

Disclaimer: This translation is prepared and provided for readers' convenience only. This summary does not constitute any guarantee, and the Company will not compensate any losses and/or damage stemming from actions taken based on these statements. In the case that there is any discrepancy between the Japanese and English versions, the Japanese version is assumed to be correct.



MEMBERSHIP  
February 10, 2017

## Summary of Non-consolidated Financial Results for the Fiscal Year ended December 31, 2016 (JGAAP)

**Listed company's name:** RaQualia Pharma Inc.  
**Listed on:** Tokyo Stock Exchange (TSE)  
**Stock code:** 4579  
**URL:** <http://www.raqualia.com/>  
**Representative:** Naoki Tani, President and CEO  
**Contact:** Kiichiro Kawada, Director and Executive Vice President (TEL) +81-52-446-6100  
**Scheduled date of general meeting of shareholders:** March 30, 2017  
**Scheduled date of dividend payment:** —  
**Scheduled date of filing of securities report:** March 31, 2017  
**Supplementary documents for financial results:** Yes  
**Financial results briefing:** Yes (for institutional investors and analysts)

(Amounts are rounded down to the nearest million yen.)

### 1. Non-consolidated financial results for the fiscal year ended December 31, 2016 (January 1, 2016 to December 31, 2016)

#### (1) Non-consolidated operating results

(Percentage figures represent changes from the previous fiscal year.)

Fiscal year ended	Net sales		Operating income		Ordinary income		Profit	
	million yen	%	million yen	%	million yen	%	million yen	%
December 31, 2016	705	384.7	(759)	—	(720)	—	(728)	—
December 31, 2015	145	(5.5)	(1,864)	—	(1,795)	—	(1,854)	—

  

Fiscal year ended	Earnings per share (Basic)	Earnings per share (Diluted)	Profit/equity	Ordinary income/total assets	Operating income/net sales
	yen	yen	%	%	%
December 31, 2016	(38.80)	—	(17.6)	(16.4)	(107.7)
December 31, 2015	(116.45)	—	(39.8)	(36.1)	(1,281.5)

Note: The financial figure that the Company presents as business revenues in the statement of income is displayed above as net sales.

#### (2) Non-consolidated financial position

As of	Total assets	Net assets	Equity ratio	Net assets per share
	million yen	million yen	%	yen
December 31, 2016	4,019	3,788	93.9	201.06
December 31, 2015	4,752	4,514	94.8	239.96

Reference: Equity As of December 31, 2016: 3,773 million yen As of December 31, 2015: 4,503 million yen

#### (3) Non-consolidated cash flows

Fiscal year ended	Cash flows from operating activities	Cash flows from investing activities	Cash flows from financing activities	Cash and cash equivalents at end of period
	million yen	million yen	million yen	million yen
December 31, 2016	(680)	(441)	—	1,087
December 31, 2015	(2,116)	665	1,701	2,243

## 2. Dividends

	Annual dividends per share					Total cash dividends (Total)	Dividend payout ratio	Ratio of dividends to net assets
	First quarter-end	Second quarter-end	Third quarter-end	Fiscal year-end	Total			
	yen	yen	yen	yen	yen	million yen	%	%
Fiscal year ended December 31, 2015	–	0.00	–	0.00	0.00	–	–	–
Fiscal year ended December 31, 2016	–	0.00	–	0.00	0.00	–	–	–
Fiscal year ending December 31, 2017 (forecast)	–	0.00	–	0.00	0.00		–	

## 3. Forecasts of non-consolidated financial results for the fiscal year ending December 31, 2017 (January 1, 2017 to December 31, 2017)

(Percentage figures represent changes from the previous year.)

	Net sales		Operating income		Ordinary income		Profit		Earnings per share (Basic)
	million yen	%	million yen	%	million yen	%	million yen	%	yen
Fiscal year ending December 31, 2017	1,100	56.0	(760)	–	(761)	–	(767)	–	(40.91)

Note: As the Company conducts performance management on an annualized basis, forecasts of results over a six-month period are omitted from this report.

