counterparties to international financial institutions with high credit ratings deemed to have no significant risk of default.

We use interest rate swaps and interest rate cap option contracts for the purpose of managing interest rate risk in relation to borrowings. Interest rate swap agreements that qualify for hedge accounting under Japanese GAAP and meet specific matching criteria are not measured at market value, but the differential to be paid or received under the swap agreement is accrued and included in interest expenses.

We use foreign currency forward contracts, currency swaps and currency option contracts for the purpose of managing the risk of fluctuations in foreign exchange rates on forecasted transactions in foreign currencies. Gains or losses arising from changes in the value of the contracts that qualify for hedge accounting are deferred and recognized in the period in which corresponding losses or gains from transactions being hedged by such contracts are recognized.

On the other hand, hedging contracts mainly related to our international tobacco operations do not qualify for hedge accounting and therefore we recognize changes in the value of foreign currency derivative instruments against earnings in the period in which they occur. This could result in gains or losses from fluctuations in exchange rates related to a derivative contract being recognized in a different period from the one in which the gains or losses expected from the underlying forecasted transactions are recognized.

For information about the contract and notional amount of interest rate swaps, interest rate cap option contracts, foreign currency forward contracts and currency swaps outstanding as of March 31, 2009 and 2010 see Note 17 to the audited consolidated financial statements included in this annual report.

Outlook of Results for the Year Ending March 31, 2011

It is too early to forecast specific business results for the fiscal year ending March 31, 2011. Based on current trends and other factors that we are aware of at this point, we expect a decline in both net sales and profits. Although we expect the favorable pricing and currency benefits in the international tobacco business, net sales are projected to decrease, affected by a decline in the sale volume due to a steep drop in overall demand that the Japanese domestic tobacco business will face as a result of a sharp increase in the tobacco excise tax scheduled to take effect on October 1, 2010. EBITDA and operating income are projected to decrease. Net income is likely to decrease due to a decline in profits from the sale of fixed assets, and an increase of other expenses due to an agreement payment to the Canadian authorities, despite the absence of the exchange losses incurred in the previous year.

Our actual operating results may differ significantly from those described above as a result of a number of factors including, but not limited to, those discussed in the "Major Risks of Businesses."

Consolidated Balance Sheets

Japan Tobacco Inc. and Consolidated Subsidiaries / March 31, 2009 and 2010

	Millions of yen		Millions of U.S. dollars (Note 2)
Assets	2009	**2010**	**2010**
Current assets:			
Cash and cash equivalents	¥ 167,258	**¥ 154,369**	**$ 1,659**
Short-term investments (Note 5)	2,610	**13,026**	**140**
Trade notes and accounts receivable	290,069	**296,885**	**3,191**
Merchandise & finished goods	122,970	**151,063**	**1,624**
Semi-finished goods	119,291	**109,622**	**1,178**
Work in process	6,562	**5,523**	**59**
Raw materials & supplies (Note 8)	215,335	**288,893**	**3,105**
Other current assets (Note 12)	174,749	**180,086**	**1,936**
Allowance for doubtful accounts	(3,162)	**(3,623)**	**(39)**
Total current assets	1,095,682	**1,195,844**	**12,853**
Property, plant and equipment (Note 8)**:**			
Land	147,219	**138,703**	**1,491**
Buildings and structures	621,469	**611,509**	**6,573**
Machinery, equipment and vehicles	642,149	**668,608**	**7,186**
Tools	165,435	**170,907**	**1,837**
Construction in progress	35,254	**41,905**	**450**
Total	1,611,526	**1,631,632**	**17,537**
Accumulated depreciation	(942,783)	**(952,071)**	**(10,233)**
Net property, plant and equipment	668,743	**679,561**	**7,304**
Investments and other assets:			
Investment securities (Note 5)	66,495	**60,178**	**647**
Investments in and advances to unconsolidated subsidiaries and associated companies	24,639	**23,932**	**257**
Trademarks	347,372	**350,901**	**3,772**
Goodwill	1,453,961	**1,387,397**	**14,912**
Deferred tax assets (Note 12)	128,787	**85,376**	**918**
Other assets	135,820	**124,102**	**1,333**
Allowance for doubtful accounts	(41,696)	**(34,695)**	**(373)**
Total investments and other assets	2,115,378	**1,997,191**	**21,466**
Total	¥3,879,803	**¥3,872,596**	**$ 41,623**

See notes to consolidated financial statements.

Liabilities and Equity	Millions of yen 2009	2010	Millions of U.S. dollars (Note 2) 2010
Current liabilities:			
Short-term bank loans (Note 8)	¥ 113,231	**¥ 109,263**	**$ 1,174**
Commercial paper (Note 8)	—	**119,000**	**1,279**
Current portion of long-term debt (Note 8)	222,256	**78,356**	**842**
Tobacco excise taxes payable	268,999	**307,795**	**3,308**
Trade notes and accounts payable	158,544	**149,462**	**1,606**
Other payable (Note 9)	62,825	**73,739**	**793**
Income taxes payable (Note 12)	51,777	**54,058**	**581**
Consumption taxes payable	43,848	**60,105**	**646**
Other current liabilities (Notes 8, 9 and 12)	171,923	**149,757**	**1,610**
Total current liabilities	1,093,403	**1,101,535**	**11,839**
Non-current liabilities:			
Long-term debt (Note 8)	660,592	**567,710**	**6,102**
Liabilities for retirement benefits (Note 9)	259,146	**251,902**	**2,707**
Deferred tax liabilities (Note 12)	110,390	**94,578**	**1,017**
Other non-current liabilities (Notes 8 and 9)	131,984	**133,592**	**1,436**
Total non-current liabilities	1,162,112	**1,047,782**	**11,262**
Commitments and contingent liabilities (Note 18)			
Equity (Note 10)**:**			
Common stock—authorized, 40,000,000 shares; issued, 10,000,000 shares in 2009 and 2010	100,000	**100,000**	**1,075**
Capital surplus	736,400	**736,407**	**7,915**
Stock acquisition rights (Note 11)	365	**565**	**6**
Retained earnings	1,224,989	**1,310,670**	**14,087**
Unrealized gain on available-for-sale securities	8,438	**12,044**	**129**
Deferred gain on derivatives under hedge accounting	92	**—**	**—**
Pension liability adjustment of foreign consolidated subsidiaries (Note 9)	(18,966)	**(26,270)**	**(282)**
Foreign currency translation adjustments	(423,562)	**(409,161)**	**(4,397)**
Treasury stock, at cost—419,920 shares in 2009 and 419,903 shares in 2010	(74,578)	**(74,575)**	**(802)**
Total	1,553,178	**1,649,680**	**17,731**
Minority interests	71,110	**73,599**	**791**
Total Equity	1,624,288	**1,723,279**	**18,522**
Total	¥3,879,803	**¥3,872,596**	**$41,623**

Consolidated Statements of Income

Japan Tobacco Inc. and Consolidated Subsidiaries / Years ended March 31, 2008, 2009 and 2010

			Millions of yen	Millions of U.S. dollars (Note 2)
	2008	2009	**2010**	**2010**
Net sales	¥6,409,727	¥6,832,307	**¥6,134,695**	**$65,936**
Cost of sales (Note 3 (f))	5,228,926	5,554,399	**5,022,637**	**53,984**
Gross profit	1,180,801	1,277,908	**1,112,058**	**11,952**
Selling, general and administrative expenses (Notes 11 and 13)	750,247	914,102	**815,553**	**8,765**
Operating income	430,554	363,806	**296,505**	**3,187**
Other income (expenses):				
Interest and dividend income	13,410	12,276	**6,982**	**75**
Gain on disposition of property, plant and equipment—net	57,179	32,787	**21,770**	**234**
Loss on impairment of long-lived assets (Note 15)	(3,825)	(16,365)	**(6,043)**	**(65)**
Interest expense (Note 8)	(41,759)	(51,356)	**(26,111)**	**(281)**
Write-down of investment securities	(11,154)	(7,063)	**(1,404)**	**(15)**
Business restructuring costs (Notes 9 and 15)	(6,442)	(24,364)	**(9,900)**	**(106)**
Other—net (Note 15)	(65,349)	(47,577)	**(5,744)**	**(62)**
Other income (expenses)—net	(57,940)	(101,662)	**(20,450)**	**(220)**
Income Before Income Taxes and Minority Interests	372,614	262,144	**276,055**	**2,967**
Income taxes (Note 12):				
Current	117,272	126,732	**114,145**	**1,227**
Deferred	11,107	8,241	**17,159**	**184**
Total income taxes	128,379	134,973	**131,304**	**1,411**
Income Before Minority Interests	244,235	127,171	**144,751**	**1,556**
Minority interests	5,533	3,771	**6,303**	**68**
Net income	¥ 238,702	¥ 123,400	**¥ 138,448**	**$ 1,488**

			Yen	U.S. dollars
Amounts per share:				
Basic net income (Notes 3 (r) and 19)	¥ 24,917	¥ 12,881	**¥ 14,452**	**$ 155**
Diluted net income (Notes 3 (r) and 19)	24,916	12,880	**14,449**	**155**
Cash dividends applicable to the year (Note 3 (r))	4,800	5,400	**5,800**	**62**

See notes to consolidated financial statements.

Consolidated Statements of Changes in Equity

Japan Tobacco Inc. and Consolidated Subsidiaries / Years ended March 31, 2008, 2009 and 2010

	Thousands	Millions of yen											
	Number of shares of common stock issued	Common stock	Capital surplus	Stock Acquisition Rights (Note 11)	Retained earnings	Unrealized gain on available-for-sale securities	Deferred gain on derivatives under hedge accounting	Pension liability adjustment of foreign consolidated subsidiaries (Note 9)	Foreign currency translation adjustments	Treasury stock	Total	Minority interests	Total equity
Balance, March 31, 2007	10,000	¥100,000	¥736,400	¥ —	¥1,158,337	¥ 33,330	¥14,580	¥(15,560)	¥ 7,745	¥(74,578)	¥1,960,254	¥64,362	¥2,024,616
Adoption of FIN 48 (Note 3 (q))	—	—	—	—	(10,548)	—	—	—	—	—	(10,548)	—	(10,548)
Net income	—	—	—	—	238,702	—	—	—	—	—	238,702	—	238,702
Appropriations:													
Cash dividends paid (¥4,400 per share)	—	—	—	—	(42,152)	—	—	—	—	—	(42,152)	—	(42,152)
Adjustment to retained earnings for change in the number of equity method affiliates	—	—	—	—	151	—	—	—	—	—	151	—	151
Net Changes in the year	—	—	—	186	—	(11,991)	(14,360)	4,848	(48,831)	—	(70,148)	14,008	(56,140)
Balance, March 31, 2008	10,000	100,000	736,400	186	1,344,490	21,339	220	(10,712)	(41,086)	(74,578)	2,076,259	78,370	2,154,629
Adjustment of retained earnings due to an adoption of PITF No. 18 (Note 3 (b))	—	—	—	—	(193,658)	—	—	—	—	—	(193,658)	—	(193,658)
Net income	—	—	—	—	123,400	—	—	—	—	—	123,400	—	123,400
Appropriations:													
Cash dividends paid (¥5,200 per share)	—	—	—	—	(49,816)	—	—	—	—	—	(49,816)	—	(49,816)
Adjustment to retained earnings for change in the number of consolidated subsidiaries	—	—	—	—	47	—	—	—	—	—	47	—	47
Adjustment to retained earnings for change in the number of equity method affiliates	—	—	—	—	526	—	—	—	—	—	526	—	526
Net changes in the year	—	—	—	179	—	(12,901)	(128)	(8,254)	(382,476)	—	(403,580)	(7,260)	(410,840)
Balance, March 31, 2009	10,000	100,000	736,400	365	1,224,989	8,438	92	(18,966)	(423,562)	(74,578)	1,553,178	71,110	1,624,288
Net income	**—**	**—**	**—**	**—**	**138,448**	**—**	**—**	**—**	**—**	**—**	**138,448**	**—**	**138,448**
Appropriations:													
Cash dividends paid (¥5,600 per share)	**—**	**—**	**—**	**—**	**(53,648)**	**—**	**—**	**—**	**—**	**—**	**(53,648)**	**—**	**(53,648)**
Adjustment to retained earnings for change in the number of equity method affiliates	**—**	**—**	**—**	**—**	**881**	**—**	**—**	**—**	**—**	**—**	**881**	**—**	**881**
Disposal of treasury stock	**—**	**—**	**7**	**—**	**—**	**—**	**—**	**—**	**—**	**3**	**10**	**—**	**10**
Net changes in the year	**—**	**—**	**—**	**200**	**—**	**3,606**	**(92)**	**(7,304)**	**14,401**	**—**	**10,811**	**2,489**	**13,300**
Balance, March 31, 2010	**10,000**	**¥100,000**	**¥736,407**	**¥565**	**¥1,310,670**	**¥ 12,044**	**¥ —**	**¥(26,270)**	**¥(409,161)**	**¥(74,575)**	**¥1,649,680**	**¥73,599**	**¥1,723,279**

	Millions of U.S. dollars (Note 2)											
	Common stock	Capital surplus	Stock Acquisition Rights (Note 11)	Retained earnings	Unrealized gain on available-for-sale securities	Deferred gain on derivatives under hedge accounting	Pension liability adjustment of foreign consolidated subsidiaries (Note 9)	Foreign currency translation adjustments	Treasury stock	Total	Minority interests	Total equity
Balance, March 31, 2009	$1,075	$7,915	$4	$13,166	$ 91	$ 1	$(204)	$(4,552)	$(802)	$16,694	$764	$17,458
Net income	**—**	**—**	**—**	**1,488**	**—**	**—**	**—**	**—**	**—**	**1,488**	**—**	**1,488**
Appropriations:												
Cash dividends paid ($60 per share)	**—**	**—**	**—**	**(576)**	**—**	**—**	**—**	**—**	**—**	**(576)**	**—**	**(576)**
Adjustment to retained earnings for change in the number of equity method affiliates	**—**	**—**	**—**	**9**	**—**	**—**	**—**	**—**	**—**	**9**	**—**	**9**
Disposal of treasury stock	**—**	**0**	**—**	**—**	**—**	**—**	**—**	**—**	**0**	**0**	**—**	**0**
Net changes in the year	**—**	**—**	**2**	**—**	**38**	**(1)**	**(78)**	**155**	**—**	**116**	**27**	**143**
Balance, March 31, 2010	**$1,075**	**$7,915**	**$6**	**$14,087**	**$129**	**$—**	**$(282)**	**$(4,397)**	**$(802)**	**$17,731**	**$791**	**$18,522**

