

## Financial Review

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## Sales and Income

## Operating Environment

The overall world economy in fiscal 2017 saw gradual recovery, with ongoing gentle expansion in the U.S. economy and signs of recovery in China. In the electronics industry, capital investment by semiconductor manufacturers was strong. This was due to growth in demand for data center servers, reflecting increases in data transmission volumes driven by the arrival of the internet of things (IoT), as well as the growing sophistication of smartphones. As a result, the wafer fab equipment market, in which Tokyo Electron operates, grew more than 10% year on year to US\$37 billion. At the same time, the display industry also saw active capital investment aimed mainly at manufacturing higher resolution panels for mobile devices. Accordingly, the market for flat panel display (FPD) production equipment was brisk, surpassing US\$10 billion for the first time since 2011.

## Sales

Net sales in fiscal 2017 rose 20.4% year on year to ¥799.7 billion. This reflected the favorable market environment, expanding demand for cutting-edge semiconductor production equipment (SPE) and increased demand for parts and used equipment sales, modifications and maintenance services. By segment, net sales in the SPE segment grew 22.3% year on year to ¥749.8 billion. Net sales in the FPD production equipment segment grew 10.5% year on year to ¥49.3 billion. For details on performance by segment, please refer to Review of Operations and Business Outlook on page 9. Furthermore, net sales in the field solutions business

(encompassing sales of parts and used equipment, modifications and maintenance services) rose 12% year on year to approximately ¥208.0 billion, accounting for 26% of overall net sales.

## Gross Profit, SG&amp;A Expenses and Operating Income

Gross profit in fiscal 2017 was up 20.6% year on year to ¥322.2 billion, reflecting the growth in net sales. However, the gross profit margin rose only 0.1 of a percentage point to 40.3%, as profitability gains from increased factory utilization were partially offset by investment in growth aimed at reinforcing product competitiveness.

SG&A expenses rose 10.8% year on year to ¥166.5 billion, but the ratio of SG&A expenses to consolidated net sales dropped 1.8 percentage points from the previous fiscal year to 20.8% in the fiscal year under review. Consequently, operating income increased 33.3% year on year to ¥155.6 billion, and the operating margin rose 1.9 percentage points to a record high of 19.5%. As this shows, the Group made progress toward its medium-term management plan target of an operating margin of 24–26%, including reducing the ratio of SG&A expenses to consolidated net sales.

## R&amp;D Expenses

R&D expenses were up 9.8% year on year to ¥83.8 billion. The main cause of this rise was the reinforcement of R&D in the fields of etch, deposition and cleaning systems, in which the Company is working to expand its market share under the medium-term management plan. Tokyo Electron focused on R&D aimed at enhancing the competitiveness of future products. This

included developing innovative technologies to not only enhance the performance of individual products, but optimize entire processes, as well as making products more intelligent, all of which are especially important in terms of differentiating the Company's products going forward.

Tokyo Electron regards advanced technological prowess as the source of its growth. Accordingly, the Company actively invests in growth to produce next-generation products, mainly focusing on fields in which market growth is forecast. In the fiscal year under review, Tokyo Electron released a new single wafer deposition system and increased its market share in all of its key product areas, making tangible progress toward the goals of the medium-term management plan.

In FPD production equipment, Tokyo Electron primarily advanced development of products for new generation 10.5/11 panels, which are expected to see rapid market growth going forward.

## Other Income (Expenses) and Net Income Attributable to Owners of Parent

During fiscal 2017, net other expenses came to ¥6.5 billion, reflecting ¥7.5 billion in loss on disaster related to the Kumamoto Earthquake and ¥1.0 billion in interest and dividend income. As a result, income before income taxes came to ¥149.1 billion, up 40.1% year on year. Net income attributable to owners of the parent totaled ¥115.2 billion in fiscal 2017, up 47.9% from fiscal 2016. Net income per share rose 52.3% year on year to ¥702.26.

## Comprehensive income

In fiscal 2017, Tokyo Electron recognized comprehensive income of ¥119.9 billion, up from ¥61.0 billion in fiscal 2016. This was mainly due to the ¥115.2 billion in net income, ¥2.8 billion in unrealized gains on investment securities related to strategically held shares, and ¥2.6 billion in gain on remeasurements of defined benefit plans due to an increase in the discount rate used to calculate retirement benefits as a result of rising interest rates.