### \* Notes

(1) Changes in accounting policies, changes in accounting estimates, and restatements of prior financial statements

- Changes in accounting policies due to the revisions to accounting standards and other regulations: Yes
- Changes in accounting policies due to other reasons: None
- Changes in accounting estimates: None
- Restatements of prior financial statements: None

(2) Number of issued shares (common shares)

a. Total number of issued shares at the end of the period (including treasury shares)

As of December 31, 2016	18,767,200 shares
As of December 31, 2015	18,767,200 shares

b. Total number of treasury shares at the end of the period

As of December 31, 2016	– shares
As of December 31, 2015	– shares

c. Average number of outstanding shares during the period

For the fiscal year ended December 31, 2016	18,767,200 shares
For the fiscal year ended December 31, 2015	15,923,610 shares

### \* Status of audit procedures for financial reports

This Summary of Financial Results is exempt from the external auditor's audit procedures for non-consolidated financial statements under the Financial Instruments and Exchange Act. Audit procedures for non-consolidated financial statements under the said Act are incomplete at the time of disclosure of this Summary of Financial Results.

### \* Appropriate use of financial forecasts and other special remarks

(Caution concerning forward-looking statements)

Forward-looking statements provided in this document, including financial forecasts, are based on the information currently available to the Company and certain assumptions considered reasonable. Such statements are included without any guarantee as to their future achievement. Actual results, etc. may differ materially from the forecasts depending on various factors. Please refer to "1. Analysis of business results and financial positions, (1) Analysis of business results" on page 2 of the attached material for the suppositions that form the assumptions for financial forecasts and cautions concerning the use of financial forecasts.

(Method of accessing supplementary documents for financial results and details of financial results briefing)

The Company plans to hold a financial results briefing for institutional investors and securities analysts on Monday, February 13, 2017.

The Company plans to post the documents used at the briefing on its website promptly after the briefing is held.

## Contents of attachment

1.	Analysis of business results and financial positions .....	2
(1)	Analysis of business results .....	2
(2)	Analysis of financial positions.....	5
(3)	Basic policy on profit distribution and dividends for fiscal years 2016 and 2017 .....	6
2.	Management policy.....	7
(1)	Basic policies for company management.....	7
(2)	Target management indicators .....	7
(3)	Medium- and long-term management strategy .....	7
(4)	Issues to address .....	8
(5)	Critical contracts for operation and others .....	9
3.	Basic rationale for selecting the accounting standard .....	15
4.	Non-consolidated financial statements .....	16
(1)	Non-consolidated balance sheet.....	16
(2)	Non-consolidated statement of income .....	18
(3)	Non-consolidated statement of changes in equity.....	19
(4)	Non-consolidated statement of cash flows.....	21
(5)	Notes to non-consolidated financial statements .....	23
	Non-consolidated statement of income .....	23
	Non-consolidated statement of changes in equity.....	23
	Significant subsequent event.....	26

## 1. Analysis of business results and financial positions

### (1) Analysis of business results

#### 1) Non-consolidated results for the fiscal year ended December 31, 2016

##### Overall trend

During the fiscal year under review, the Japanese economy was on a moderate recovery track with export-oriented companies reviving, in particular, supported by the solid performance of the U.S. economy that experienced the first policy interest rate hike by the Federal Reserve Board in nine and a half years. Meanwhile, the outlook for the Japanese economy remained uncertain amid a sense of caution about the economic policies of U.S. President-elect Donald Trump, who won the 58th U.S. presidential election conducted on November 8, 2016, coupled with political turmoil in Europe and concerns over potential deceleration of the Chinese and other emerging economies.

In the country's pharmaceutical sector, the Ministry of Health, Labour and Welfare has been continuing initiatives to rein in medical expenses. The sector's players are being faced with a highly exceptional and challenging business environment, as evidenced by the fact that, in the fiscal 2016 National Health Insurance drug price revision, the average drug price was reduced by a significant 6.47% and that the official price of some innovative drugs was decided to be lowered by the ministry as an emergency measure even prior to the expiration of the ongoing official price term. Consequently, individual pharmaceutical companies have been increasing their efforts in the selection process for compounds developed as pharmaceuticals. This situation has a non-negligible effect on the licensing activities of drug discovery venture such as the Company.

Against this backdrop, the Company pushed ahead with research and development and sales activities, aiming to continuously generate compounds developed as pharmaceuticals, to expand its research and development portfolio, and to license out developed compounds.

As for the status of clinical trials at our licensees, Phase III clinical trials of potassium-competitive acid blocker (RQ-00000004, "tegoprazan") licensed out to CJ HealthCare Corporation (South Korea) ("CJ HealthCare") continued smoothly in the country. Moreover, CJ HealthCare has been working to prepare for launching clinical trials of the compound in China. Meanwhile, as for a second generation (atypical) antipsychotic drug, ziprasidone, licensed out to Meiji Seika Pharma Co., Ltd. ("Meiji Seika Pharma"), Phase III clinical trials are progressing smoothly in Japan.