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

Japan Tobacco Inc. and Consolidated Subsidiaries / Years ended March 31, 2008, 2009 and 2010

			Millions of yen	Millions of U.S. dollars (Note 2)
	2008	2009	**2010**	**2010**
Operating Activities:				
Income before income taxes and minority interests	¥ 372,614	¥ 262,144	**¥ 276,055**	**$ 2,967**
Adjustments for:				
Income taxes paid	(132,725)	(114,414)	**(116,339)**	**(1,250)**
Depreciation and amortization other than goodwill	167,658	176,900	**132,770**	**1,427**
Amortization of goodwill	3,883	105,512	**97,427**	**1,047**
Gain on disposition of property, plant and equipment	(57,179)	(32,787)	**(21,770)**	**(234)**
Loss on impairment of long-lived assets	3,825	16,365	**6,043**	**65**
Write-down of investment securities	11,154	7,063	**1,404**	**15**
Change in assets and liabilities:				
Decrease (increase) in trade notes and accounts receivable	47,485	(43,141)	**5,703**	**61**
Decrease (increase) in inventories	27,115	(47,632)	**(79,457)**	**(854)**
Increase (decrease) in tobacco excise taxes payable	(213,134)	28,981	**30,842**	**331**
Increase (decrease) in trade notes and accounts payable	(16,650)	2,699	**(12,821)**	**(138)**
Increase (decrease) in other payable	(39,956)	(7,940)	**14,905**	**160**
Decrease in liabilities for retirement benefits	(4,932)	(13,159)	**(8,035)**	**(86)**
Other—net	(24,128)	(65,320)	**(6,703)**	**(71)**
Total adjustments	(227,584)	13,127	**43,969**	**473**
Net cash provided by operating activities	145,030	275,271	**320,024**	**3,440**
Investing Activities:				
Purchases of short-term investments	(2,443)	(1,643)	**(3,999)**	**(43)**
Proceeds from sale and redemption of short-term investments	6,846	3,272	**2,471**	**27**
Purchases of property, plant and equipment	(124,832)	(112,408)	**(121,459)**	**(1,305)**
Proceeds from sale of property, plant and equipment	83,336	55,256	**44,058**	**474**
Purchases of trademarks and other assets	(6,831)	(6,949)	**(6,639)**	**(71)**
Purchases of shares of newly consolidated subsidiaries, net of cash acquired (Note 4)	(1,608,081)	(3,061)	**(9,975)**	**(107)**
Other—net	(16,630)	525	**11,486**	**122**
Net cash used in investing activities	(1,668,635)	(65,008)	**(84,057)**	**(903)**
Financing Activities:				
Net increase (decrease) in short-term bank loans and commercial paper	136,063	(125,182)	**93,444**	**1,005**
Proceeds from long-term debt	378,863	94,130	**1,712**	**18**
Repayments of long-term debt	(90,199)	(54,663)	**(191,041)**	**(2,053)**
Proceeds from issuance of bonds	149,723	—	**100,304**	**1,078**
Payment for redemption of bonds	(10,000)	(70,810)	**(191,928)**	**(2,063)**
Dividends paid	(42,152)	(49,752)	**(53,642)**	**(577)**
Proceeds from issuance of common stock to minority shareholders	—	—	**191**	**2**
Dividends paid to minority shareholders	(2,890)	(3,540)	**(3,681)**	**(40)**
Repayments of finance lease obligations	—	(6,606)	**(5,757)**	**(61)**
Other—net	(407)	(1,047)	**0**	**0**
Net cash provided by (used in) financing activities	519,001	(217,470)	**(250,398)**	**(2,691)**
Foreign Currency Translation Adjustments on Cash and Cash Equivalents	40,091	(39,591)	**1,542**	**15**
Net Decrease in Cash and Cash Equivalents	(964,513)	(46,798)	**(12,889)**	**(139)**
Cash and Cash Equivalents, Beginning of Year	1,179,522	215,009	**167,258**	**1,798**
Decrease in Cash and Cash Equivalents Resulting from Exclusion of Subsidiaries from Consolidation	—	(953)	**—**	**—**
Cash and Cash Equivalents, End of Year	¥ 215,009	¥ 167,258	**¥ 154,369**	**$ 1,659**

Finance lease obligations regarded as non-cash transactions incurred for the year ended March, 2009 and 2010 amounted to ¥6,176 million and ¥3,417 million ($37 million), respectively.

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Japan Tobacco Inc. and Consolidated Subsidiaries

1. Business

Japan Tobacco Inc. ("JT") is a joint stock corporation (kabushikikaisya) incorporated under the companies act of Japan (the "Companies Act") pursuant to the Japan Tobacco Inc. Law (the "JT Law"). JT and its consolidated subsidiaries (the "Group") operate primarily in the domestic and international tobacco businesses, the pharmaceutical business and the food business. In the Group's domestic and international tobacco businesses, the Group develops, manufactures, distributes, and sells tobacco products, primarily cigarettes. In the Group's pharmaceutical business, the Group develops, manufactures and sells pharmaceutical products. In the Group's food business, the Group develops, manufactures and sells processed food, and develops and sells beverages. The Group's other business segment includes its commercial real estate and other operations.

2. Basis of Presenting Consolidated Financial Statements

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

In the case of most foreign consolidated subsidiaries, their financial statements are prepared in conformity with U.S. GAAP (see Note 3 (q) Foreign Consolidated Subsidiaries) and are included in the consolidated financial statements on that basis.

In preparing these consolidated financial statements, certain reclassifications and rearrangements have been made to the consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan. In addition, certain reclassifications have been made in the 2008 and 2009 financial statements to conform to the classifications used in 2010.

The consolidated financial statements are stated in Japanese yen, the currency of the country in which JT is incorporated and operates. The translations of Japanese yen amounts into U.S. dollar amounts are included solely for the convenience of readers outside Japan and have been made at the rate of ¥93.04 to $1, the approximate rate of exchange at March 31, 2010. Such translations should not be construed as representations that the Japanese yen amounts could be converted into U.S. dollars at that or any other rate.

3. Summary of Significant Accounting Policies

a) Consolidation

The consolidated financial statements as of March 31, 2010 include the accounts of JT and its 258 significant (299 as of March 31, 2008 and 274 as of March 31, 2009) subsidiaries.

Consolidation of the remaining unconsolidated subsidiaries would not have had a material effect on the accompanying consolidated financial statements.

Most foreign consolidated subsidiaries have a December 31 fiscal year-end, which differs from the March 31 fiscal year-end of JT. Any necessary adjustments for the three-month period are made for consolidation purposes.

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

Investments in 17 material associated companies as of March 31, 2010 (25 as of March 31, 2008 and 22 as of March 31, 2009) are accounted for by the equity method. The equity method is not applied to account for the investments in unconsolidated subsidiaries and the remaining associated companies, since the effect on the accompanying consolidated financial statements would not have been material. Investments in the remaining unconsolidated subsidiaries and the associated companies are stated at cost (see (d) Securities).

All significant inter-company balances and transactions have been eliminated in consolidation. All material unrealized gains resulting from inter-company transactions have been eliminated.

The excess of the cost of the Group's investments in consolidated subsidiaries over the fair value of the net assets purchased at the date of acquisition is recorded as goodwill. Goodwill is amortized on a straight-line basis over five to twenty years. Such amortization expense is included in selling, general and administrative expenses. However, insignificant goodwill is charged to income when incurred.

b) Unification of Accounting Policies Applied to Foreign Subsidiaries for Consolidated Financial Statements

In May 2006, the Accounting Standards Board of Japan (the "ASBJ") issued ASBJ Practical Issues Task Force (PITF) No. 18, "Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries for the Consolidated Financial Statements." PITF No. 18 prescribes: (1) the accounting policies and procedures applied to a parent company and its subsidiaries for similar transactions and events under similar circumstances should in principle be unified for the preparation of the consolidated financial statements, (2) financial statements prepared by foreign subsidiaries in accordance with either International Financial Reporting Standards or the generally accepted accounting principles in the United States of America tentatively may be used for the consolidation process, (3) however, the following items should be adjusted in the consolidation process so that net income is accounted for in accordance with Japanese GAAP unless they are not material:

1. Amortization of goodwill
2. Scheduled amortization of actuarial gain or loss of pensions that has been directly recorded in the equity
3. Expensing capitalized development costs of R&D
4. Cancellation of the fair value model accounting for property, plant, and equipment and investment properties and incorporation of the cost model accounting
5. Recording the prior years' effects of changes in accounting policies in the income statement where retrospective adjustments to financial statements have been incorporated
6. Exclusion of minority interests from net income, if contained

JT applied this accounting standard effective April 1, 2008. As a result of this change, operating income and income before income taxes and minority interests for the year ended March, 2009 decreased by ¥94,235 million respectively, and as of April 1, 2008, retained earnings decreased by ¥193,658 million as JT amortized goodwill posted at consolidated foreign subsidiaries.

Also, income before income taxes and minority interests for the year ended March 31, 2009 decreased by ¥912 million respectively, as JT posted the retrospective adjustment in the Consolidated Statements of Income. The adjustment was caused by an accounting policy change in foreign subsidiaries as a result of a change of U.S. GAAP.

c) Cash Equivalents

Cash equivalents are short-term investments that are readily convertible into cash and that are exposed to insignificant risk of changes in value. All of cash equivalents mature or become due within three months of the date of acquisition.

d) Securities

The Group's securities are classified as held-to-maturity debt securities or available-for-sale securities, depending on management's holding intent. Held-to-maturity debt securities are reported at amortized cost. Available-for-sale marketable securities are reported at fair value, with unrealized gains and losses, net of applicable taxes, reported in a separate component of equity.

The cost of available-for-sale marketable securities sold is determined based on the moving-average method. Non-marketable available-for-sale securities are stated at cost determined by the moving-average method. For significant impairment in value that is judged unrecoverable, carrying amounts of securities are reduced to fair value, with a resulting charge to income. An allowance for loss on investments is recorded to provide for the loss on investments in certain non-marketable equity accounted for by the cost method and is determined based on the respective financial condition of the investees.

e) Allowance for Doubtful Accounts

The allowance for doubtful accounts is stated in amounts considered to be appropriate based on the companies' past credit loss experience and an evaluation of potential losses in the receivables outstanding.

f) Inventories

Inventories are generally stated at the lower of cost or net selling value, cost being determined by the average method.

In July 2006, the Accounting Standards Board of Japan ("ASBJ") issued ASBJ Statement No. 9," Accounting Standard for Measurement of Inventories," and JT and its domestic subsidiaries adopted the standard from fiscal year beginning on April 1, 2007. This standard requires that inventories held for sale in the ordinary course of business be measured at the lower of cost or net selling value, which is defined as the selling price less additional estimated manufacturing costs and estimated direct selling expenses. The replacement cost may be used in place of the net selling value, if appropriate.

In addition, leaf tobacco held by JT was subject to annual devaluation prior to April 1, 2007. JT no longer applies annual devaluation for its leaf inventories from the year ended March 31, 2008 (see Note 6).

g) Property, Plant and Equipment

Property, plant and equipment are stated at cost. Depreciation is generally computed using the declining-balance method while the straight-line method is applied to buildings acquired after April 1, 1998. The useful lives of buildings and structures, and machinery, equipment and vehicles are principally from 38 to 50 years and 10 years, respectively.

For finance leases that do not transfer ownership of the leased property to the lessee, depreciation is mainly computed using straight-line method over the lease period as the useful life and assuming no residual value.

(Changes in useful life of property, plant and equipment)

The useful life of property, plant and equipment with respect to Domestic Group was changed as a result of the use review of these assets in conjunction with the revision of the corporate tax act, principally, the useful life of tobacco manufacturing was changed from 8 years to 10 years.

The effect of this change for the year ended March, 2009 is immaterial.

h) Impairment of Long-Lived Assets

The Domestic Group reviews its long-lived assets for impairment whenever events or changes in circumstance indicate the carrying amount of an asset or asset group may not be recoverable. An impairment loss would be recognized if the carrying amount of an asset or asset group exceeds the sum of the undiscounted future cash flows expected to result from the continued use and eventual disposition of the asset or asset group.

The impairment loss would be measured as the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of the discounted cash flows from the continued use and eventual disposition of the asset or the net selling price at disposition.

i) Intangible Assets

Trademarks are carried at cost less accumulated amortization, which is calculated by the straight-line method principally over 10 years.

j) Income Taxes

The provision for income taxes is computed based on the pretax income or loss included in the consolidated statements of income. The asset and liability approach is used to recognize deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities, and tax operating loss and other credit carry-forwards. Deferred taxes are measured by applying currently enacted tax laws to the temporary differences, tax operating loss and other credit carry-forwards. A valuation allowance is provided for any portion of the deferred tax assets where it is considered more likely than not that they will not be realized.

k) Accrued bonuses

Bonuses to directors, cooperate auditors and employees are accrued at the year end to which such bonuses are attributable.

l) Liabilities for Retirement Benefits

(1) Employees' retirement benefits

JT has an unfunded severance indemnity plan and a cash balance pension plan (the ''Pension Plans'') as well as a defined contribution plan, which cover substantially all of its employees. Its consolidated subsidiaries principally have unfunded severance indemnity plans and/or non-contributory defined pension plans.

The Pension Plans and the subsidiaries' plans are stated based on actuarially estimated retirement benefit obligations, considering the estimated fair value of plan assets at each balance sheet date. Certain domestic subsidiaries apply a simplified method, under which retirement benefit obligations are recorded based on the amount required if all employees terminated their employment as of the balance sheet date. Contributions to the defined contribution plan are charged to expenses when they are paid or accrued.

(2) Obligations under the Public Official Mutual Assistance Association Law

As a formerly wholly government-owned company, JT is obligated by the Public Official Mutual Assistance Association Law to reimburse the Japanese government for pension expenses incurred each year by the government for former employees of Japan Tobacco and Salt Public Corporation ("JTSPC"), JT's predecessor entity, and others for their services during certain periods before July 1, 1956. Such obligations are recognized as liabilities at their present value using the actuarially determined computation method.

m) Leases

In March 2007, the ASBJ issued ASBJ Statement No. 13, "Accounting Standard for Lease Transactions," which revised the previous accounting standard for lease transactions issued in June 1993. The revised accounting standard for lease transactions is effective for fiscal years beginning on or after April 1, 2008 with early adoption permitted for fiscal years beginning on or after April 1, 2007.