## Dividend Policy and Dividends

It is the policy of Tokyo Electron to pay dividends on the basis of business performance. The Company aims for a payout ratio of 50% of net income. Furthermore, with an eye to ensuring stable dividends, a lower limit of ¥150 per share has been set on annual dividends.\* Reflecting the Company's strong sales and profit growth, Tokyo Electron paid annual dividends for fiscal 2017 of ¥352 per share (for a payout ratio of 50.1%), its highest ever. Going forward, the Company will seek to build world-class profitability and reciprocate the support of shareholders by delivering profit growth.

\* This lower limit may be revised in the event that the Company does not generate net income for two consecutive fiscal years.

## Financial Position and Cash Flows

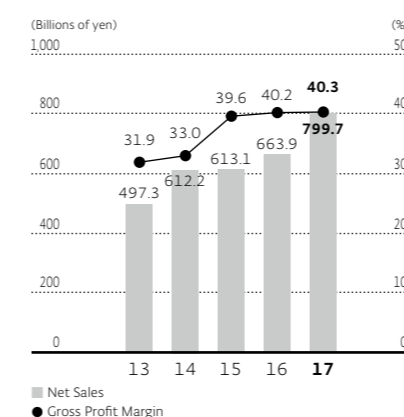
## Assets, Liabilities and Net Assets

## Assets

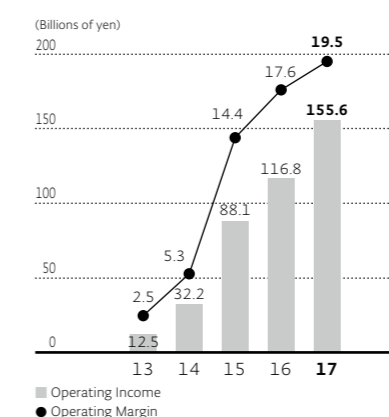
Current assets increased ¥158.5 billion from the end of the previous fiscal year to ¥775.9 billion, reflecting

	Millions of yen				
Sales and Income	2013	2014	2015	2016	2017
Net sales	¥497,300	¥612,170	¥613,125	¥663,949	¥799,719
Gross profit	158,755	201,892	242,774	267,210	322,291
Gross profit margin	31.9%	33.0%	39.6%	40.2%	40.3%
Selling, general and administrative expenses	146,206	169,687	154,661	150,421	166,594
Operating income	12,549	32,205	88,113	116,789	155,697
Operating margin	2.5%	5.3%	14.4%	17.6%	19.5%
Income (loss) before income taxes	17,767	(11,756)	86,828	106,467	149,116
Net income (loss) attributable to owners of parent	6,076	(19,409)	71,888	77,892	115,208

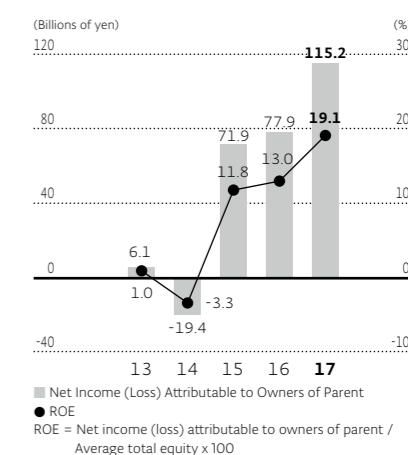
## Net Sales and Gross Profit Margin



## Operating Income and Operating Margin



## Net Income (Loss) Attributable to Owners of Parent and ROE



Financial Review

Financial Review

a ¥78.6 billion increase in cash on hand\* due to the generation of ¥118.0 billion in free cash flow,\*\* a ¥41.1 billion increase in inventories due to increased production to meet robust demand from semiconductor and display manufacturers, and a ¥17.3 billion increase in trade notes and accounts receivable. The turnover period for trade notes and accounts receivable in fiscal 2017 was 61 days, compared with 64 days in fiscal 2016, and the inventory turnover period in fiscal 2017 was 108 days, compared with 107 days in fiscal 2016.

Net property, plant and equipment increased ¥4.1 billion year on year to ¥100.4 billion. This was largely due to ¥20.6 billion in new fixed asset acquisitions, including part of the construction costs for a new logistics building being constructed at the Miyagi Plant to increase productivity as well as R&D equipment acquired to bolster the development of next-generation technologies. These and other positive factors more than offset ¥17.8 billion in depreciation and amortization.

Investments and other assets increased ¥1.4 billion year on year to ¥81.0 billion.

As a result, total assets as of March 31, 2017 stood at ¥957.4 billion, up ¥164.0 billion year on year.