For two compounds licensed out to Aratana Therapeutics Inc. (U.S.) ("Aratana"), namely, Galliprant<sup>®</sup>, a pain management compound for dog osteoarthritis, and Entyce<sup>®</sup>, a dog anorexia management compound, Aratana has obtained the approval of the U.S. Food and Drug Administration ("FDA") and is continuing to prepare for the planned product rollouts slated for the fiscal year ending December 31, 2017. With regard to Galliprant<sup>®</sup>, Aratana has entered into a global strategic collaboration with Elanco Animal Health ("Elanco"), an animal pharmaceutical division of Eli Lilly and Company, and applied to the European Medicines Agency ("EMA") for approval in Europe. As for Entyce<sup>®</sup>, Aratana launched long-term toxicity studies on cats in December 2016, while also continuing a program to develop the compound as a potential cat anorexia management drug.

As for the status of clinical trials conducted by the Company itself, we completed Phase I clinical trials in Japan of tegoprazan in August 2015, thus verifying the compound to have the faster effect of reining in the secretion of stomach acids compared with the current products for treatment of gastro-esophageal reflux disease. The Company will continue striving to license out the compound. In addition, the Company has been making smooth progress with Phase I clinical trials in the U.K. for a 5-HT<sub>2B</sub> antagonist (RQ-00310941), a compound that is currently under development for indications of irritable bowel syndrome with diarrhea (IBS-D).

On the clinical research front, in investigator-initiated clinical trials of the Company's 5-HT<sub>4</sub> partial agonist (RQ-00000010) that were conducted by Virginia Commonwealth University, Parkinson's and Movement Disorders Center ("VCU") of the United States, a research partner of the Company, the compound has started to be prescribed to Parkinson's disease patients.

In addition, in a project for TRPM8 blocker compounds primarily for indications such as neuropathic pain, the Company completed the investigation of preclinical efficacy for compounds developed as pharmaceuticals (RQ-00434739), and its Board of Directors meeting held in August 2016 approved moving on to a preclinical phase.

In the area of collaboration with academia, the Company entered into an agreement on collaborative research for a retinopathy treatment drug with the Molecular Pharmacology, Biofunctional Evaluation of Gifu Pharmaceutical University (Hideaki Hara, Professor and Vice President) as well as an agreement on collaborative research for a non-alcoholic steatohepatitis (NASH) treatment drug with the Department of Molecular Medicine and Metabolism, Research Institute of Environmental Medicine of Nagoya University (Takayoshi Suganami, Professor). As such, proactive collaborative research activities through academic-industrial collaboration are progressing.

Financial results for the fiscal year ended December 31, 2016, the reporting period, were as follows. Business revenue for the period was 705 million yen, operating loss totaled 759 million yen, ordinary loss totaled 720 million yen, and loss was 728 million yen. Total business expenses were 1,465 million yen, of which 117 million yen in royalty payments was recorded under cost of business revenue. Moreover, research and development expenses were 796 million yen and other selling, general and administrative expenses totaled 551 million yen.

#### Research and development activities

Research and development expenses of the Company during the fiscal year ended December 31, 2016 were 796 million yen. The main components of these activities were as follows:

#### <RaQualia's research and development and collaborative research>

##### (A) Exploratory and discovery phase

The Company continued to examine a suitable administration method for a compound discovered in a project to evaluate a selective sodium channel blocker compound for indications such as inflammatory pain and neuropathic pain. In addition, the Company explored new lead compounds and discovered several candidate compounds.

The Company continued collaborative research with four companies.

Company	Start date	Content
EA Pharma Co., Ltd. (*Note)	October 2012	Collaboration on a specific ion channel target for gastrointestinal treatments
Interprotein Corporation	February 2013	Collaboration on a specific protein-protein interaction (PPI) inhibitor for pain treatments
XuanZhu Pharma Co., Ltd.	December 2015	Collaboration on a specific ion channel target for pain treatments
Asahi Kasei Pharma Corporation	January 2016	Collaboration on a specific ion channel target for pain treatments

Note: Effective April 1, 2016, EA Pharma Co., Ltd. was established as a new company that resulted from the integration of a portion of Eisai Co., Ltd.'s gastrointestinal disease treatment business and Ajinomoto Pharmaceuticals Co., Ltd., which was the successor company in the integration.