–Lessee–

Under the previous accounting standard, finance leases that deem to transfer ownership of the leased property to the lessee are to be capitalized. However, other finance leases were permitted to be accounted for as operating lease transactions if certain "as if capitalized" information is disclosed in the note to the lessee's financial statements. The revised accounting standard requires that all finance lease transactions should be capitalized to recognize lease assets and lease obligations in the balance sheet.

In addition, the revised accounting standard permits leases which existed at the transition date and do not transfer ownership of the leased property to the lessee to be measured at the obligations under finance leases less interest expense at the transition date and recorded as acquisition cost of lease assets.

–Lessor–

Under the previous accounting standard, finance leases that deem to transfer ownership of the leased property to the lessee are to be treated as sales. However, other finance leases were permitted to be accounted for as operating lease transactions if certain "as if sold" information is disclosed in the note to the lessor's financial statements. The revised accounting standard requires that all finance leases that deem to transfer ownership of the leased property to the lessee should be recognized as lease receivables, and all finance leases that deem not to transfer ownership of the leased property to the lessee should be recognized as investments in lease.

JT and its domestic subsidiaries applied this accounting standard effective April 1, 2008. In addition, the Company accounted for leases which existed at the transition date and do not transfer ownership of the leased property to the lessee as acquisition cost of lease assets measured at the obligations under finance leases less interest expense at the transition date. The effect of this change on operating income and income before income taxes and minority interests is immaterial.

n) Appropriations of Retained Earnings

Appropriations of retained earnings are reflected in the financial statements for the following year upon shareholders' approval.

o) Foreign Currency Transactions

Receivables and payables denominated in foreign currencies are translated into Japanese yen at the rates prevailing at each balance sheet date. The exchange gains or losses from translation are recognized in the consolidated statements of income to the extent that hedging derivative financial instruments for foreign currency transactions do not qualify for hedge accounting (see (p) Derivatives).

All assets and liabilities of foreign consolidated subsidiaries are translated into Japanese yen at the exchange rate at each subsidiary's respective fiscal year end. All revenue and expense accounts are translated at average exchange rates during each subsidiary's respective fiscal year.

Differences arising from such translation are shown as "Foreign currency translation adjustments" and "Minority interests" in a separate component of equity.

p) Derivatives

All derivatives, except for certain foreign exchange forward contracts, foreign currency option contracts, foreign currency swap contracts and interest rate swap contracts described below, are recognized as either assets or liabilities and measured at fair value, and gains or losses on derivative transactions are recognized in the consolidated statements of income.

For derivatives which qualify for hedge accounting because of high correlation and effectiveness between the hedging instruments and the hedged items, gains or losses on derivatives are deferred until the corresponding hedged items are recognized in earnings.

The Group's trade payables that are denominated in foreign currencies and have been hedged by foreign exchange forward contracts are translated at the foreign exchange rate stipulated in the contracts.

Interest rate swaps that qualify for hedge accounting and meet specific matching criteria are not remeasured at market value, but the differential to be paid or received under the swap agreements are accrued and included in interest expense or income.

q) Foreign Consolidated Subsidiaries

JT International and other foreign consolidated subsidiaries principally maintain their accounting records in conformity with U.S. GAAP.

The significant accounting policies, which are different from JT's policies, are as follows:

(1) Inventories

Inventories are generally stated at the lower of cost or market, cost being determined by the first-in, first-out method or average cost.

(2) Property, plant and equipment

Depreciation of property, plant and equipment is generally computed using the straight-line method over the estimated useful lives of the respective assets.

(3) Trademarks

Trademarks are principally amortized using straight-line method over 20 years.

(4) Retirement benefit pension plans

According to FASB statement 158 "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans—an amendment of FASB statements No. 87, 88, 106 and 132(R)" ("FASB 158"), the difference of retirement benefits obligation and fair value of plan assets is recognized on the consolidated balance sheets as of March 31, 2009 and 2010 as assets/liabilities.

Unrecognized actuarial net loss and prior service cost, net of applicable taxes, are recorded as a part of equity as pension liability adjustment of foreign consolidated subsidiaries.

(5) Derivatives

All derivatives are used to hedge the exposure to foreign exchange risk and interest rate risk are recognized as either assets or liabilities in the balance sheet and measured at fair value.

Changes in the fair value of derivatives are recorded in current earnings for each fiscal year.

(6) Income Taxes

Foreign consolidated subsidiaries that apply in conformity with U.S. GAAP adopt the provisions of FASB Interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes.

r) Per Share Information

Basic net income per share is computed by dividing net income available to common shareholders by the weighted-average number of common shares outstanding in each period, which were 9,580,080 shares for the years ended March 31, 2008 and 2009, and 9,580,092 shares for the year ended March 31, 2010 (see Note 19).

Diluted net income per share for the year ended March 31, 2008, 2009 and 2010 reflects the potential dilution that could occur if stock acquisition rights were exercised. Diluted net income per share of common stock assumes full exercise of the outstanding stock acquisition rights at the beginning of the year or at the time of issuance. (see Note 19)

Cash dividends per share presented in the Consolidated Statements of Income are dividends applicable to the respective years including dividends to be paid after the end of the year.

s) Stock Option

The ASBJ Statement No. 8, "Accounting Standard for Stock Options" and related guidance are applicable to stock options granted on and after May 1, 2006. This standard requires companies to recognize compensation expense for employee stock options based on the fair value at the date of grant and over the vesting period as consideration for receiving goods or services. The standard also requires companies to account for stock options granted to non-employees based on the fair value of either the stock option or the goods or services received. In the balance sheet, the stock option is presented as a stock acquisition right as a separate component of equity until exercised. JT has applied the accounting standard for stock options to those granted on and after May 1, 2006.

t) Retirement Allowances for Directors and Corporate Auditors

Retirement allowances for directors and corporate auditors are recorded to state the liability at the amount that would be required if all directors and corporate auditors retired at each balance sheet date.

u) Provision for Loss on Debt guarantees

Possible losses arose from debt guarantees are provided based on the financial position of guaranteed parties.

v) New Accounting Pronouncements

Asset Retirement Obligations—

In March 2008, the ASBJ published a new accounting standard for asset retirement obligations, ASBJ Statement No. 18 "Accounting Standard for Asset Retirement Obligations" and ASBJ Guidance No. 21 "Guidance on Accounting Standard for Asset Retirement Obligations." Under this accounting standard, an asset retirement obligation is defined as a legal obligation imposed either by law or contract that results from the acquisition, construction, development and the normal operation of a tangible fixed asset and is associated with the retirement of such tangible fixed asset.

The asset retirement obligation is recognized as the sum of the discounted cash flows required for the future asset retirement and is recorded in the period in which the obligation is incurred if a reasonable estimate can be made. If a reasonable estimate of the asset retirement obligation cannot be made in the period the asset retirement obligation is incurred, the liability should be recognized when a reasonable estimate of asset retirement obligation can be made. Upon initial recognition of a liability for an asset retirement obligation, an asset retirement cost is capitalized by increasing the carrying amount of the related fixed asset by the amount of the liability. The asset retirement cost is subsequently allocated to expense through depreciation over the remaining useful life of the asset. Over time, the liability is accreted to its present value each period. Any subsequent revisions to the timing or the amount of the original estimate of undiscounted cash flows are reflected as an increase or a decrease in the carrying amount of the liability and the capitalized amount of the related asset retirement cost. This standard is effective for fiscal years beginning on or after April 1, 2010 with early adoption permitted for fiscal years beginning on or before March 31, 2010.

Segment Information Disclosures—

In March 2008, the ASBJ revised ASBJ Statement No. 17 "Accounting Standard for Segment Information Disclosures" and issued ASBJ Guidance No. 20 "Guidance on Accounting Standard for Segment Information Disclosures." Under the standard and guidance, an entity is required to report financial and descriptive information about its reportable segments. Reportable segments are operating segments or aggregations of operating segments that meet specified criteria. Operating segments are components of an entity about which separate financial information is available and such information is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. Generally, segment information is required to be reported on the same basis as is used internally for evaluating operating segment performance and deciding how to allocate resources to operating segments. This accounting standard and the guidance are applicable to segment information disclosures for the fiscal years beginning on or after April 1, 2010.

Business Combinations—

In December 2008, the ASBJ issued a revised accounting standard for business combinations, ASBJ Statement No. 21, "Accounting Standard for Business Combinations." Major accounting changes under the revised accounting standard are as follows;

(1) The current accounting standard for business combinations allows companies to apply the pooling of interests method of accounting when certain specific criteria are met such that the business combination is essentially regarded as a uniting-of-interests. The revised standard requires to account for such business combination by the purchase method and the pooling of interests method of accounting is no longer allowed.

(2) The current accounting standard accounts for the research and development costs to be charged to income as incurred. Under the revised standard, an in-process research and development (IPR&D) acquired by the business combination is capitalized as an intangible asset.

(3) The current accounting standard accounts for a bargain purchase gain (negative goodwill) to be systematically amortized within 20 years. Under the revised standard, the acquirer recognizes a bargain purchase gain in profit or loss on the acquisition date after reassessing whether it has correctly identified all of the assets acquired and all of the liabilities assumed with a review of such procedures used.

This standard is applicable to business combinations undertaken on or after April 1, 2010 with early adoption permitted for fiscal years beginning on or after April 1, 2009.

Unification of Accounting Policies Applied to Foreign Associated Companies for the Equity Method—
The current accounting standard requires to unify accounting policies within the consolidation group. However, the current guidance allows to apply the equity method for the financial statements of its foreign associated company which have been prepared in accordance with generally accepted accounting principles in their respective jurisdictions without unification of accounting policies.

In December 2008, the ASBJ issued ASBJ Statement No. 16 (Revised 2008), "Revised Accounting Standard for Equity Method of Accounting for Investments." The new standard requires adjustments to be made to conform the associate's accounting policies for similar transactions and events under similar circumstances to those of the parent company when the associate's financial statements are used in applying the equity method unless it is impracticable to determine adjustments. In addition, financial statements prepared by foreign associated companies in accordance with either International Financial Reporting Standards or the generally accepted accounting principles in the United States tentatively may be used in applying the equity method if the following items are adjusted so that net income is accounted for in accordance with Japanese GAAP unless they are not material:
(1) amortization of goodwill
(2) scheduled amortization of actuarial gain or loss of pensions that has been directly recorded in the equity
(3) expensing capitalized development costs of R&D
(4) cancellation of the fair value model accounting for property, plant, and equipment and investment properties and incorporation of the cost model accounting
(5) recording the prior years' effects of changes in accounting policies in the income statement where retrospective adjustments to the financial statements have been incorporated
(6) exclusion of minority interests from net income, if contained.

This standard is applicable to equity method of accounting for investments effective on or after April 1, 2010 with early adoption permitted for fiscal years beginning on or after April 1, 2009.

4. Business Combinations

I. Via consolidated subsidiary JTI (UK) MANAGEMENT LTD, on April 18, 2007, JT acquired the outstanding shares of the Gallaher Group Plc (now known as "Gallaher Group Ltd.") of the United Kingdom through an acquisition method under English law known as a scheme of arrangement, converting Gallaher Group Plc into a wholly owned subsidiary.

As the direct acquirer of the outstanding shares in Gallaher Group Plc was JTI (UK) MANAGEMENT LTD, which follows generally accepted accounting principles and practices in the United States ("U.S. GAAP"), the business combination was accounted for under the purchase method, based on FASB Statement No. 141.

In August 2007, JT reorganized JTI (UK) MANAGEMENT LTD into a subsidiary of JT International Holding B.V., a consolidated subsidiary of JT.

1. The following were the name of the acquired company, business contents, main reasons for business combination, the date of business combination, the legal form of the business combination, and ratio of voting rights acquired.
   (1) The name of acquired company: Gallaher Group Plc
   (2) Business contents: Manufacturing and selling of tobacco products
   (3) Main reasons for business combination
   Through the acquisition of the Gallaher Group Plc, JT could expand its business and enjoy economies of scale, build a well-balanced and competitive brand portfolio in each market and price segmentation, strengthen technology/distribution infrastructures, and synergize business growth expected by the business combination through effective business operations.
   (4) Date of business combination: April 18, 2007
   (5) Legal form of the business combination: The issued shares were acquired for cash.
   (6) Ratio of voting rights acquired: 100%
2. Period of operating results included in the consolidated financial statements:
   As the closing date of the accounting period of the acquired company is set on December 31, operating results from April 18, 2007 to December 31, 2007 for this company have been included in the current consolidated statement of income.
3. Acquisition costs
   The acquisition was conducted for 7.5 billion sterling pounds in cash.

4. Amount of goodwill recognized, basis for recognition, and method and period for amortization of goodwill
   (1) Amount of goodwill recognized:
   ¥1,721,368 million ($17,181 million)
   (2) Basis for recognition:
   Goodwill was recognized because the acquisition cost of the company exceeded the net value allocated to the assets acquired and liabilities assumed.
   (3) Method and period for amortization of goodwill:
   In accordance with FASB Statement No. 142, "Goodwill and Other Intangible Assets," the amount of goodwill recognized shall not be amortized. Rather, the decision of whether to recognize impairment shall be made once each year, or each time an event occurs indicating that the fair value of goodwill has fallen below its book value.
5. Principal details of assets acquired and liabilities assumed on the day of the business combination were as follows:

Current assets:	¥ 410,572 million	($ 4,098 million)
Non-current assets:	¥2,531,125 million	($25,263 million)
Total assets:	¥2,941,697 million	($29,361 million)
Current liabilities:	¥ 405,712 million	($ 4,049 million)
Non-current liabilities:	¥ 749,479 million	($ 7,481 million)
Total liabilities:	¥1,155,191 million	($11,530 million)

Regarding allocation of acquisition costs, the major intangible asset that was acquired in addition to goodwill was ¥523,263 million ($5,223 million) in trademarks. This asset has an amortization period of 20 years.

