Analysis of Business Results, Financial Position, and Cash Flows

Analysis of Business Results

Company Overview

In the global economy during fiscal 2017, the U.S. economy continued to recover owing to increases in consumer spending and improvements in the job market, and the trend in both Europe and China also proved to be one of moderate improvement. However, the outlook remains uncertain due to factors that include policy developments following on from the change of the government administration in the United States and the decision of the United Kingdom to leave the European Union. In the Japanese economy, the trend of moderate improvement continued amid the improvements in corporate earnings supported by the ongoing depreciation of the yen since the presidential election in the United States.

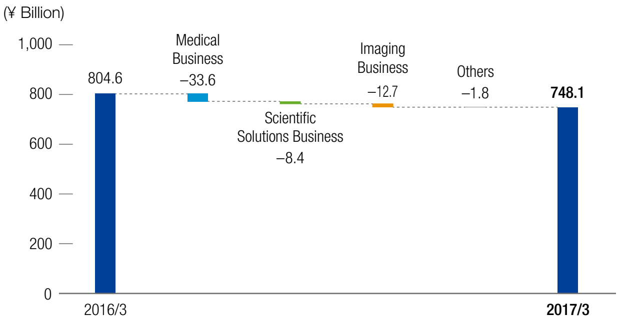
Amid this business environment, the Olympus Group launched the newly formulated 2016 Corporate Strategic Plan (16CSP), a five-year medium-term management plan that took effect in fiscal 2017. Under this plan, the Company has been forging ahead with strengthening business foundations and developing an aggressive business portfolio for sustainable growth with the basic policies of "Business to Specialist" Company and One Olympus.

In the Medical Business, we moved forward with efforts geared toward expanding staff numbers as needed to fortify production and maintenance systems while enhancing quality assurance and regulatory assurance measures. We also promoted the development of new mainstay products in the surgical device field. In the Scientific Solutions Business, we proceeded with organizational development efforts to facilitate the shift toward customer group-oriented strategies and also released new products that included laser scanning confocal microscopes and industrial videoscopes. In the Imaging Business, in addition to introducing new products, such as the OLYMPUS OM-D E-M1 Mark II, a new flagship mirrorless camera model, we accelerated structural reform measures for streamlining operations by narrowing down our focus sales areas and cutting costs.

During fiscal 2017, the Olympus Group invested ¥79,178 million in research and development and spent ¥49,347 million on capital expenditures. With respect to foreign exchange, the yen appreciated against both the U.S. dollar and the euro in comparison with the previous fiscal year. The average exchange rate during the year was ¥108.38 against the U.S. dollar (¥120.14 in the previous fiscal year) and ¥118.79 against the euro (¥132.58 in the previous fiscal year). These rates placed downward pressure on consolidated net sales and operating income to the extent of ¥74,281 million and ¥30,069 million year on year.

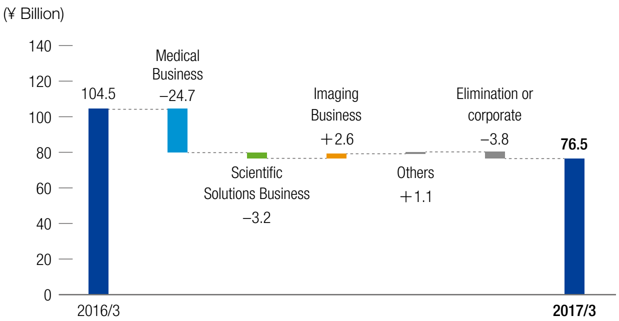
■ Net Sales

Consolidated net sales decreased 7.0% year on year, to ¥748,050 million, due to appreciation of the yen and other factors that lowered sales in the three core business domains of the Medical Business, the Scientific Solutions Business, and the Imaging Business.



■ Operating Income

Operating income was down 26.8% year on year, to ¥76,487 million, as a result of lower net sales.



■ Net Income (Loss)

Net income increased 24.9% year on year, to ¥78,191 million, a considerable improvement over the previous fiscal year resulting from the recording of extraordinary income of ¥27,757 million, which included gain on sale of investment securities and counteracted the impacts of the decline in operating income.