##### (B) Preclinical development phase

###### a) Ghrelin receptor agonist (RQ-00433412)

The compound is under development for cancer-related anorexia/cachexia syndrome. The Company has completed investigation of preclinical efficacy and has not detected any inadequacy for moving on to the next stage of performing preclinical development study.

###### b) TRPM8 blocker compounds (RQ-00434739)

The compound is under development for neuropathic pain (chemotherapy-induced cold allodynia). The Company has completed investigation of preclinical efficacy and has not detected any inadequacy for moving on to the next stage of performing preclinical development study.

###### c) Motilin receptor agonist (RQ-00201894)

The compound is under development for gastroparesis, functional dyspepsia and post-operative Ileus. The Company has completed the preclinical studies, including *in vivo* pharmacology studies, metabolism and pharmacokinetics studies, toxicity studies (GLP) and safety pharmacology studies (GLP), which were the prerequisite studies for Phase I clinical trials. So far, the Company has not detected any inadequacy for moving on to the next clinical development stage.

##### (C) Clinical development phase

###### a) 5-HT<sub>4</sub> partial agonist (RQ-00000010)

The compound is under development for gastroparesis, functional dyspepsia and chronic constipation. In August 2016, VCU, a research partner of the Company, launched investigator-initiated clinical trials of the compound. These trials, while obtaining a research grant from The Michael J. Fox Foundation for Parkinson's Research, are currently under way as a clinical research program aimed to examine the safety and efficacy of the compound for managing gastroparesis, a complication of Parkinson's disease patients.

**b) Potassium-competitive acid blocker (RQ-0000004, tegoprazan)**

The compound is under development for gastro-esophageal reflux disease (RE/NERD), and the Company completed the Phase I clinical trials in Japan, following those in the U.S. Utilizing data on clinical trials in South Korea where development has been underway, we will continue consultations toward licensing out the compound.

**c) 5-HT<sub>2B</sub> antagonist (RQ-00310941)**

For the compound, which is under development for irritable bowel syndrome with diarrhea (IBS-D), the Company launched the Phase I clinical trials for the first administration of the compound to human (involving healthy adults and patients) in July 2015 in U.K., which is currently ongoing.

**d) Second-generation semisynthetic lipoglycopeptide antibacterial agent (dalbavancin)**

The Company is now in the process of having consultations with the view to licensing out the agent in Japan. This agent was put on the U.S. market as a drug to treat acute bacterial skin and skin structure infections (ABSSSI) under the trademark of DALVANCE™. In Europe, in March 2015, we obtained regulatory approval for the distribution of this agent under the trademark of XYDALBA™.

**<Status of development at licensee corporation>**

**a) Potassium-competitive acid blocker (RQ-0000004, tegoprazan)**

The compound is under development primarily for gastro-esophageal reflux disease (RE/NERD) by CJ HealthCare, and is undergoing Phase III clinical trials in South Korea. In addition, preparations are under way to start its development in China.

**b) Serotonin 5-HT<sub>2A</sub> and dopamine D2 receptor blocker (ziprasidone)**

The compound is under development for schizophrenia by Meiji Seika Pharma Co., Ltd., and is undergoing Phase III clinical trials in Japan. The agent has already been marketed in 83 countries by Pfizer Inc. in the U.S., and is listed as a first-line drug in the U.S. Treatment Guidelines.

**c) EP4 antagonist (Galliprant®, RQ-0000007, AT-001, grapiprant)**

The compound was developed for pain management for pets by Aratana, a licensed partner of the Company. Following favorable results of clinical trials with dogs in the U.S., Aratana has obtained manufacturing and marketing approval with the FDA. The preparation for the commencement of sales in the first quarter of 2017 is currently underway by Aratana and Elanco. Furthermore, in Europe, application for the compound's approval has been submitted by Aratana to the EMA in February 2016, and such approval is currently being reviewed.

**d) Ghrelin receptor agonist (Entyce®, RQ-0000005, AT-002, capromorelin)**

The compound was developed for anorexia management for pets by Aratana. Following favorable results of clinical trials with dogs, Aratana has obtained manufacturing and marketing approval with the FDA. Preparations are underway for the commencement of sales coinciding with the North American Veterinary Community Conference slated for February 2017. While continuing the program to develop the compound as a cat anorexia management drug, Aratana launched long-term toxicity studies on cats in December 2016.