Note: Amount of yen mentioned above is translated at the exchange rate as of the business combination date. The amount of goodwill (¥1,791,189 million ($17,878 million)) included in non-current assets differs from the amount of goodwill which is described in consolidated balance sheet.

II. On January 8, 2008, JT converted Katokichi Co., Ltd. (now known as TableMark Co., Ltd.) into a subsidiary through tender offer for Katokichi shares.

In addition, JT acquired all of Katokichi's voting rights on April 18, 2008.

1. The following were the name of the acquired company, business contents, main reasons for business combination, the date of business combination, the legal form of the business combination, and ratio of voting rights acquired.
   (1) The name of acquired company: Katokichi Co., Ltd.
   (2) Business contents: The main business contents are manufacturing and selling of frozen foods and frozen fishery products. The other business contents are a distribution business incidental to the main business and a service business such as a hotel and restaurant management.
   (3) Main reasons for business combination
   JT anticipated that the Group could realize further expansion of its business value because the Group would enjoy the effect of mutual reinforcement and management resources synergy through the business combination.
   (4) Date of business combination: January 8, 2008
   (5) Legal form of the business combination: The issued shares were acquired for cash.
   (6) Ratio of voting rights acquired: 93.89%
2. Period of operating results included in the consolidated financial statements
   From January 1, 2008 to March 31, 2008
3. Acquisition costs
   The acquisition was conducted for ¥108.6 billion ($1,084 million) in cash.
4. Amount of goodwill recognized, basis for recognition, and method and period for amortization of goodwill
   (1) Amount of goodwill recognized ¥41,885 million ($418 million)
   (2) Basis for recognition
   Goodwill was recognized because the acquisition cost of the company exceeded the net value allocated to the assets acquired and liabilities assumed.
   (3) Method and period for amortization of goodwill
   Method for amortization: straight-line method
   Period for amortization: five years
5. Principal details of assets acquired and liabilities assumed on the day of the business combination were as follows:

Current assets:	¥ 89,279 million	($ 891 million)
Non-current assets:	¥136,995 million	($1,367 million)
Total assets:	¥226,274 million	($2,258 million)
Current liabilities:	¥ 84,813 million	($ 847 million)
Non-current liabilities:	¥ 24,532 million	($ 244 million)
Total liabilities:	¥109,345 million	($1,091 million)

	Millions of Yen	Millions of U.S. dollars
Assets acquired and liabilities assumed in acquisition of shares of Gallaher Group plc. and Katokichi Co., Ltd mainly consist of purchase of shares of newly consolidated subsidiaries, net of cash acquired in 2008;		
Current assets	**¥ 499,851**	**$ 4,989**
Non-current assets	**835,046**	**8,335**
Goodwill	**1,833,074**	**18,296**
Current liabilities	**(490,525)**	**(4,897)**
Non-current liabilities	**(774,011)**	**(7,726)**
Minority interest	**(11,530)**	**(115)**
Foreign currency translation adjustment	**(47,824)**	**(477)**
Acquisition price in 2007	**(166,312)**	**(1,660)**
Acquisition price in 2008	**1,677,769**	**16,745**
Cash and cash equivalents	**(69,680)**	**(695)**
Payments for purchases of shares of subsidiaries	**1,608,089**	**16,050**

III. Transactions under Common Control during the year ended March 31, 2009

1. Outline of the transactions
   (1) Transferred business: Processed food business (excluding chilled processed food business) and seasoning business of JT
   (2) Description of transferred business: Mainly manufacturing and sales of processed frozen foods and seasoning product
   (3) Legal form of the business combination: Business transfer of JT's processed food business and seasoning business, and stock transfer of affiliated companies including JT Foods, and consolidated subsidiaries
   (4) Name of the company after business combinations: Katokichi Co., Ltd. (now known as TableMark Co., Ltd.)
   (5) Outline and purpose of the transactions:
   The business combination enables the group to integrate JT's food business head office function and affiliated companies which are engaged with processed food business and seasoning business into Katokichi. After the combination, Katokichi holds the processed food business including the largest scale of frozen food business in Japan and seasoning business with leading manufacturing capability. Katokichi keeps implementing a business restructuring and setting up further business fundamentals.
2. Overview of accounting methods used
   These business combinations are accounted as transactions under common control with "Accounting for Business Combinations" issued by the Business Accounting Council ("BAC") on October 31, 2003, and "Guidance for Accounting Standard for Business Combinations and Business Divestitures" (ASBJ Guidance No. 10 updated on November 15, 2007).

5. Short-term Investments and Investment Securities

Short-term investments and investment securities at March 31, 2009 and 2010 consisted of the following:

	Millions of yen		Millions of U.S. dollars
	2009	**2010**	**2010**
Short-term investments:			
Time deposits	¥ 713	**¥ 7,856**	**$ 84**
Government and Corporate bonds	1,700	**4,698**	**50**
Trust fund investments and other	197	**472**	**6**
Total	¥ 2,610	**¥13,026**	**$140**
Investment securities:			
Equity securities	¥54,217	**¥51,147**	**$550**
Government and Corporate bonds	4,137	**3,300**	**35**
Trust fund investments and other	8,141	**5,731**	**62**
Total	¥66,495	**¥60,178**	**$647**

The costs and aggregate fair values of marketable securities at March 31, 2009 and 2010 were as follows:

				Millions of yen
				2009
	Cost	Unrealized gain	Unrealized loss	Fair value
Available-for-sale				
Equity securities	¥35,334	¥19,286	¥5,105	¥49,515
Government and Corporate bonds	4,124	108	3	4,229
Trust fund investments and other	8,083	—	535	7,548
Held-to-maturity				
Government bonds and municipal bonds	600	1	—	601

				Millions of yen
				2010
	Cost	Unrealized gain	Unrealized loss	Fair value
Available-for-sale				
Equity securities	**¥29,070**	**¥19,755**	**¥1,874**	**¥46,951**
Government and Corporate bonds	**7,583**	**128**	**13**	**7,698**
Trust fund investments and other	**4,641**	**1,048**	**108**	**5,581**
Held-to-maturity				
Government bonds and municipal bonds	**300**	**0**	**—**	**300**

				Millions of U.S. dollars
				2010
	Cost	Unrealized gain	Unrealized loss	Fair value
Available-for-sale				
Equity securities	**$312**	**$213**	**$20**	**$505**
Government and Corporate bonds	**81**	**1**	**0**	**82**
Trust fund investments and other	**50**	**11**	**1**	**60**
Held-to-maturity				
Government bonds and municipal bonds	**3**	**0**	**—**	**3**

Available-for-sale securities whose fair value cannot be reliably determined at March 31, 2009 and 2010 were as follows:

	Millions of yen		Millions of U.S. dollars
	2009	**2010**	**2010**
Available-for-sale			
Equity securities	¥4,702	**¥4,196**	**$45**
Corporate bonds	1,007	**—**	**—**
Trust fund investments and other	791	**622**	**7**
Total	¥6,500	**¥4,818**	**$52**

Amortized cost of held-to-maturity securities and related proceeds from sales and related realized losses on those sales for the years ended March 31, 2008, 2009 and 2010, were as follows:

	Millions of yen			Millions of U.S. dollars
	2008	2009	**2010**	**2010**
Amortized cost	¥300	¥—	**¥—**	**$—**
Proceeds from sales	¥293	¥—	**¥—**	**$—**
Net realized loss	¥ (7)	¥—	**¥—**	**$—**

A domestic consolidated subsidiary sold held-to-maturity security for the year ended March 31, 2008 due to significant deterioration in the issuer's creditworthiness, which is considered to be a reasonable reason consistent with Practical Guidelines on Accounting Standards for Financial Instruments No. 83-1.

Proceeds from sales of available-for-sale securities and related gross realized gains and losses on those sales, computed on the moving average cost basis for the years ended March 31, 2008, 2009 and 2010, were as follows:

	Millions of yen			Millions of U.S. dollars
	2008	2009	**2010**	**2010**
Proceeds from sales	¥1,902	¥2,719	**¥12,962**	**$139**
Gross realized gains	¥ 566	¥ 220	**¥ 3,683**	**$ 40**
Gross realized losses	(43)	(48)	**(1,939)**	**(21)**
Net realized gain	¥ 523	¥ 172	**¥ 1,744**	**$ 19**

For the years ended March 31, 2008, 2009 and 2010, losses on write-downs of securities including investments in affiliated companies totaled ¥11,154 million, ¥7,062 million and ¥1,404 million ($15 million), respectively. In evaluating security values, a security, whose value has declined by more than 50% is considered to have experienced "significant deterioration." A security whose value has declined from 30% to 50% and the effect of the decline on JT's financial position is material, is considered to have experienced "significant deterioration." If a security has a strong chance of regaining its value, the security is not written down.

The carrying value of short-term investments and investment securities by contractual maturities at March 31, 2010 were as follows:

	Millions of yen			Millions of U.S. dollars		
	Time deposits	Held-to-Maturity	Available for Sale	Time deposits	Held-to-Maturity	Available for Sale
Due within one year	**¥7,856**	**¥300**	**¥4,870**	**$84**	**$3**	**$53**
Due after one year through five years	**—**	**—**	**2,501**	**—**	**—**	**27**
Due after five years through ten years	**—**	**—**	**10**	**—**	**—**	**0**
Due after ten years	**—**	**—**	**—**	**—**	**—**	**—**
Total	**¥7,856**	**¥300**	**¥7,381**	**$84**	**$3**	**$80**

6. Inventories

Inventories at March 31, 2009 and 2010 consisted of the following:

	Millions of yen		Millions of U.S. dollars
	2009	**2010**	**2010**
Leaf tobacco	¥294,020	**¥359,152**	**$3,860**
Finished products	88,234	**123,327**	**1,326**
Other	81,903	**72,621**	**780**
Total	¥464,157	**¥555,100**	**$5,966**

Prior to adoption of ASBJ Statement No. 9," Accounting Standard for Measurement of Inventories" JT leaf tobacco inventory in excess of the minimum amount necessary for future production was subject to annual devaluation.

Annual devaluation was discontinued beginning in the year ended March 31, 2007. Effective from April 1, 2007, JT and its domestic subsidiaries applied the "Accounting Standard for Measurement of Inventories" (see Note 3 (f)).

7. Investment Property

JT and certain consolidated subsidiaries hold some rental properties such as office buildings and residences in Tokyo and other areas.

The carrying amounts, changes in such balances and market prices of such properties were as follows:

				Millions of yen
	Carrying amount			Fair value
Use application	April 1, 2009	Increase/ (Decrease)	**March 31, 2010**	**March 31, 2010**
Office buildings for rent	¥41,506	¥ (2,420)	**¥39,086**	**¥140,606**
Residences for rent	5,279	(143)	**5,136**	**26,738**
Others	29,271	(10,951)	**18,320**	**66,774**
Total	¥76,056	¥(13,514)	**¥62,542**	**¥234,118**

				Millions of U.S. dollars
	Carrying amount			Fair value
Use application	April 1, 2009	Increase/ (Decrease)	**March 31, 2010**	**March 31, 2010**
Office buildings for rent	$446	$ (26)	**$420**	**$1,511**
Residences for rent	57	(2)	**55**	**287**
Others	314	(117)	**197**	**718**
Total	$817	$(145)	**$672**	**$2,516**

Notes:

1) Carrying amount is net of accumulated depreciation and accumulated impairment losses, if any.

2) Decrease during the fiscal year ended March 31, 2010 primarily represents the sales of domestic idle properties of ¥11,214 million ($121 million).

3) Fair value of investment properties at March 31, 2010 is principally measured based on the real-estate appraisal assessed by the external real-estate appraiser. And the others are measured by the Group based on the assessed value of taxable fixed asset. However, unless the appraisal or indicators that are regarded to reflect the fair value of the investment properties appropriately change significantly since the date of acquisition or the date of the latest appraisal, the Group measure the fair value of the investment properties based on such appraisal or indicators.

The income and expenses for the investment properties for the year ended March 31, 2010 were as follows:

				Millions of yen
Use application	Income	Expense	Net gain/(loss)	Other income/ (expense)
Office buildings for rent	¥11,546	¥5,179	¥6,367	¥ (44)
Residences for rent	1,512	502	1,010	(21)
Others	2,942	3,329	(387)	21,768
Total	¥16,000	¥9,010	¥6,990	¥21,703

				Millions of U.S. dollars
Use application	Income	Expense	Net gain/(loss)	Other income/ (expense)
Office buildings for rent	$124	$56	$68	$ 0
Residences for rent	16	5	11	0
Others	32	36	(4)	233
Total	$172	$97	$75	$233

The expenses above primarily consist of depreciation, repairs and maintenance expenses, insurance expense and fixed assets tax of each investment property.

8. Short-term Bank Loans, Commercial Paper and Long-term Debt

Short-term bank loans and commercial paper at March 31, 2009 and 2010 consisted of the following:

	Millions of yen		Millions of U.S. dollars
	2009	2010	2010
Yen loans with interest rates of 0.216% to 2.750% at March 31, 2009 and of 0.090% to 3.500% at March 31, 2010	¥ 51,444	**¥ 48,929**	**$ 526**
Foreign currency loans with interest rates of 0.130% to 83.000% at March 31, 2009 and of 1.040% to 27.250% at March 31, 2010	61,787	**60,334**	**648**
Commercial paper with interest rates of 0.106% to 0.145% at March 31, 2010	—	**119,000**	**1,279**
Total	¥113,231	**¥228,263**	**$2,453**

Long-term debt at March 31, 2009 and 2010 consisted of the following:

	Millions of yen		Millions of U.S. dollars
	2009	2010	2010
1.98% yen bonds, due 2009	¥ 150,000	**¥ —**	**$ —**
1.34% yen bonds, due 2010	49,998	**50,000**	**537**
1.53% yen bonds, due 2011	40,000	**40,000**	**430**
1.68% yen bonds, due 2012	59,996	**59,997**	**645**
1.13% yen bonds, due 2014	—	**100,000**	**1,075**
Unsecured 6.63% Sterling pound bonds issued by foreign subsidiary due in 2009	39,523	**—**	**—**
Unsecured 4.63% Euro bonds issued by foreign subsidiary due in 2011	102,673	**105,829**	**1,137**
Unsecured 5.75% Sterling pound bonds issued by foreign subsidiary due in 2013	32,733	**36,514**	**392**
Unsecured 4.50% Euro bonds issued by foreign subsidiary due in 2014	63,974	**66,055**	**710**
Other bonds	1,261	**1,013**	**12**
Long-term bank loans due through 2028	325,944	**172,594**	**1,855**
Lease obligations due through 2019	16,746	**14,064**	**151**
Total	882,848	**646,066**	**6,944**
Less current portion	(222,256)	**(78,356)**	**(842)**
Long-term debt, less current portion	¥ 660,592	**¥567,710**	**$6,102**

The weighted average interest rates for long-term lease obligations outstanding at March 31, 2009 and 2010 were 12.97% and 6.77%, respectively, and those for current portion were 8.16% and 8.95%, respectively.