\* Cash on hand: Cash and cash equivalents + Short-term investments with original maturities of less than one year

\*\* Free cash flow: Cash flows from operating activities + Cash flows from investing activities (excluding changes in short-term investments with original maturities of less than one year)

Liabilities and Net Assets

Current liabilities increased ¥81.7 billion from the end of fiscal 2016 to ¥247.7 billion at the end of fiscal 2017. This was mainly due to a ¥34.4 billion increase in customer advances, a ¥24.1 billion increase in trade notes and accounts payable, a ¥10.2 billion increase in accrued employees' bonuses and an ¥8.6 billion increase in income taxes payable.

Non-current liabilities increased ¥0.6 billion year on year to ¥63.6 billion.

Net assets came to ¥645.9 billion at the end of fiscal 2017, up ¥81.7 billion from the end of fiscal 2016. This was mainly due to a ¥75.7 billion increase in retained earnings, reflecting the recording of ¥115.2 billion in net income attributable to owners of the parent and ¥39.3

billion paid in cash dividends (¥18.3 billion for the fiscal 2016 year-end dividend and ¥20.9 billion for the fiscal 2017 interim dividend).

As a result, the equity ratio fell 3.7 percentage points year on year to 67.2% at the end of March 2017. ROE climbed to 19.1% from 13.0% in fiscal 2016.

Capital Expenditures\* and Depreciation and Amortization\*\*

Capital expenditures totaled ¥20.6 billion in fiscal 2017, a 55.1% year-on-year increase. Major expenditures included the acquisition of R&D machinery and equipment in order to strengthen key areas in the SPE business.

Depreciation and amortization decreased 7.2% to ¥17.8 billion.

\* Capital expenditures represent only the gross increase in property, plant and equipment.

\*\* Depreciation and amortization does not include amortization of goodwill or losses on impairment.

Cash Flows

The balance of cash and cash equivalents at the end of March 2017 stood at ¥164.3 billion, an increase of ¥68.7 billion from the end of fiscal 2016. Cash on hand, which consists of cash and cash equivalents as well as

short-term investments with original maturities of less than one year not included in cash and cash equivalents, increased ¥78.6 billion year on year to ¥315.3 billion at the end of March 2017. Cash flows during the fiscal year under review were as follows.

Net cash provided by operating activities came to ¥136.9 billion, up ¥67.5 billion from fiscal 2016. Major contributors were ¥149.1 billion in income before income taxes, a ¥34.4 billion increase in customer advances, a ¥24.0 billion increase in trade notes and accounts payable, and ¥17.8 billion in depreciation and amortization. Major negative factors included a ¥44.1 billion increase in inventories, ¥32.6 billion in income taxes paid, and a ¥17.4 billion increase in trade notes and accounts receivable.

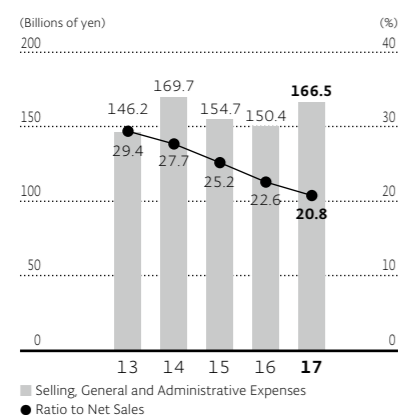
Net cash used in investing activities was ¥28.8 billion, compared with ¥150.0 billion used in the previous fiscal year. Major outflows included ¥17.5 billion used as payment for purchases of property, plant and equipment and a ¥9.9 billion net increase in short-term investments.

Net cash used in financing activities came to ¥39.3 billion, compared with ¥138.6 billion in fiscal 2016. This was mainly attributable to ¥39.3 billion in dividends paid.

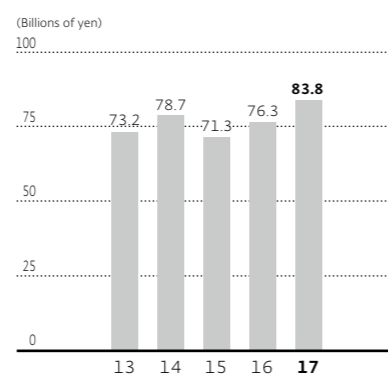
Financial Position	Millions of yen				
	2013	2014	2015	2016	2017
Total current assets	¥521,501	¥621,492	¥670,883	¥617,416	¥775,938
Net property, plant and equipment	135,698	112,344	106,896	96,317	100,441
Total investments and other assets	118,329	94,756	98,375	79,635	81,067
Total assets	775,528	828,592	876,154	793,368	957,447
Total current liabilities	106,670	170,510	172,812	166,061	247,770
Total liabilities	170,401	237,978	234,991	229,129	311,447
Total net assets (Total shareholders' equity)	605,127	590,614	641,163	564,239	645,999