**e) EP4 antagonist (RQ-0000007, AAT-007, grapiprant)**

Preparations are currently underway at a licensee of AskAt Inc. ("AskAt") for implementing clinical trials.

**f) cyclooxygenase-2 (COX-2) inhibitor (RQ-00317076, AAT-076)**

Preparations are currently underway at a licensee of AskAt for implementing clinical trials.

**2) Outlook for the fiscal year ending December 31, 2017**

Looking ahead to the next fiscal year (the fiscal year ending December 31, 2017), on the business front, the Company will work steadily to secure profits by licensing out development compounds and managing alliances. On the research and development front, the Company will promote alliances and collaborative research with pharmaceutical companies and others through the advancement of projects at the exploratory and development phases, and thus enhance its corporate value.

On the revenue front, the Company will obtain from Aratana a certain amount of milestone payment as well as royalty corresponding to sales if, under the out-licensing agreement entered into by and between both parties in December 2010, Aratana launches sales in the U.S. of EP4 antagonist (Galliprant®, RQ-0000007, AT-001, grapiprant), and Ghrelin receptor agonist (Entyce®, RQ-0000005, AT-002, capromorelin). Moreover, under the joint research agreement by and between the Company and Asahi Kasei Pharma Corporation, the former will continue to obtain research collaboration fund from the latter and will obtain from it a milestone payment if certain results are attained. The Company will also obtain a research collaboration fund as the collaborative research projects with pharmaceutical companies including XuanZhu Pharma Co., Ltd. (China) progress. Meanwhile, as for tegoprazan, licensee CJ HealthCare is currently preparing for a clinical trial process in China. After it is launched, the Company will obtain a milestone payment from the licensee. While

considering in-house development of medicinal drug compounds candidates under clinical development phase, such as dalbavancin as well as the ion channel drug discovery, the Company aims to partner with pharmaceutical companies via out-licensing agreements.

With regard to costs, business expenses are expected to fall substantially in an ongoing effort to cut operating costs, and in addition, a voluntary retirement scheme in fiscal 2015 and employees' salary revision in fiscal 2016 have been implemented. On the other hand, the Company plans to engage in continued research and development activities aimed at earning further revenue in the future, and will likely incur research and development expenses related to the termination of clinical trials.

As for the outlook of non-consolidated financial results for the fiscal year ending December 31, 2017, the Company forecasts business revenues of 1,100 million yen, operating loss of 760 million yen, ordinary loss of 761 million yen and loss of 767 million yen.

The forecast figures presented above are based on the information currently available to the Company and certain assumptions considered reasonable. Such statements are included without any guarantee as to their future achievement. Actual results, etc., may differ materially from the forecasts depending on various factors. The outlook for fiscal 2017 is based on the assumption that Aratana, the licensee, is to commence sales in the U.S. and that CJ HealthCare is to start clinical trials in China, and thus actual results may differ from the financial forecast depending on the regulatory review. In the case where the Company acknowledges the need to revise the financial forecast, it will disclose such information promptly.

## **(2) Analysis of financial positions**

### **1) Status of assets, liabilities and net assets**

#### Assets

Total assets as of December 31, 2016 were 4,019 million yen. The major components were 1,427 million yen in cash and deposits, 205 million yen in advance payments - trade, and 1,937 million yen in investment securities.

#### Liabilities

Total liabilities as of December 31, 2016 were 231 million yen. The major components were 125 million yen in accounts payable - other, 40 million yen in accrued expenses, and 30 million yen in deferred tax liabilities.

#### Net assets

Total net assets as of December 31, 2016 were 3,788 million yen (down 16.1% from the previous fiscal year). The major components were 2,237 million yen in capital stock, 2,237 million yen in capital surplus, negative 728 million yen in retained earnings, and 26 million yen in valuation difference on available-for-sale securities. The equity ratio was 93.9%.

### **2) Status of cash flows**

The balance of cash and cash equivalents ("cash") as of December 31, 2016 amounted to 1,087 million yen, a decrease of 1,155 million yen compared with the end of the previous fiscal year.

The respective cash flows in the fiscal year ended December 31, 2016 and the factors thereof are as follows.

#### Cash flows from operating activities

Net cash used in operating activities was 680 million yen (compared with 2,116 million yen used a year earlier). This is mainly attributable to loss before income taxes of 722 million yen, depreciation of 79 million yen, interest and dividend income received of 61 million yen and payments for extra retirement payments of 32 million yen.