JT entered into interest rate swap agreements in March 2004 to convert interest payments on 1.98% yen bonds due 2009 to floating rate payments on a LIBOR basis, which was at 1.24% at March 31 2005, in order to manage interest rate risks on these bonds. Taking changes in market conditions into consideration, JT unwound the above interest swap agreements in May 2005. Consequently, JT paid a fixed rate interest of 1.61%.

In addition, certain domestic consolidated subsidiaries have entered into interest rate swap agreements to fix variable rate interest payments of Japanese yen loans.

Annual interest rates applicable to Japanese yen long-term loans of JT and certain domestic consolidated subsidiaries at March 31, 2009 and 2010 ranged from 0.77% to 5.30% and 0.90% to 5.30%, respectively.

Annual interest rates applicable to long-term loans denominated in foreign currencies outstanding at March 31, 2009 and 2010 ranged from 2.35% to 8.00% and 0.97% to 8.75%, respectively.

Annual maturities of short-term bank loans, commercial paper and long-term debt at March 31, 2010 were as follows:

Years Ending March 31,	Millions of yen	Millions of U.S. dollars
2011	**¥306,525**	**$3,295**
2012	**172,228**	**1,851**
2013	**166,974**	**1,795**
2014	**59,149**	**636**
2015	**168,558**	**1,812**
2016 and thereafter	**873**	**8**
Total	**¥874,307**	**$9,397**

Under the JT Law, obligations created by the bonds issued by JT are secured by a statutory preferential right over the property of JT.

This right entitles the holders thereof to claim satisfaction in preference to unsecured creditors (with the exception of national and local taxes and certain other statutory obligations).

Substantially all of the short-term bank loans, commercial paper and long-term debt are unsecured. Secured loans and debt of certain consolidated subsidiaries at March 31, 2010 were as follows:

	Millions of yen	Millions of U.S. dollars
Short-term bank loans	**¥10,862**	**$117**
Long-term bank loans	**5,281**	**57**
Current portion of Long-term bank loans	**1,756**	**19**
Others	**420**	**4**
Total	**¥18,319**	**$197**

The carrying amounts of assets pledged as collateral for the above secured loans and debt at March 31, 2010 were as follows:

	Millions of yen	Millions of U.S. dollars
Buildings and structures	**¥ 5,821**	**$ 63**
Land	**4,316**	**46**
Machinery, equipment and vehicles	**2,447**	**26**
Others	**4,492**	**49**
Total	**¥17,076**	**$184**

General agreements with respective banks provide, as is customary in Japan, that additional collateral must be provided under certain circumstances if requested by such banks and that certain banks have the right to offset cash deposited with them against any long-term or short-term debt or other debt payable to the banks. JT has never been requested to provide additional collateral.

9. Liabilities for Retirement Benefits

(1) Employees' Retirement Benefit

JT has unfunded severance indemnity plan and a cash balance pension plan as well as a defined contribution plan.

The unfunded severance indemnity plan provides lump-sum retirement benefits based on credits earned in each year of service.

Employees are entitled to receive larger payments in certain circumstances such as involuntary termination, retirement at the mandatory retirement age, voluntary termination at certain specific ages prior to mandatory retirement age or death.

The cash balance pension plan provides retirement benefits in the form of a lump-sum payment or annuity payments based on current and past principal credits earned and interest credits over time based on these principal credits.

Domestic consolidated subsidiaries principally have unfunded severance indemnity plans and/or defined benefit pension plans covering substantially all of their employees, under which benefits are provided based on the rate of pay at the time of termination, years of service and certain other factors.

Foreign consolidated subsidiaries principally sponsor non-contributory defined benefit pension plans covering most of their employees. Plans covering regular full-time employees provide pension benefits based on credits, determined by age, earned throughout an employee's service and final average compensation before retirement.

Certain foreign consolidated subsidiaries also provide certain health and life insurance benefits for retired employees and their dependents.

The liabilities for employees' retirement benefits at March 31, 2009 and 2010 consisted of the following:

	Millions of yen		Millions of U.S. dollars
	2009	**2010**	**2010**
Projected benefit obligations	¥(424,413)	**¥(455,264)**	**$(4,893)**
Fair value of plan assets	280,513	**321,317**	**3,453**
Funded status	(143,900)	**(133,947)**	**(1,440)**
Unrecognized actuarial net loss	44,997	**42,196**	**454**
Unrecognized prior service cost	6,204	**4,790**	**51**
Net amount recognized	(92,699)	**(86,961)**	**(935)**
Pension liability adjustment of foreign consolidated subsidiaries (see Note 3 (q))	(25,662)	**(35,742)**	**(384)**
Prepaid pension cost	(27,642)	**(23,391)**	**(251)**
Other current liabilities	(5,136)	**(3,721)**	**(40)**
Liabilities for employees' retirement benefits	¥(140,867)	**¥(142,373)**	**$(1,530)**

"Pension liability adjustment of foreign consolidated subsidiaries" is the unfunded obligation recognized by foreign consolidated subsidiaries applying U.S. GAAP. "Other current liabilities" is the amount by which the actuarial present value of benefits included in the benefit obligation payable in the next 12 months exceeds the fair value of plan assets in foreign consolidated subsidiaries applying U.S. GAAP.

JT transferred a portion of the unfunded severance indemnity plan to the defined contribution plan on April 1, 2006, and thereby recognized ¥3,097 million for the year ended March 31, 2006 as other expense which led to an increase of liabilities for retirement benefits by the same amount in accordance with "Accounting for the Transfer between Retirement Benefits Plans (ASBJ Guideline No. 1)" and "Practical Solution on Accounting for Transfer Between Retirement Benefit Plans (Practical Issues Task Forces Report No. 2)."

	Millions of yen
	2006
Settlement of projected benefit obligations	¥ 4,567
Prior service cost recognized in earnings	(199)
Actuarial gain recognized in earnings	139
Decrease in liabilities for retirement benefits	4,507
Related assets due to be transferred to defined contribution plan	(7,604)
Loss on partial termination of defined benefit plan	¥(3,097)

Related assets of ¥7,604 million due to be transferred to the defined contribution plan were eventually paid in installment by 2010.

The components of net periodic retirement benefit cost for the years ended March 31, 2008, 2009 and 2010 were as follows:

	Millions of yen			Millions of U.S. dollars
	2008	2009	**2010**	**2010**
Service cost	¥ 13,115	¥ 13,123	**¥ 11,294**	**$ 121**
Interest cost	20,149	21,720	**18,090**	**194**
Expected return on plan assets	(19,782)	(20,133)	**(12,902)**	**(139)**
Recognized actuarial loss	(430)	748	**3,876**	**42**
Amortization of prior service cost	1,530	1,256	**1,744**	**20**
Net periodic retirement benefit costs	¥ 14,582	¥ 16,714	**¥ 22,102**	**$ 238**

Significant assumptions used for the years ended March 31, 2008, 2009 and 2010 were as follows:

Year ended March 31, 2008		Japan	Overseas
Discount rate	principally	2.5%	principally between 3.5% and 5.6%
Expected rate of return on plan assets	principally	2.5%	principally between 5.5% and 7.0%
Amortization period of prior service cost	principally	10 years	principally between 10 years and 14 years
Recognition period of actuarial gain/loss	principally	10 years	principally between 7 years and 22 years

Year ended March 31, 2009		Japan	Overseas
Discount rate	principally	2.5%	principally between 3.3% and 6.3%
Expected rate of return on plan assets	principally	2.5%	principally between 4.3% and 6.0%
Amortization period of prior service cost	principally	10 years	principally between 7 years and 10 years
Recognition period of actuarial gain/loss	principally	10 years	principally between 7 years and 15 years

Year ended March 31, 2010		Japan	Overseas
Discount rate	**principally**	**2.5%**	**principally between 3.0% and 5.8%**
Expected rate of return on plan assets	**principally**	**2.5%**	**principally between 4.5% and 6.2%**
Amortization period of prior service cost	**principally**	**10 years**	**principally between 6 years and 10 years**
Recognition period of actuarial gain/loss	**principally**	**10 years**	**principally between 5 years and 19 years**

Actuarial gains or losses that result from changes in plan experience and actuarial assumptions are principally amortized over the employees' average remaining service period from the next fiscal year. The prior service cost that resulted from retroactive application of a plan amendment is principally amortized over the employees' average remaining service period. The retirement benefit attributable to each year is calculated by assigning the same amount of pension benefits to each year of service. In determining service cost, certain foreign subsidiaries attribute benefits to periods of service under the plan's benefit formula.

The Group's contributions to the defined contribution plans which were charged to expenses for the years ended March 31, 2008, 2009 and 2010 were ¥4,208 million, ¥ 3,948 million and ¥5,680 million ($61 million), respectively.

Certain domestic and foreign subsidiaries provided additional retirement benefits for early-retired employees in connection with the rationalization of the Domestic and International tobacco businesses for the years ended March 31, 2008, 2009 and 2010.

These restructuring activities resulted in recognition of additional retirement benefits as business restructuring costs of ¥2,285 million, ¥2,691 million and ¥7,288 million ($78 million) for the years ended March 31, 2008, 2009 and 2010, respectively, and as other expenses of ¥1,122 million, ¥32 million and ¥1,235 million ($13 million) for the years ended March 31, 2008, 2009 and 2010, respectively, which included a one-time charge for the unrecognized actuarial net loss and unrecognized prior service cost attributable to the employees who retired earlier than expected.

Certain domestic consolidated subsidiaries participate in multi-employer contributory pension plans, the required contributions to which are recognized as a net pension cost for the year. Of these pension plans, information about Tokyo pharmaceutical industry employees' pension funds for the years ended March 31, 2008 and 2009 were as follows:

	Millions of yen		Millions of U.S. dollars
	2008	2009	2009
Fair value of plan assets	¥ 415,833	¥ 325,177	$ 3,495
Benefit obligations	(497,473)	(502,794)	(5,404)
Deficit	¥ (81,640)	¥(177,617)	$(1,909)

	2009	**2010**
Proportion of the Domestic consolidated subsidiary's contributions to the entire plan	1.2%	**1.3%**

(2) Obligation Under the Public Official Mutual Assistance Association Law

Employees of JT, including former employees of JTSPC and others are entitled to receive benefits under the government-sponsored pension plan by the Public Official Mutual Assistance Association Law (the "Law"). The benefits, in the form of lifetime annuity payments by the Social Insurance Agency, are determined based on the standard pay rate, the length of service and other factors.

As a formerly wholly government-owned company, JT is obligated by the Law to reimburse the Japanese government for pension expenses incurred each year by the government in respect of former employees of JTSPC and others for their services during certain periods before July 1, 1956, the enactment date of the Law.

Such obligations were first recorded as liabilities at April 1, 2003 based on the actuarially determined computation method. Any actuarial gain or loss arising subsequent to April 1, 2003 is deferred and amortized over 10 years.

The liabilities and costs recognized for such obligations as of and for the year ended March 31, 2008, 2009 and 2010 were as follows:

	Millions of yen		Millions of U.S. dollars
	2009	**2010**	**2010**
Benefit obligations	¥(116,890)	**¥(106,346)**	**$(1,143)**
Unrecognized actuarial (gain) loss	(1,389)	**(3,184)**	**(34)**
Liabilities recognized	¥(118,279)	**¥(109,530)**	**$(1,177)**

	Millions of yen			Millions of U.S. dollars
	2008	2009	**2010**	**2010**
Interest cost	¥2,094	¥1,918	**¥1,753**	**$19**
Recognized actuarial (gain) loss	240	107	**(28)**	**0**
Net periodic costs	¥2,334	¥2,025	**¥1,725**	**$19**

The assumed discount rate used in the actuarial computation for the year ended March 31, 2008, 2009 and 2010 was 1.5%.

(3) Retirement Allowances for Directors and Corporate Auditors

The Domestic Group's liabilities for retirement benefits for directors and corporate auditors as of March 31, 2008, 2009 and 2010 were ¥744 million, ¥624 million and ¥764 million ($8 million), respectively.

10. Equity

Japanese companies are subject to the Companies Act. The significant provisions in the Companies Act that affect financial and accounting matters are summarized below:

(a) Dividends

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

Semiannual interim dividends may also be paid once a year upon resolution by the Board of Directors if the articles of incorporation of the company so stipulate. The Companies Act provides certain limitations on the amounts available for dividends or the purchase of treasury stock.

(b) Increases/decreases and transfer of common stock, reserve and surplus

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

(c) Treasury stock

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

The Special Taxation Measures Law in Japan permits companies to take as tax deductions certain reserves if provided through year-end book closing. Under Japanese tax laws, these reserves must be reversed to income in future years. The deferred gain on sales of fixed assets, net of tax, included in retained earnings provided under the Special Taxation Measures Law at March 31, 2009 and 2010 was ¥47,969 million and ¥43,446 million ($467 million), respectively.

11. Stock Options

Stock option expense that was accounted for as Selling, general and administrative expenses on the consolidated statement of income for the years ended March 31, 2008, 2009 and 2010 amounted to ¥186 million, ¥179 million and ¥210 million ($2 million), respectively.

The stock options outstanding as of March 31, 2010 were as follows:

Stock Option	Persons Granted	Number of Options Granted	Date of Grant	Exercise Price	Service Period Covered	Exercise Period
2008 stock option	11 Directors 16 Executive officers	426 shares	January 8, 2008	¥1 ($0.01)	From June 22, 2007 to June 24, 2008	From January 9, 2008 to January 8, 2038
2009 stock option	11 Directors 14 Executive officers	547 shares	October 6, 2008	¥1 ($0.01)	From June 24, 2008 to June 23, 2009	From October 7, 2008 to October 6, 2038
2010 stock option	9 Directors 14 Executive officers	1,153 shares	October 13, 2009	¥1 ($0.01)	From June 23, 2009 to June 24, 2010	From October 14, 2009 to October 13, 2039

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The rights become exercisable from one year later when a holder no longer holds a position as a director, a corporate auditor or an executive officer.