Performance by Segment

■ Medical Business

In the Medical Business, consolidated net sales totaled ¥575,285 million, down 5.5% year on year, and operating income was ¥115,482 million, down 17.6%. The decrease in net sales in the Medical Business was a result of yen appreciation. When the impacts of foreign exchange influences are excluded, net sales rose 4% year on year.

In the gastrointestinal endoscope field, sales were strong for mainstay gastrointestinal video endoscopy systems EVIS EXERA III and EVIS LUCERA ELITE. In the surgical device field, surgical endoscopy systems equipped with 4K technologies and 3D laparoscopy systems saw solid sales performance, while sales continued to grow for the THUNDERBEAT integrated energy device, which features both advanced bipolar and ultrasonic energy. In the endotherapy device field, favorable sales were seen for the VisiGlide 2™, a disposable guidewire product for use in endoscopic diagnosis and the treatment of biliary and pancreatic ducts.

Similar to net sales, operating income in the Medical Business decreased due to the impacts of yen appreciation. However, the strong growth in all fields led to a 1% year-on-year increase in operating income if the impacts of foreign exchange influences are excluded.

■ Scientific Solutions Business

In the Scientific Solutions Business, consolidated net sales totaled ¥93,227 million, down 8.2% year on year, and operating income amounted to ¥5,280 million, down 37.8%. The decrease in net sales in the Scientific Solutions Business was a result of yen appreciation. When the impacts of foreign exchange influences are excluded, net sales increased 1% year on year.

While sales of products for hospitals and life science research declined in Europe due to the impact of budget cuts and delays in budget execution, sales of these products were strong in Japan, the United States, and Asia. Sales of industrial microscopes to universities and research institutions were sluggish. Meanwhile, performance of non-destructive testing equipment was brisk, supported by the recovery in resource prices seen in the second half of the fiscal year.

Yen appreciation caused operating income to decline in the Scientific Solutions Business. When the impacts of foreign exchange influences are excluded, operating income was up 3% year on year due to effective efforts to control expenses and expenditures.

■ Imaging Business

In the Imaging Business, consolidated net sales came to ¥65,574 million, down 16.2% year on year, while operating income amounted to ¥498 million, compared with operating loss of ¥2,064 million in the previous fiscal year. Net sales in the Imaging Business declined as a result of measures to achieve an appropriate business scale in conjunction with the contraction of the market as well as the delays in supplying certain products due to the impacts of the April 2016 Kumamoto earthquakes.

The Imaging Business returned to profitability after having recorded operating loss in the previous fiscal year due to progress made in curtailing expenses combined with the benefits of introducing new products, including the flagship mirrorless camera OLYMPUS OM-D E-M1 Mark II.

■ Others

In the Others Business, consolidated net sales amounted to ¥13,964 million, down 11.4% year on year, and operating loss was ¥4,621 million, compared with ¥5,800 million in the previous fiscal year. Net sales in the Others Business declined as a result of having reorganized our non-core business domains through initiatives that included transferring shares of subsidiary Nippon Outsourcing Corporation on October 31, 2016. In addition, operating loss decreased reflecting a reduction in expenses.

Fiscal 2018 Outlook

Looking ahead with respect to the global economy, concerns of a downturn in economic conditions are likely to intensify despite an overall trend of economic recovery, amid developments that include policy moves undertaken by the U.S. government and issues with respect to the United Kingdom's decision to leave the European Union. In the Japanese economy, despite the likelihood of ongoing recovery on the back of improved corporate earnings, prospects ahead remain uncertain amid negative factors that include growing uncertainties regarding the global economy and volatility in financial and capital markets.

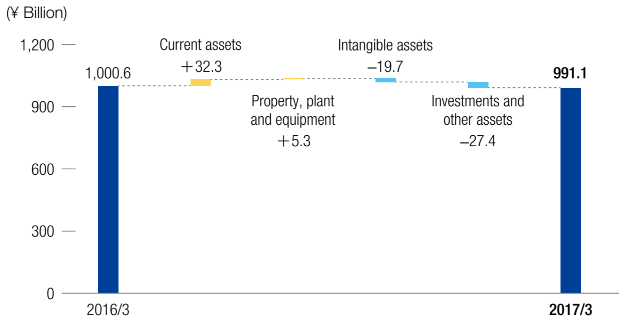
Given this environment, the Olympus Group will steadily press forward with 16CSP, the medium-term management plan that was drawn up during fiscal 2016.