#### Cash flows from investing activities

Net cash used in investing activities was 441 million yen (compared with 665 million yen provided a year earlier). This is primarily due to the purchase of investment securities of 426 million yen and the purchase of property, plant and equipment of 35 million yen, although there were proceeds from redemption of securities of 300 million yen, proceeds from redemption of investment securities of 185 million yen.

#### Cash flows from financing activities

Cash flows from financing activities were non-existent (compared with 1,701 million yen provided a year earlier).

(Reference) Trend in cash flow-related indicators

	Fiscal year ended December 31, 2012	Fiscal year ended December 31, 2013	Fiscal year ended December 31, 2014	Fiscal year ended December 31, 2015	Fiscal year ended December 31, 2016
Equity ratio (%)	96.5	85.9	89.6	94.8	93.9
Market value equity ratio (%)	83.9	138.9	125.3	132.69	184.90
Interest-bearing debt to cash flow ratio (years)	–	–	–	–	–
Interest coverage ratio (factor)	–	–	–	–	–

Equity ratio: equity / total assets

Market value equity ratio: market capitalization / total assets

Interest-bearing debt to cash flow ratio: interest-bearing debt / cash flow

Interest coverage ratio: cash flow / paid interest

- Notes: 1. Figures are obtained from the consolidated financial statements for the fiscal year ended December 31, 2013 and the fiscal year ended December 31, 2014 and from non-consolidated financial statements for other fiscal years.
2. Interest-bearing debt to cash flow ratio and interest coverage ratio are not provided since operating cash flow was a minus figure.

**(3) Basic policy on profit distribution and dividends for fiscal years 2016 and 2017**

The Company is a bio venture company specializing in drug discovery research. Therefore, looking forward, the Company must continually conduct research and development activities. In view of this, we have decided to concentrate on securing internal reserves and to attach priority on securing funds for the continuation of research and development activities without paying dividends. Therefore, because we presently remain in a situation where we continue to record a loss, we have not carried out profit distributions. Since we expect to also record a loss in the next fiscal year, we plan not to carry out profit distributions in that fiscal year.

Nevertheless, we consider the distribution of profits to shareholders to be an important management issue, and we intend to make future profit distributions a continual consideration.



## **2. Management policy**

### **(1) Basic policies for company management**

The Company is a research and development-oriented drug discovery company whose aim is to create new pharmaceutical products leveraging its cutting-edge science and technology focusing on medical fields where patients have the greatest need. The foundation of our business development is the acquisition of revenue from upfront payment, milestones and royalties by licensing out the original development compounds for new drugs that we discover to pharmaceutical companies and others. The basic policies of the Company are as below.

- 1) We will establish an integrated drug discovery business model from exploratory research and initial development right through to licensing out, with the aim of setting up and streamlining our system.
- 2) We will strive to generate innovative development compounds by conducting cutting-edge drug discovery research through industry-academia-government collaboration research.
- 3) We will build relationships of trust with our business partners, resulting in dependable business outcomes.

### **(2) Target management indicators**

The Company will aim for sustained growth by promoting research and development into drugs and licensing out the compounds discovered as a result of exploratory research, preclinical trials and initial clinical trials as well as securing revenue through the commercialization and marketing carried out by licensees. We are pursuing business activities with the objective of licensing out a large number of development compounds at an early stage by further enhancing our research and development projects and promoting research and development of each development compound.

### **(3) Medium- and long-term management strategy**

Research and development of pharmaceuticals generally requires considerable time and expense. In addition, the chances of success are not high as there are various risks before a development compound comes to market, including circumstances such as suspension or delay of research and development due to efficacy, safety and other problems at each phase of the research and development.

Under such circumstances, the Company is developing its business based on the following strategies.

#### **1) Licensing-out and alliance management strategy**

The Company has developed responsive and flexible activities for licensing-out by making its entire research and development portfolio available for licensing out at each stage from the initial exploratory phase through to the development phase. Although the top priority objective for the Company's research and development portfolio is the licensing-out of worldwide development, marketing and manufacturing rights, the Company's policy aims for licensing out in a variety of forms in order to maximize revenue, including licensing out for each region and licensing out for each dosage form as well as licensing out for animal pharmaceutical applications in accordance with the characteristics of each project and the needs of the client pharmaceutical companies and others.