The stock option activity was as follows:

	2008 stock option	2009 stock option	2010 stock option
For the year ended March 31, 2009			
Non-Vested	(Shares)	(Shares)	
March 31, 2008—Outstanding	106	—	
Granted	—	547	
Canceled	—	—	
Vested	(106)	(410)	
March 31, 2009—Outstanding	—	137	
Vested			
March 31, 2008—Outstanding	320	—	
Vested	106	410	
Exercised	—	—	
Canceled	—	—	
March 31, 2009—Outstanding	426	410	
For the year ended March 31, 2010			
Non-Vested	(Shares)	(Shares)	**(Shares)**
March 31, 2009—Outstanding	—	137	**—**
Granted	—	—	**1,153**
Canceled	—	—	**—**
Vested	—	(137)	**(865)**
March 31,2010—Outstanding	—	—	**288**
Vested			
March 31, 2009—Outstanding	426	410	**—**
Vested	—	137	**865**
Exercised	(17)	—	**—**
Canceled	—	—	**—**
March 31, 2010—Outstanding	409	547	**865**
Exercise price	¥1	¥1	**¥1**
	($0.01)	($0.01)	**($0.01)**
Average stock price at exercise	¥272,959	—	**—**
Fair value price at the grant date	¥581,269	¥285,904	**¥197,517**
			($2,123)

The assumptions used to measure fair value of 2010 stock options were as follows:

	2010 stock option
Estimate Method	Black-Scholes option pricing model
Volatility of stock price*[1]	34.536%
Estimated remaining outstanding period*[2]	15 years
Estimated dividend*[3]	¥5,400 per share ($58 per share)
Interest rate with risk free*[4]	1.778%

*[1] Calculated based on stock prices for the period on and after listing date (from October 27, 1994 to October 13, 2009)

*[2] Due to difficulty in reasonably estimating due to insufficient data accumulation, expected remaining period is estimated on the assumption that stock option would be exercised at a mid-point of exercising period.

*[3] Based on interim dividend and year-end dividend for the year 2009

*[4] A yield of 15-year government bond, a period of which corresponds to expected remaining period

12. Income Taxes

The Domestic Group is subject to Japanese corporate tax, inhabitants tax and enterprise tax based on income which, in the aggregate, resulted in a normal effective statutory tax rate of approximately 40.35% for the years ended March 31, 2008, 2009 and 2010. Foreign consolidated subsidiaries are subject to income taxes of the countries in which they operate.

The tax effects of significant temporary differences and loss carry-forwards which resulted in deferred tax assets and liabilities at March 31, 2009 and 2010 were as follows:

	Millions of yen		Millions of U.S. dollars
	2009	**2010**	**2010**
Deferred tax assets:			
Liabilities for employees' retirement benefits	¥ 55,718	**¥ 42,984**	**$ 462**
Obligations under the Public Official Mutual Assistance Association Law	47,726	**44,195**	**475**
Net operating loss carryforwards	42,855	**45,685**	**491**
Foreign currency exchange losses	26,558	**20,139**	**216**
Allowance for doubtful accounts	16,330	**10,489**	**113**
Other	99,558	**73,256**	**787**
Less valuation allowance	(64,920)	**(74,102)**	**(796)**
Total	223,825	**162,646**	**1,748**
Deferred tax liabilities:			
Deferred gain on sales of fixed assets for income tax purposes	(32,360)	**(26,306)**	**(283)**
Basis differences in assets acquired and liabilities assumed upon acquisition	(73,387)	**(72,287)**	**(777)**
Prepaid pension cost	(10,227)	**(8,783)**	**(94)**
Other	(62,694)	**(40,214)**	**(432)**
Total	(178,668)	**(147,590)**	**(1,586)**
Net deferred tax assets (liabilities)	¥ 45,157	**¥ 15,056**	**$ 162**

Net deferred tax assets and liabilities at March 31, 2009 and 2010 were reflected on the accompanying consolidated balance sheets under the following captions:

	Millions of yen		Millions of U.S. dollars
	2009	**2010**	**2010**
Other current assets	¥ 29,675	**¥ 26,615**	**$ 286**
Deferred tax assets	128,787	**85,376**	**918**
Other current liabilities	(2,915)	**(2,357)**	**(25)**
Deferred tax liabilities	(110,390)	**(94,578)**	**(1,017)**
Net deferred tax assets (liabilities)	¥ 45,157	**¥ 15,056**	**$ 162**

A reconciliation between the normal effective statutory tax rate for the years ended March 31, 2008, 2009 and 2010 and the actual effective tax rate reflected in the accompanying consolidated statements of income was as follows:

	2008	2009	**2010**
Normal effective statutory tax rate	40.35%	40.35%	**40.35%**
Tax rate difference applied for foreign consolidated subsidiaries	(9.67)	(12.60)	**(6.90)**
Non-deductible expenses	2.34	3.77	**1.95**
Amortization of goodwill	0.48	10.05	**8.81**
Increase in valuation allowance	7.26	5.42	**6.10**
Increase (reduction) of FIN48 liability, net	(1.51)	3.41	**1.14**
Increase (reduction) in enacted tax rates, net	(5.49)	(0.49)	**0.02**
Gain from the reversal of liability on a fine levied under the UK competition law	—	—	**(2.44)**
Other—net	0.69	1.58	**(1.47)**
Actual effective tax rate	34.45%	51.49%	**47.56%**

13. Research and Development Costs and Advertising Costs

Research and development costs charged to expenses as incurred for the years ended March 31, 2008, 2009 and 2010 were ¥45,163 million, ¥47,296 million and ¥49,645 million ($534 million), respectively.

Advertising costs were charged to expenses as incurred and totaled ¥186,607 million, ¥188,023 million and ¥165,684 million ($1,781 million) for the years ended March 31, 2008, 2009 and 2010, respectively.

14. Lease Transactions

The Group, as a lessee, leases certain vehicles, vending machines and other assets.

For the year ended March 31, 2008, the Group recorded an impairment loss of ¥14 million on certain leased property held under finance leases that do not transfer ownership and an allowance for impairment loss on leased property, which is included in current liabilities.

Pro forma information of leased property, such as depreciation expense and other information of finance lease that do not transfer ownership of the leased property to the lessee on an "as if capitalized" basis at March 31, 2008 was as follows:

	Millions of yen
	2008
Depreciation expense and other information:	
Depreciation expense	¥5,230
Lease payments	5,230
Reversal of allowance for impairment loss on leased property	1

Depreciation expenses, which were not reflected in the accompanying consolidated statements of income, were computed by the straight-line method.

The minimum rental commitments under noncancellable operating leases at March 31, 2009 and 2010 were as follows:

	Millions of yen		Millions of U.S. dollars
	2009	**2010**	**2010**
Due within one year	¥ 7,497	**¥ 7,362**	**$ 79**
Due after one year	24,020	**21,153**	**227**
Total	¥31,517	**¥28,515**	**$306**

15. Other Income (Expenses)

(1) Business Restructuring Costs

Business restructuring costs for the years ended March 31, 2008, 2009 and 2010 consisted of the following:

	Millions of yen			Millions of U.S. dollars
	2008	2009	**2010**	**2010**
Additional Retirement Benefits (see Note 9)	¥(2,285)	¥ (2,691)	**¥(7,288)**	**$ (78)**
Loss on disposition of property, plant and equipment	—	(404)	**(1,395)**	**(15)**
Others-net	(4,157)	(21,269)	**(1,217)**	**(13)**
Total	¥(6,442)	¥(24,364)	**¥(9,900)**	**$(106)**

Business restructuring costs were incurred in line with the business restructuring measures mainly for the rationalization of the Domestic and International tobacco businesses. Others-net for the year ended March 31, 2009 included a revision of the business model in the Philippines.

(2) Loss on Impairment of Long-lived Assets

Asset grouping is based on the smallest identifiable unit that generates cash flows that are largely independent of the cash flows from other assets, except for idle property, which is grouped individually.

Loss on Impairment for the years ended March 31, 2008, 2009 and 2010 amounted to ¥3,825 million, ¥16,365 million and ¥6,043 million ($65 million) respectively, which relates principally to land, and certain buildings and structures of company housing which are planned to be demolished.

The recoverable value of such assets was calculated mainly by its value in use, which was set at "nil."

(3) Other—net

"Other—net" included in "Other Income (Expenses)" for the years ended March 31, 2008, 2009 and 2010 consisted of the following:

	Millions of yen			Millions of U.S. dollars
	2008	2009	**2010**	**2010**
Financial support for domestic tobacco growers	¥ (2,005)	¥ (768)	**¥ (522)**	**$ (6)**
Foreign exchange loss—net	(31,790)	(21,802)	**(20,228)**	**(217)**
Equity in earnings of affiliates	1,773	2,370	**2,401**	**26**
Periodic costs from the Public Official Mutual Assistance Association liabilities (see Note 9)	(2,334)	(2,025)	**(1,725)**	**(19)**
Gain from the reversal of liability on a fine levied under the UK competition law	—	—	**16,710**	**180**
Expense for disposal of PCB-containing wastes	—	—	**(4,056)**	**(44)**
Introduction costs for vending machines with adult identification functions	(12,879)	(13,469)	**—**	**—**
Costs related to the recall of frozen foods products	(5,624)	—	**—**	**—**
Others—net	(12,490)	(11,883)	**1,676**	**18**
Total	¥(65,349)	¥(47,577)	**¥ (5,744)**	**$ (62)**

"Introduction costs for vending machines with adult identification functions" is the cost to establish the system of vending machines with functions to prevent minors from purchasing cigarettes from vending machines and to dispense cigarettes only after scanning and verifying special IC cards that indicate whether the purchaser is an adult or not.

"Costs related to the recall of frozen foods products" is mainly the cost to recall some frozen foods products which were imported and sold by the Group.

On April 16, 2010, Gallaher Group Ltd. (former Gallaher Group Plc) and Gallaher Ltd. (together, hereinafter, "Gallaher"), JT's tobacco business subsidiaries in the United Kingdom, received the decision from Office of Fair Trading ("OFT"), the UK competition authority, concluding that a fine of approximate 50 million sterling pound was levied to Gallaher for anti-competitive business practices relating to the retail pricing of tobacco products in the market during the period prior to JT's acquisition of Gallaher.

Approximate 164 million sterling pound in total, based on the company's assumption about the risk of fine being levied, had been booked as liabilities in the purchase price allocation related to JT's acquisition of Gallaher Group Plc (now Gallaher Group Ltd.) on April 18, 2007 and such liabilities had been included in Other current liabilities and Other non-current liabilities on the Consolidated Balance Sheets.

As the amount of fine decided by the OFT was lower than the liabilities which had been originally booked, the liability has been reversed to the amount of fine sentenced in the decision by the OFT, and consequently, the relevant variance of approximate 114 million sterling pound has been recognized and disclosed in the Other income on the Consolidated Statements of Income, which is presented "Gain from the reversal of liability on a fine levied under the UK competition law" in "Other—net."

16. Financial Instruments and Related Disclosures

(1) Policy for Financial Instruments

JT and major subsidiaries effectively raise necessary funds (for business operations) with mainly bank loans and bonds considering their business environment.

Cash surplus, if any, is invested in low risk and highly liquid financial instruments.

Derivatives are used, not for speculative nor trading purposes, but to manage risk exposure arising from business operations.

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

Receivables such as trade notes and accounts receivable are exposed to customer's credit risk. Receivables in foreign currencies are exposed to the market risk of fluctuation in foreign currency exchange rates.

Short-term investments and investment securities are mainly bonds for surplus investment and equities of customers and suppliers of the Group and those are exposed to the issuer's credit risk and market price fluctuation risk.

Payables such as trade notes and accounts payable in foreign currencies are exposed to the market risk of fluctuation in foreign currency exchange rates.

Bank loans, commercial paper and bonds issued by the Group are exposed to the liquidity risk that the Group would not be able to prepare funding to repay such debts due to deterioration of financial market.

Bank loans and bonds in variable interest rates are exposed to market risks of interest rate fluctuation and those in foreign currencies are exposed to the market risk of fluctuation in foreign currency exchange rates.

Derivatives mainly include foreign currency forward contracts to manage the market risk of fluctuation in foreign currency exchange rate related to future cashflow in foreign currency and interest rate swaps to manage the market risk of fluctuation interest rate related to interest payment for bank loans and bonds. These derivatives are exposed to counterparty's credit risk.

For hedging instruments, hedged items, hedging policies and assessment methods of effectiveness of hedging instruments, please see Note 17.

(3) Risk Management for Financial Instruments

Credit Risk Management

With respect to receivables, in order to control customer's credit risk, JT and its major subsidiaries set credit limits or payment terms to major customers based on the Credit Management Guideline in principle. In addition, receivable balance of each customer is constantly checked to reduce risk of customer's default. The Treasury Division of JT regularly monitors status of occurrence and collections of bad debts, and reports them to JT's Executive Committee.

To control credit risk related to surplus investment and derivatives, based on an internal guide line, JT and its major subsidiaries invest cash surplus into bonds and other financial instruments with a certain credit grade and have derivatives with counterparties which has high credit grade. In addition, the Treasury Division of JT regularly monitors such transactions and reports them to it's Executive Committee.

Foreign exchange risk management

In accordance with the internal guidelines, JT and its major subsidiaries, to reduce the market risk of fluctuation in foreign currency exchange rate mainly related to future cashflow in foreign currency, establishes foreign exchange hedging strategy based on the environment and the forecast of foreign exchange market. The foreign exchange hedging strategy is reviewed and approved by the Financial Risk Management Committee of JT and, based on which, the derivative transactions are originated. The Treasury Division of JT regularly reports such derivative transactions to the JT's Executive Committee.

Interest rate risk management

In accordance with the internal guidelines, JT and its major subsidiaries, to reduce the market risks of interest rate fluctuation related to bank loans and bonds, establishes interest rate hedging strategy based on the environment and the forecast of interest market. The interest rate hedging strategy is reviewed and approved by the Financial Risk Management Committee of JT and, based on which, derivative transactions are originated. The Treasury Division of JT regularly reports such derivative transactions to JT's Executive Committee.