Cash Flows	Millions of yen				
	2013	2014	2015	2016	2017
Cash flows from operating activities	¥ 84,267	¥ 44,449	¥ 71,806	¥ 69,398	¥136,948
Cash flows from investing activities	(141,769)	(19,599)	155,738	(150,014)	(28,893)
Cash flows from financing activities	(10,625)	(187)	(18,214)	(138,601)	(39,380)
Cash and cash equivalents at end of year	85,314	104,797	317,632	95,638	164,366

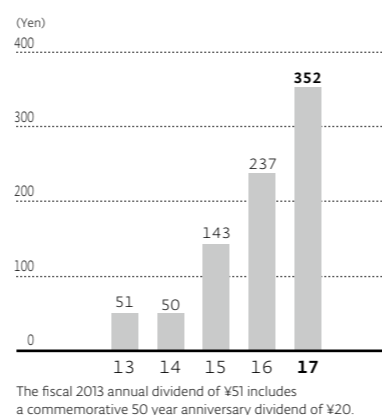
Selling, General and Administrative Expenses and Ratio to Net Sales



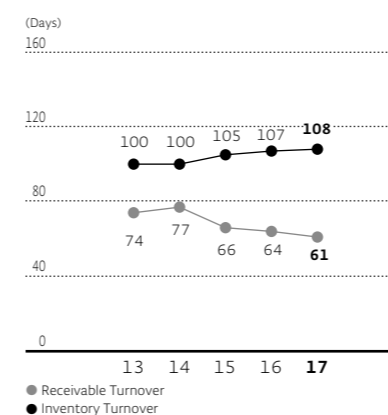
R&D Expenses



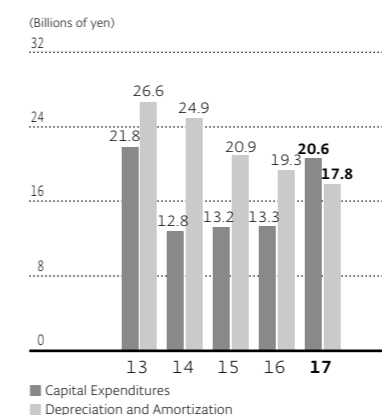
Cash Dividends per Share



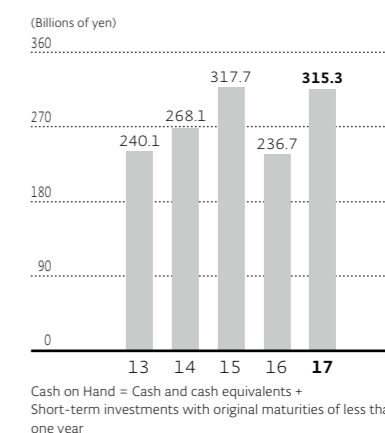
Receivable Turnover and Inventory Turnover



Capital Expenditures and Depreciation and Amortization



Cash on Hand



## Financial Review

### Business-related and Other Risks

The following risks may have a material impact on Tokyo Electron's business performance, stock price, or financial position.

#### (1) Impact from Changes in the Semiconductor Market

Tokyo Electron has achieved a high profit margin by concentrating resources in high-tech fields, including semiconductor production equipment, where technological innovation is rapid but Tokyo Electron can effectively use its strengths. Although technological change is responsible for the semiconductor market's rapid growth, Tokyo Electron has actively undertaken structural reforms to be able to generate profits under any circumstances, including when the market contracts temporarily due to imbalance of supply and demand. However, order cancellations, excess capacity and personnel and increased inventories resulting from an unexpectedly large market contraction, losses from bad debts resulting from the worsening of a customer's financial position, and supply shortages resulting from the worsening of a supplier's management situation, could adversely affect Tokyo Electron's business performance considerably.

#### (2) Impact from Concentration of Transactions on Particular Customers

Tokyo Electron has been successful at increasing transactions with the leading semiconductor manufacturers worldwide, including those in Japan, through the provision of products featuring outstanding, cutting-edge technology and of services offering a high level of customer satisfaction. However, Tokyo Electron's sales may from time to time be temporarily concentrated on particular customers due to the timing of large capital investments of major semiconductor manufacturers. The resulting escalation in sales competition could adversely affect Tokyo Electron's business performance.