Furthermore, the Company supports promotion of satisfactory development for its compounds developed as pharmaceuticals that have already been licensed out based on the structure of the collaboration with each licensee corporation, implementing alliance management with the aim of achieving acquisition of revenue at the earliest stage possible as well as acquiring stable revenue over the long term.

#### **2) Research and development strategy**

##### **(A) Continuous reinforcement of research and development portfolio**

Since its foundation, the Company has been working on the generation of new development compounds with pain and gastrointestinal diseases as the core of our research and development program. The Company established a new division for academic-industrial research collaboration in Nagoya University in fiscal year 2014, and has since been engaging in joint research projects, ranging from cutting-edge drug discovery research to generation of innovative development compounds.

In addition, the Company will continue to undertake Research Collaboration projects, which it is conducting with domestic and overseas pharmaceutical companies, with the aim of continually strengthening its research and development portfolio.

##### **(B) Enhancement of development project value and achievement of revenue at an early stage**

The clinical trial phase requires considerable research and development expenses. Therefore, the Company has been implementing "Selection and Concentration" with regard to its development compounds with the aim of reducing research and development expenses and the burden of risk. In addition to concentrating internal resources on selected programs, we will further enhance project value through the utilization of external project finance and other means as needed to achieve early acquisition of revenue. Moreover, we aim to acquire future revenue through the acceleration of development.

#### **(4) Issues to address**

The Company will work on the following as its main business challenges, with the aim of achieving profitable research results in the medium and long-term.

##### **1) Reinforce the research and development portfolio**

In order to enhance corporate value as a drug discovery venture company, the Company needs to continuously generate highly innovative development compounds and strengthen its research and development portfolio. In the U.S., which leads the world in drug development, nearly 60 percent of newly launched drugs are said to be developed by academia or drug discovery venture companies. Amid the progress of drug discovery by academia and drug discovery venture companies in Japan, the Company established a new division for academic-industrial research collaboration in Nagoya University in fiscal 2014, and is working on generation of innovative development compounds based on the cutting-edge drug discovery research in academia.

To this end, the Company will implement the following measures:

- Early generation of development compounds leveraging its unique assessment system, related database, etc., and expansion of new indications
- Early generation of development compounds through joint research that leverages the Company's strength in ion channel drug discovery
- Advancement of exploratory research activities through industry-academia-government collaboration and expansion of new development compounds based on cutting-edge drug discovery research

##### **2) Enhance the value of each project by selection and concentration of resources**

The Company will take the following measures according to the status of development compounds, in order to advance research and development of development compounds it owns by leveraging funds and human resources effectively.

- Licensing out preparation program... Program in which the Company promotes a focus on independent research and development of development compounds mainly at the exploratory phase and Phase I clinical trials in which the Company has strength for the purpose of future out-licensing.
- Licensed out program ..... Program whereby the Company mainly provides support to clinical development for which licensee corporation take the initiative in conducting Phase II and Phase III clinical trials.
- Research collaboration program ..... Program whereby the Company and pharmaceutical company combine our respective strengths mainly at the explorative stage to generate innovative development compounds.

##### **3) Strengthen the activities for licensing out and bolster alliance management functions**

In order for the Company to commercialize its portfolio of development compounds, it is necessary that the Company conduct clinical development. In the meantime, the Company needs to tie up with pharmaceutical companies and license out in order to advance development and minimize risk. The Company has thus set this as a high-priority issue and is working globally on licensing out activities through various channels. After licensing out, the Company will actively support promotion of development by providing data to and periodically communicating with licensee corporation, with the aim to achieve commercialization of licensed out products as early as possible.

##### **4) Strengthen business foundation**

Drug discovery venture companies including the Company need to reliably obtain financing according to its operating activities as its pipeline development progresses, accompanied by growing development compounds, during the period until its products are put on the market. For this reason, in an effort to secure and broaden the scope of its financing means, the Company will diversify its financing activities in the form of obtaining necessary cash through the equity market and acquiring loans from banks. Moreover, the Company will strive to further bolster its financial position by reining in costs through rigorous budget control efforts.

##### **5) Recruit personnel**

We consider talented human resources as the Company's most important business resource. Thus, in the coming years, we will acquire appropriate talented human resources as we see fit in order to continue to explore and develop new drugs and expand the scope of their applications.

**(5) Critical contracts for operation and others**

The critical contracts for the Company's operation are as below.