Risk Management of market price fluctuation

With respect to short-term investments and investment securities, JT and its major subsidiaries regularly monitors prices and issuer's financial status. Except for held-to-maturity bonds, responsible divisions revise investment strategy if necessary by taking relationship with issuers into consideration.

Liquidity risk management (Liquidity risk comprises the risk that the Group cannot meet it's contractual obligations in full on maturity dates)

In accordance with the internal guidelines, JT and its major subsidiaries establishes finance plan based on the annual business plan and the Treasury Division of JT regularly monitors the balance of liquidity-in-hand and interest-bearing debts and reports them to JT's Executive Committee. In addition, JT and its major subsidiaries keep necessary credit facilities to manage liquidity risk, having commitment lines with several financial institutions.

(4) Fair Values of Financial Instruments

Fair values of financial instruments are based on quoted price in active markets. If quoted price is not available, other rational valuation techniques are used instead. The results of valuation may differ among assumptions because the rational valuation techniques include variable factors. Also please see Note 17 for the detail of fair value for derivatives.

(a) Fair values of financial instruments

	Millions of yen		
March 31, 2010	Carrying amount	Fair value	Unrecognized gain/loss
Cash and cash equivalents	**¥ 154,369**	**¥ 154,369**	**¥ —**
Trade notes and accounts receivable	**296,885**		
Allowance for doubtful accounts*1	**(2,860)**		
Subtotal	**294,025**	**294,025**	**—**
Short-term investments and Investment securities	**68,385**	**68,386**	**1**
Time deposits	**7,856**	**7,856**	**—**
Held-to-maturity securities	**300**	**301**	**1**
Available-for-sale securities	**60,229**	**60,229**	**—**
Total	**516,779**	**516,780**	**1**
Short-term bank loans	**109,263**	**109,263**	**—**
Commercial paper	**119,000**	**119,000**	**—**
Tobacco excise taxes payable	**307,795**	**307,795**	**—**
Trade notes and accounts payable	**149,462**	**149,462**	**—**
Other payable	**73,739**	**73,739**	**—**
Income taxes payable	**54,058**	**54,058**	**—**
Consumption taxes payable	**60,105**	**60,105**	**—**
Bonds	**459,410**	**474,273**	**14,863**
Long-term bank loans	**172,595**	**173,733**	**1,138**
Total	**1,505,427**	**1,521,428**	**16,001**
Derivatives	**2,039**	**2,039**	**—**

	Millions of U.S. dollars		
March 31, 2010	Carrying amount	Fair value	Unrecognized gain/loss
Cash and cash equivalents	**$ 1,659**	**$ 1,659**	**$ —**
Trade notes and accounts receivable	**3,191**		
Allowance for doubtful accounts*1	**(31)**		
Subtotal	**3,160**	**3,160**	**—**
Short-term investments and Investment securities	**735**	**735**	**0**
Time deposits	**84**	**84**	
Held-to-maturity securities	**3**	**3**	**0**
Available-for-sale securities	**648**	**648**	**—**
Total	**5,554**	**5,554**	**0**
Short-term bank loans	**1,174**	**1,174**	**—**
Commercial paper	**1,279**	**1,279**	**—**
Tobacco excise taxes payable	**3,308**	**3,308**	**—**
Trade notes and accounts payable	**1,606**	**1,606**	**—**
Other payable	**793**	**793**	**—**
Income taxes payable	**581**	**581**	**—**
Consumption taxes payable	**646**	**646**	**—**
Bonds	**4,938**	**5,098**	**160**
Long-term bank loans	**1,855**	**1,867**	**12**
Total	**16,180**	**16,352**	**172**
Derivatives	**22**	**22**	**—**

*1 Allowance for doubtful accounts are deducted from trade notes and accounts receivable to which they relate.

Cash and cash equivalents and receivables

The carrying values of cash and cash equivalents and receivable approximate fair value because of their short maturities.

Short-term investments and investment securities

The fair value of short-term investments and investment securities are measured at the quoted market price of the stock exchange for the equity instruments, and at the quoted price obtained from the financial institution for certain debt instruments.

The information of the fair value for the short-term investments and investment securities by classification is included in Note 5.

Payables, short-term bank loans, commercial paper, other payables, tobacco excise tax payables, Income taxes payable and Consumption taxes payable

The carrying values of the liabilities approximate fair value because of their short maturities.

Bonds

The fair value of bonds that JT and its subsidiaries issued is determined by the market price, if it is available, or by discounting the cash flows related to the debt at the rate assumed based on debt's maturity and credit risk.

Long-term bank loans

The fair value of long-term bank loans is determined by discounting the cash flows related to the loans at the rate assumed based on debt's maturity and credit risk.

Derivatives

The information of the fair value for derivatives is included in Note 17.

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

	Carrying amount	
March 31, 2010	Millions of yen	Millions of U.S. dollars
Investments in equity instruments that do not have a quoted market price in an active market	¥28,400	$305

(5) Maturity analysis for Cash and cash equivalents and Trade notes and accounts receivable with contractual maturities

	Millions of yen		Millions of U.S. dollars	
March 31, 2010	Due in one year or less	Due after one year	Due in one year or less	Due after one year
Cash and cash equivalents	**¥154,369**	**¥—**	**$1,659**	**$—**
Trade notes and accounts receivable	**296,885**	**—**	**3,191**	**—**
Total	**451,254**	**—**	**4,850**	**—**

Please see Note 5 for the carrying value of short-term investments and investment securities by contractual maturities.

Please see Note 8 for annual maturities of short-term bank loans, commercial paper and long-term debt.

17. Derivatives

JT and certain consolidated subsidiaries use derivative financial instruments ("derivatives"), including derivatives described below, to hedge the foreign exchange risk associated with certain assets and liabilities in foreign currencies.

Financial instruments

2008	2009	**2010**
Foreign currency forward contracts	Foreign currency forward contracts	**Foreign currency forward contracts**
Currency swaps	Currency swaps	**Currency swaps**
Currency options	Currency options	

JT and certain consolidated subsidiaries also entered into derivatives described below as a manner of managing their interest rate exposure.

Financial instruments

2008	2009	**2010**
Interest rate swaps	Interest rate swaps	**Interest rate swaps**
Interest rate cap options	Interest rate cap options	**Interest rate cap options**
Interest rate swaption		

Derivatives are subject to market risk and credit risk. Market risk is the exposure created by potential fluctuations in market conditions, including interest or foreign exchange rates. Credit risk is the possibility that a loss may result from a counterparty's failure to perform according to the terms and conditions of the contract.

The Group does not hold or issue derivatives for trading purposes. The main objective of using derivatives is to hedge the Group exposure to interest rate risks associated with certain interest payments on borrowings and bonds and forecasted foreign currency denominated transactions.

The effectiveness of the hedging instruments is assessed in accordance with the Risk Management Policy and Practice Manual for financial instruments of JT and certain consolidated subsidiaries by comparing the accumulated amount of changes in hedging instruments with hedged items. Hedging instruments and hedged items were summarized as follows:

2008

Hedging instruments	Hedged items
Foreign currency forward contracts	Forecasted foreign currency transactions
Currency swaps	Forecasted foreign currency transactions
Currency options	Forecasted foreign currency transactions

2009

Hedging instruments	Hedged items
Foreign currency forward contracts	Forecasted foreign currency transactions
Interest rate swaps	Borrowings

2010

Hedging instruments	Hedged items
Foreign currency forward contracts	**Forecasted foreign currency transactions**
Interest rate swaps	**Borrowings**

The fair value of derivative transactions is measured at the quoted price obtained from the financial institution.

The contract or notional amounts of derivatives which are shown in the below table do not represent the amounts exchanged by the parties and do not measure the Group's exposure to credit or market risk.

Derivative transactions to which hedge accounting is not applied at March 31, 2008, 2009 and 2010:

	2008			2009			2010 (Millions of yen)			
	Contract/ Notional Amount	Fair Value	Gain (Loss)	Contract/ Notional Amount	Fair Value	Gain (Loss)	Contract/ Notional Amount	Contract Amount due after One Year	Fair Value	Gain (Loss)
Foreign currency forward contracts:										
Buying	¥317,417	¥311,944	¥(5,473)	¥154,553	¥151,600	¥(2,953)	**¥296,523**	**¥ 2,894**	**¥ 654**	**¥ 654**
Selling	607,925	611,502	(3,577)	183,728	185,286	(1,558)	**133,768**	**2,416**	**(490)**	**(490)**
Currency swaps:										
Buying	7,784	(306)	(306)	59,712	(242)	(242)	**59,712**	**—**	**(123)**	**(123)**
Selling	2,193	(151)	(151)	3,148	287	287	**2,260**	**2,260**	**(460)**	**(460)**
Currency options:										
Buying	1,935	1	1	—	—	—	**—**	**—**	**—**	**—**
Selling	—	—	—	—	—	—	**—**	**—**	**—**	**—**
Total			¥(9,506)			¥(4,466)				**¥ (419)**
Interest rate swaps:										
Receive fixed pay floating	270,582	(1,218)	2,211	72,284	2,811	2,811	**36,606**	**36,606**	**2,297**	**2,297**
Receive floating pay fixed	—	—	—	470	(5)	(5)	**—**	**—**	**—**	**—**
Interest rate cap options:										
Buying	484,867	718	718	318,042	101	(1,504)	**297,744**	**36,606**	**161**	**(1,209)**
Total			¥ 2,929			¥ 1,302				**¥ 1,088**

	2010 (Millions of U.S. dollars)			
	Contract/ Notional Amount	Contract Amount due after One Year	Fair Value	Gain (Loss)
Foreign currency forward contracts:				
Buying	**$3,187**	**$ 31**	**$ 7**	**$ 7**
Selling	**1,438**	**26**	**(5)**	**(5)**
Currency swaps:				
Buying	**642**	**—**	**(1)**	**(1)**
Selling	**24**	**24**	**(5)**	**(5)**
Currency options:				
Buying	**—**	**—**	**—**	**—**
Selling	**—**	**—**	**—**	**—**
Total				**$ (4)**
Interest rate swaps:				
Receive fixed pay floating	**393**	**393**	**25**	**25**
Receive floating pay fixed	**—**	**—**	**—**	**—**
Interest rate cap options:				
Buying	**3,200**	**393**	**2**	**(13)**
Total				**$ 12**

Derivative transactions to which hedge accounting is applied at March 31, 2010:

	Millions of yen			
	2010			
	Hedged item	Contract Amount	Contract Amount due after One Year	Fair Value
Interest rate swaps (fixed rate payment, floating rate receipt)	**Long-term bank loans**	**¥1,137**	**437**	***1**

	Millions of U.S. dollars			
	2010			
	Hedged item	Contract Amount	Contract Amount due after One Year	Fair Value
Interest rate swaps (fixed rate payment, floating rate receipt)	**Long-term bank loans**	**$12**	**5**	***1**

*1 The above interest rate swaps which qualify for hedge accounting and meet specific matching criteria are not remeasured at market value but the differential paid or received under the swap agreements are recognized and included in interest expense.
In addition, the fair value of such interest rate swaps is included in that of hedged items (see Note 16).

18. Commitments and Contingencies

On September 29, 2009, the Government of Ontario, Canada filed a lawsuit against 13 tobacco manufacturers including JT's Canadian consolidated subsidiary JTI-Macdonald Corp. ("JTI-Mac") and 1 industry organization. The detail is as follows.

(1) Parties to the lawsuit

Plaintiff Government of Ontario (Canada)

Defendants 13 tobacco manufacturers including JTI-Mac and 1 industry organization

(2) Content of the complaint

To seek compensation for damages for the cost of health care benefits, resulting from the treatment of tobacco related disease or the risk of tobacco related disease, which have been paid or will be paid by the government of Ontario to relevant insured persons.

(3) Amount of the claim

CAD50.0 billion (approximately ¥4,568 billion)

* The statement of claim in this case 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, which is claimed from any individual defendant.

JTI-Mac has valid grounds to defend the action which it will pursue by all appropriate means with the full support of JT. There are similar pending lawsuits against JTI-Mac and others field in Canada by the Government of British Columbia and the Government of New Brunswick claiming the recovery of health care costs; however, the amounts of claims have not been specified in these lawsuits.

19. Net Income Per Share

Reconciliation of the differences between basic and diluted net income per share ("EPS") for the years ended March 31, 2008, 2009 and 2010 was as follows:

	Millions of yen	Shares	Yen	U.S. dollars
	Net Income	Weighted average shares	EPS	EPS
For the year ended March 31, 2010:				
Basic EPS				
Net income available to common shareholders	**¥138,448**	**9,580,092**	**¥14,452**	**$155**
Effect of dilutive securities:				
Stock acquisition rights		**1,849**		
Diluted EPS:				
Net income for computation	**¥138,448**	**9,581,941**	**¥14,449**	**$155**
For the year ended March 31, 2009:				
Basic EPS				
Net income available to common shareholders	¥123,400	9,580,080	¥12,881	$131
Effect of dilutive securities:				
Stock acquisition rights		846		
Diluted EPS:				
Net income for computation	¥123,400	9,580,926	¥12,880	$131
For the year ended March 31, 2008:				
Basic EPS				
Net income available to common shareholders	¥238,702	9,580,080	¥24,917	$249
Effect of dilutive securities:				
Stock acquisition rights		97		
Diluted EPS:				
Net income for computation	¥238,702	9,580,177	¥24,916	$249

20. Segment Information

The Group's business is divided into the domestic tobacco, international tobacco, pharmaceutical, food and other industry segments.

The domestic tobacco segment consists of manufacturing and sale of tobacco products, primarily cigarettes, in Japan, including tobacco products sold at duty free shops in Japan, as well as at markets in China, Hong Kong and Macau, which are covered by the China Division. The domestic tobacco segment includes the sales by TS Network Co., Ltd., JT's subsidiary. TS Network Co., Ltd. distributes the tobacco products and conducts wholesale etc. of foreign brand tobacco products purchased from foreign tobacco manufacturers through importers. The international tobacco segment consists of manufacturing and sale of cigarettes in other markets worldwide not covered by the domestic tobacco segment. The pharmaceutical segment is concerned with the development, manufacturing and sale of prescription drugs. The food segment involves manufacturing and sale of beverages and processed foods. Other segments include the real estate business and other operations.