#### (3) Impact from Research and Development

Through ongoing and proactive R&D investment and activities in cutting-edge technologies—miniaturization, vacuum, plasma, thermal processing, coating/developing, cleaning, wafer-transfer and clean technologies—Tokyo Electron has created advanced technologies. At the same time, by quickly bringing to market new products incorporating these technologies, Tokyo Electron has successfully captured a high market share in each of the product fields it has entered and generated a high profit margin. However, delays in the launch of new products and other factors could adversely affect Tokyo Electron's business performance.

#### (4) Safety-related Impact

Tokyo Electron's basic philosophy is to always bear in mind safety and health in the execution of business activities, including development, manufacturing, sales, services and management. In accordance with this philosophy, Tokyo Electron works actively and continuously to improve the safety of its products and to eliminate any harmful impact on health. However, harm to customers, order cancellations or other circumstances resulting from safety or other problems related to Tokyo Electron's products could adversely affect Tokyo Electron's business performance.

#### (5) Impact from Quality Issues

Tokyo Electron actively develops outstanding, cutting-edge technologies for incorporation in new products that are brought quickly to market. At the same time, Tokyo Electron works to establish a quality assurance system, efforts that include obtaining ISO 9001 certification, as well as to establish a world-class service system. These actions have resulted in a large number of customers adopting Tokyo Electron's products. However, because Tokyo Electron's products are based on cutting-edge technologies, and due to other factors, many of the technologies developed are in unfamiliar fields. The occurrence of unforeseen defects or other issues could adversely affect Tokyo Electron's business performance.

#### (6) Impact of Intellectual Property Rights

In order to distinguish its products and make them more competitive, Tokyo Electron has promoted its R&D strategy for the early development of cutting-edge technologies together with its business and intellectual property strategies. This approach has enabled Tokyo Electron to obtain sole possession of many proprietary technologies that have been instrumental to the Company's ability to capture a high market share and generate high profit margins in each of its product fields. Tokyo Electron's products incorporate and optimize many of these proprietary cutting-edge technologies. There may be cases in which, by avoiding the use of third-party technologies and intellectual property rights, Tokyo Electron's business performance could be adversely affected.

#### (7) Impact of Fluctuating Foreign Exchange Rates

Success in the development of overseas operations has increased the share of sales generated overseas. As a rule, Tokyo Electron conducts export transactions on a yen basis to avert exposure to foreign currency risks. However, some exports are denominated in foreign currencies. In these cases, Tokyo Electron hedges foreign currency risk by using a forward foreign exchange contract when an order is received or by other means. However, foreign exchange rate risks can arise from fluctuations in prices due to sudden foreign exchange movements, which could have an indirect adverse effect on Tokyo Electron's business performance.

#### (8) Influence of Corporate Acquisitions

As part of its business strategy, Tokyo Electron conducts corporate acquisitions in order to expand into new business areas, secure new technologies and business platforms, and strengthen the competitiveness of existing businesses. The Company conducts due diligence and carefully deliberates each specific acquisition. However, in the event that the results following an acquisition do not meet expectations, Tokyo Electron's business performance could be adversely affected.

#### (9) Impact from Major Lawsuits or Legal Actions

Tokyo Electron is not currently involved in any lawsuits or other legal actions that are likely to significantly influence its business results. However, in the event that the Company's business or other activities become the subject of a major lawsuit or other legal action, depending on the outcome of such action, Tokyo Electron's business results could be adversely affected.

#### (10) Other Risks

Tokyo Electron is actively engaged in reforming its corporate structure so that it can generate profits even when markets contract. These reforms have entailed creating new high-growth and high-return businesses and pursuing higher earnings from existing businesses. At the same time, Tokyo Electron has promoted activities to preserve the environment and worked to restructure its compliance, risk management and information security management systems. However, as long as it conducts business activities, as with peer companies or companies in different industries, Tokyo Electron is subject to the effect of many other factors. These include the world and regional economic environments, natural disasters, war, terrorism, infectious diseases and other unavoidable occurrences, financial or stock markets, government or other regulations, supply chains, market conditions for products and real estate, the ability to recruit personnel in Japan and overseas, competition over standardization, and loss of key personnel. Any of these factors could adversely affect Tokyo Electron's business performance.