In the Medical Business, we aim to expand the scale of our operations primarily by providing value in terms of both early diagnosis and minimally invasive therapies. To this end, we have been proactively investing in each of this segment's business units—namely, the GI&R (gastrointestinal and respiratory) Business Unit, the GS (general surgery) Business Unit, the Uro / Gyn (urology / gynecology) Business Unit, the ENT (ear, nose, and throat) Business Unit, and the MS (medical service) Business Unit. We will work to improve profitability in the Medical Business by achieving dramatic growth in both the endotherapy device and surgical device fields, maintaining our overwhelming competitive edge in the gastrointestinal endoscope field, and strengthening single-use device operations. In the Scientific Solutions Business, we will establish earnings foundations by promoting customer group-oriented strategies and by enhancing shared business functions and streamlining operations through globally integrated management. In the Imaging Business, we will establish a profitable operating structure by further boosting business efficiency while also pursuing initiatives geared toward improving our responsiveness to the changing market and further reducing inventory risks.

Financial Position

Total Assets

As of March 31, 2017, total assets stood at ¥991,062 million, down ¥9,552 million from a year earlier. Total current assets were up ¥32,300 million due mainly to an increase of ¥32,877 million in cash and deposits, and total non-current assets declined ¥41,852 million following decreases of ¥42,195 million in investment securities and ¥10,526 million in goodwill.



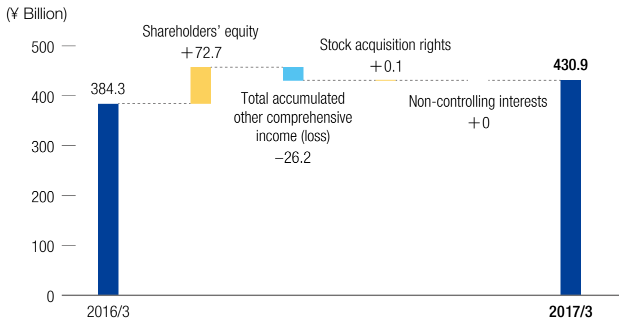
Liabilities

Total liabilities decreased ¥56,149 million compared with the end of the previous fiscal year, to ¥560,182 million, due mainly to a ¥46,977 million decrease in long-term borrowings, less current maturities and a ¥4,247 million decrease in short-term borrowings.

Total Net Assets and Equity Ratio

Total net assets at the end of the fiscal year amounted to ¥430,880 million, up ¥46,597 million from the previous fiscal year-end. This rise was primarily due to the posting of net income of ¥78,191 million, which offset the ¥26,210 million increase in total accumulated other comprehensive loss arising from fluctuations in foreign exchange rates and stock prices.

As a result of the above, the equity ratio increased from 38.2% at the end of the previous fiscal year to 43.3%.



Cash Flows

Cash Flows from Operating Activities

Net cash provided by operating activities was ¥90,194 million. Major factors increasing cash included ¥81,686 million in income before provision for income taxes as well as adjustments for non-cash items such as ¥44,658 million in depreciation and amortization, ¥8,642 million in amortization of goodwill, and ¥6,922 million in loss related to securities litigation. Major factors decreasing cash included ¥25,057 million in gain on available-for-sale securities, net and ¥14,801 million in increase in inventories.

Cash Flows from Investing Activities

Net cash used in investing activities was ¥8,305 million. Major factors decreasing cash included ¥43,542 million in purchases of property, plant and equipment and ¥7,358 million in repayments of loans receivable. Major factors increasing cash included ¥42,239 million in sales of investment securities.

Cash Flows from Financing Activities

Net cash used in financing activities was ¥44,244 million. Major factors decreasing cash included ¥30,000 million in redemption of bonds and ¥20,217 million in repayments of long-term borrowings. Major factors increasing cash included ¥20,000 million in proceeds from long-term borrowings.