With respect to the international tobacco business, the accounting period of consolidated overseas subsidiaries, represented by JT International, ends December 31, 2009 and the results for the twelve months ended December 31, 2009 are consolidated for the year ended March 31, 2010.

(1) Industry Segments

Information about the industry segments of the Group for the years ended March 31, 2008, 2009 and 2010 were as follows:

Millions of yen

2008

	Domestic Tobacco	International Tobacco	Pharmaceutical	Food	Others	Total	Elimination/ Corporate	Consolidated
Sales to customers	¥3,362,398	¥2,639,969	¥ 49,064	¥336,420	¥21,876	¥6,409,727	¥ —	¥6,409,727
Intersegment sales	48,981	35,341	—	115	22,332	106,769	(106,769)	—
Total sales	3,411,379	2,675,310	49,064	336,535	44,208	6,516,496	(106,769)	6,409,727
Operating expenses	3,189,031	2,469,950	58,708	335,868	33,760	6,087,317	(108,144)	5,979,173
Operating income (loss)	¥ 222,348	¥ 205,360	¥ (9,644)	¥ 667	¥10,448	¥ 429,179	¥ 1,375	¥ 430,554
Assets	¥ 847,123	¥3,804,414	¥111,422	¥353,283	¥90,001	¥5,206,243	¥(119,029)	¥5,087,214
Depreciation and amortization other than goodwill	83,290	65,398	3,375	4,891	11,606	168,560	(902)	167,658
Impairment Loss	344	346	—	380	—	1,070	2,755	3,825
Amortization of goodwill	1,088	—	—	2,795	—	3,883	—	3,883
Capital expenditures	57,201	48,431	4,257	6,033	14,793	130,715	(1,160)	129,555

Millions of yen

2009

	Domestic Tobacco	International Tobacco	Pharmaceutical	Food	Others	Total	Elimination/ Corporate	Consolidated
Sales to customers	¥3,200,494	¥3,118,319	¥ 56,758	¥435,966	¥20,770	¥6,832,307	¥ —	¥6,832,307
Intersegment sales	48,390	40,631	—	133	12,044	101,198	(101,198)	—
Total sales	3,248,884	3,158,950	56,758	436,099	32,814	6,933,505	(101,198)	6,832,307
Operating expenses	3,060,625	2,984,178	55,738	447,550	23,119	6,571,210	(102,709)	6,468,501
Operating income (loss)	¥ 188,259	¥ 174,772	¥ 1,020	¥ (11,451)	¥ 9,695	¥ 362,295	¥ 1,511	¥ 363,806
Assets	¥ 788,673	¥2,700,099	¥111,519	¥332,670	¥87,432	¥4,020,393	¥(140,590)	¥3,879,803
Depreciation and amortization other than goodwill	82,933	68,960	3,870	18,293	3,456	177,512	(612)	176,900
Impairment Loss	—	—	—	3,830	—	3,830	12,535	16,365
Amortization of goodwill	1,089	94,235	—	10,188	—	105,512	—	105,512
Capital expenditures	46,506	59,776	3,426	23,201	1,129	134,038	235	134,273

Millions of yen

2010

	Domestic Tobacco	International Tobacco	Pharmaceutical	Food	Others	Total	Elimination/ Corporate	Consolidated
Sales to customers	**¥3,042,836**	**¥2,633,636**	**¥ 44,069**	**¥394,653**	**¥19,501**	**¥6,134,695**	**¥ —**	**¥6,134,695**
Intersegment sales	**54,922**	**38,128**	**—**	**112**	**10,448**	**103,610**	**(103,610)**	**—**
Total sales	**3,097,758**	**2,671,764**	**44,069**	**394,765**	**29,949**	**6,238,305**	**(103,610)**	**6,134,695**
Operating expenses	**2,894,419**	**2,562,637**	**57,662**	**408,461**	**19,392**	**5,942,571**	**(104,381)**	**5,838,190**
Operating income (loss)	**¥ 203,339**	**¥ 109,127**	**¥ (13,593)**	**¥ (13,696)**	**¥10,557**	**¥ 295,734**	**¥ 771**	**¥ 296,505**
Assets	**¥ 782,293**	**¥2,765,948**	**¥114,060**	**¥311,190**	**¥85,094**	**¥4,058,585**	**¥(185,989)**	**¥3,872,596**
Depreciation and amortization other than goodwill	**53,218**	**56,090**	**3,942**	**16,498**	**2,782**	**132,530**	**240**	**132,770**
Impairment Loss	**17**	**1,030**	**—**	**3,136**	**—**	**4,183**	**1,860**	**6,043**
Amortization of goodwill	**1,088**	**84,652**	**—**	**11,687**	**—**	**97,427**	**—**	**97,427**
Capital expenditures	**45,828**	**64,552**	**2,954**	**23,446**	**346**	**137,126**	**8**	**137,134**

Notes to Consolidated Financial Statements

	Domestic Tobacco	International Tobacco	Pharmaceutical	Food	Others	Total	Elimination/ Corporate	Consolidated
	Millions of U.S. dollars							
	2010							
Sales to customers	**$32,705**	**$28,306**	**$ 474**	**$4,242**	**$209**	**$65,936**	**$ —**	**$65,936**
Intersegment sales	**590**	**410**	**—**	**1**	**113**	**1,114**	**(1,114)**	**—**
Total sales	**33,295**	**28,716**	**474**	**4,243**	**322**	**67,050**	**(1,114)**	**65,936**
Operating expenses	**31,109**	**27,543**	**620**	**4,390**	**209**	**63,871**	**(1,122)**	**62,749**
Operating income (loss)	**$ 2,186**	**$ 1,173**	**$ (146)**	**$ (147)**	**$113**	**$ 3,179**	**$ 8**	**$ 3,187**
Assets	**$ 8,408**	**$29,729**	**$1,226**	**$3,345**	**$914**	**$43,622**	**$(1,999)**	**$41,623**
Depreciation and amortization other than goodwill	**572**	**603**	**42**	**177**	**30**	**1,424**	**3**	**1,427**
Impairment Loss	**0**	**11**	**—**	**34**	**—**	**45**	**20**	**65**
Amortization of goodwill	**12**	**910**	**—**	**125**	**—**	**1,047**	**—**	**1,047**
Capital expenditures	**493**	**694**	**32**	**252**	**3**	**1,474**	**0**	**1,474**

Operating expenses represent the aggregate amount of the cost of sales and selling, general and administrative expenses.

Increase of long-term expenses is included in capital expenditures and amortization expense of the long-term prepaid expenses is included in depreciation and amortization other than goodwill.

The domestic tobacco segment includes the sales by TS Network Co., Ltd. Net sales of such imported tobacco products via TS Network Co., Ltd. for the year ended March 31, 2008, 2009 and 2010 were ¥1,193,178 million, ¥1,135,320 million and ¥1,084,321 million ($11,654 million), respectively.

Effective from April 1, 2008, JT applied the "Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries for Consolidated Financial Statements" (see Note 3 (b)). As a result of this change, the operating income for the international tobacco segment for the year ended March 31, 2009 decreased by ¥94,235 million as compared to the case where the previous method was adopted.

(2) Geographical Segments

The geographical segments of the Group for the years ended March 31, 2008, 2009 and 2010 were summarized as follows:

	Japan	Western Europe	Others	Total	Elimination/ Corporate	Consolidated
	Millions of yen					
	2008					
Sales to customers	¥3,711,763	¥1,678,770	¥1,019,194	¥6,409,727	¥ —	¥6,409,727
Intersegment sales	52,308	181,062	29,212	262,582	(262,582)	—
Total sales	3,764,071	1,859,832	1,048,406	6,672,309	(262,582)	6,409,727
Operating expenses	3,541,731	1,803,896	897,008	6,242,635	(263,462)	5,979,173
Operating income	¥ 222,340	¥ 55,936	¥ 151,398	¥ 429,674	¥ 880	¥ 430,554
Assets	¥1,160,749	¥3,436,185	¥ 420,170	¥5,017,104	¥ 70,110	¥5,087,214

	Japan	Western Europe	Others	Total	Elimination/ Corporate	Consolidated
	Millions of yen					
	2009					
Sales to customers	¥3,672,004	¥2,038,028	¥1,122,275	¥6,832,307	¥ —	¥6,832,307
Intersegment sales	53,334	223,872	39,186	316,392	(316,392)	—
Total sales	3,725,338	2,261,900	1,161,461	7,148,699	(316,392)	6,832,307
Operating expenses	3,538,899	2,286,088	961,828	6,786,815	(318,314)	6,468,501
Operating income (loss)	¥ 186,439	¥ (24,188)	¥ 199,633	¥ 361,884	¥ 1,922	¥ 363,806
Assets	¥1,083,962	¥2,378,679	¥ 351,080	¥3,813,721	¥ 66,082	¥3,879,803
Amortization of goodwill	11,277	94,235	—	105,512	—	105,512

	Japan	Western Europe	Others	Total	Elimination/ Corporate	Consolidated
						Millions of yen 2010
Sales to customers	**¥3,482,548**	**¥1,677,755**	**¥ 974,392**	**¥6,134,695**	**¥ —**	**¥6,134,695**
Intersegment sales	**59,889**	**196,601**	**34,326**	**290,816**	**(290,816)**	**—**
Total sales	**3,542,437**	**1,874,356**	**1,008,718**	**6,425,511**	**(290,816)**	**6,134,695**
Operating expenses	**3,357,884**	**1,914,645**	**858,222**	**6,130,751**	**(292,561)**	**5,838,190**
Operating income (loss)	**¥ 184,553**	**¥ (40,289)**	**¥ 150,496**	**¥ 294,760**	**¥ 1,745**	**¥ 296,505**
Assets	**¥1,031,911**	**¥2,358,103**	**¥ 433,866**	**¥3,823,880**	**¥ 48,716**	**¥3,872,596**
Amortization of goodwill	**12,775**	**84,652**	**—**	**97,427**	**—**	**97,427**

	Japan	Western Europe	Others	Total	Elimination/ Corporate	Consolidated
						Millions of U.S. dollars 2010
Sales to customers	**$37,430**	**$18,033**	**$10,473**	**$65,936**	**$ —**	**$65,936**
Intersegment sales	**644**	**2,113**	**369**	**3,126**	**(3,126)**	**—**
Total sales	**38,074**	**20,146**	**10,842**	**69,062**	**(3,126)**	**65,936**
Operating expenses	**36,091**	**20,579**	**9,224**	**65,894**	**(3,145)**	**62,749**
Operating income (loss)	**$ 1,983**	**$ (433)**	**$ 1,618**	**$ 3,168**	**$ 19**	**$ 3,187**
Assets	**$11,091**	**$25,345**	**$ 4,663**	**$41,099**	**$ 524**	**$41,623**
Amortization of goodwill	**137**	**910**	**—**	**1,047**	**—**	**1,047**

"Western Europe" includes Switzerland, United Kingdom and Germany while "Others" includes Canada, Russia and Malaysia.

Operating expenses represent the aggregate amount of the cost of sales and selling, general and administrative expenses.

Effective from April 1, 2008, JT applied the "Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries for Consolidated Financial Statements" (see Note 3 (b)). As a result of this change, the operating income for the Western Europe segment for the year ended March 31, 2009 decreased by ¥94,235 million as compared to the case where the previous method was adopted.

(3) Sales to Foreign Customers

Sales to Foreign Customers, which consist of sales of JT and its consolidated subsidiaries in countries or regions outside Japan, for the years ended March 31, 2008, 2009 and 2010 were as follows:

	Millions of yen 2008	2009	2010	Millions of U.S. dollars 2010
Sales to foreign customers				
Western Europe	¥1,634,921	¥2,002,739	**¥1,646,648**	**$17,698**
Others	1,070,540	1,177,113	**1,008,326**	**10,838**
Total	¥2,705,461	¥3,179,852	**¥2,654,974**	**$28,536**
Consolidated sales	¥6,409,727	¥6,832,307	**¥6,134,695**	**$65,936**

	Percentage of 2008	2009	2010
Sales to foreign customers			
Western Europe	25.5	29.3	**26.8**
Others	16.7	17.2	**16.5**
Total	42.2	46.5	**43.3**

"Western Europe" includes Switzerland, United Kingdom and Germany while "Others" includes Canada, Russia and Malaysia.

21. Subsequent Events

On April 13, 2010, JTI-Macdonald Corp. ("JTI-Mac"), JT's Canadian consolidated subsidiary, entered into a comprehensive agreement with the Government of Canada and all provinces and territories (the "Canadian Governments") to establish a cooperation mechanism in combating cigarette smuggling and contraband. In addition, JTI-Mac pleaded to a regulatory offense for its involvement in the illicit trade of cigarettes prior to JT's acquisition of non-US tobacco operations of RJR Nabisco Inc. and paid CAD150 million (approximately ¥13.8 billion). As a result, all of the contraband-related claims against JTI-Mac and others associated with it by the Canadian Governments have been withdrawn and the Notice of Assessment from the Quebec Ministry of Revenue has been withdrawn.

At the same time, the RJR Group entered into another agreement with the Canadian Governments and made payments totaling CAD400 million (approximately ¥37.0 billion), resulting in total payments by the JT Group and RJR Group to the Canadian Governments of CAD550 million (approximately ¥50.9 billion). As a result of indemnification rights under the purchase agreement in 1999 and subsequent negotiations with the RJR Group, the JT Group and the RJR Group entered into an agreement whereby the JT Group would incur CAD150 million among the aforementioned CAD550 million total.

Independent Auditors' Report

Deloitte.

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To the Board of Directors of

Japan Tobacco Inc.:

We have audited the accompanying consolidated balance sheets of Japan Tobacco Inc. and consolidated subsidiaries (the "Company") as of March 31, 2010 and 2009, and the related consolidated statements of income, changes in equity, and cash flows for each of the three years in the period ended March 31, 2010, all expressed in Japanese yen. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Japan. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of March 31, 2010 and 2009, and the consolidated results of their operations and their cash flows for each of the three years in the period ended March 31, 2010, in conformity with accounting principles generally accepted in Japan.

Our audits also comprehended the translation of Japanese yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made in conformity with the basis stated in Note 2. Such U.S. dollar amounts are presented solely for the convenience of readers outside Japan.

Deloitte Touche Tohmatsu LLC

June 24, 2010

Member of
Deloitte Touche Tohmatsu