1) Agreements relating to the establishment of Industry-Academia Collaborative Chair (or laboratories)

Agreement title	ESTABLISHMENT OF NEW ACADEMIC-INDUSTRIAL RESEARCH COLLABORATION DIVISION AGREEMENT
Agreement partner	Nagoya University
Date of execution	February 18, 2014
Term of agreement	Three years starting on April 1, 2014
Main content of agreement	a) The Company will establish the Industry-Academia Collaborative Chair (course name: Division for the analytical study of pharmacology efficacy) in Nagoya University's Research Institute of Environmental Medicine (Furo-cho, Chikusa-ku, Nagoya, Aichi Prefecture). b) In line with the establishment of this division for academic-industrial research collaboration Nagoya University will provide the facility and associated services (utilities), and the Company will use the facility and associated services. c) The Company will pay Nagoya University the specified research expenses and academic-industrial research collaboration promotion expenses.

Agreement title	ESTABLISHMENT OF NEW ACADEMIC-INDUSTRIAL RESEARCH COLLABORATION LABORATORY AGREEMENT
Agreement partner	Nagoya University
Date of execution	February 17, 2015
Term of agreement	Three years starting on April 1, 2015
Main content of agreement	a) The Company will establish the laboratory for academic-industrial research collaboration (course name: Laboratory of Pharmaceutical Sciences & Analytical Chemistry) in Nagoya University Graduate School of Medicine (Furo-cho, Chikusa-ku, Nagoya, Aichi Prefecture). b) In line with the establishment of this laboratory for academic-industrial research collaboration Nagoya University will provide the facility and associated services (utilities), and the Company will use the facility and associated services. c) The Company will pay Nagoya University the specified research expenses and academic-industrial research collaboration promotion expenses.

Agreement title	ESTABLISHMENT OF NEW ACADEMIC-INDUSTRIAL RESEARCH COLLABORATION LABORATORY AGREEMENT
Agreement partner	Nagoya University
Date of execution	February 17, 2015
Term of agreement	Three years starting on April 1, 2015
Main content of agreement	a) The Company will establish the laboratory for academic-industrial research collaboration (course name: Laboratory of Medicinal Chemistry) in Nagoya University Graduate School of Pharmaceutical Sciences (Furo-cho, Chikusa-ku, Nagoya, Aichi Prefecture). b) In line with the establishment of this laboratory for academic-industrial research collaboration Nagoya University will provide the facility and associated services (utilities), and the Company will use the facility and associated services. c) The Company will pay Nagoya University the specified research expenses and academic-industrial research collaboration promotion expenses.

2) Agreements relating to transfer and license of intellectual property

Agreement title	INTELLECTUAL PROPERTY TRANSFER & LICENSE AGREEMENT
Agreement partner	Pfizer Inc. (U.S.)
Date of execution	June 30, 2008
Term of agreement	Fifty years starting on June 30, 2008
Main content of agreement	<p>a) Pfizer Inc. will transfer the intellectual property rights or license (includes the right to sublicense) the use of intellectual property rights relating to a number of projects at the exploratory phase and development phase to the Company.</p> <p>b) The Company will pay Pfizer Inc. the consideration for a) and the ANIDULAFUNGIN MARKETING RIGHTS AGREEMENT, DALBAVANCIN MARKETING RIGHTS AGREEMENT and ZIPRASIDONE HCL / ZIPRASIDONE MESYLATE MARKETING RIGHTS AGREEMENT below.</p> <p>c) The Company will pay Pfizer Inc. royalties for specified compounds from among the number of compounds covered by the aforementioned a).</p>

Note: Payment of the consideration for b) above was completed on July 14, 2008.

Agreement title	ANIDULAFUNGIN MARKETING RIGHTS AGREEMENT
Agreement partner	Pfizer Inc. (U.S.)
Date of execution	June 30, 2008
Term of agreement	From June 30, 2008 until marketing in Japan ceases
Main content of agreement	<p>a) Pfizer Inc. will license development, commercialization and formulation manufacturing rights and sublicensing rights pertaining to Andulafungin in Japan to the Company, and the Company will pay the consideration provided for in the separate INTELLECTUAL PROPERTY TRANSFER &amp; LICENSE AGREEMENT.</p> <p>b) The Company will pay Eli Lilly and Company, which owns the patent for the compound, milestones after regulatory approval in Japan and royalties after the commencement of marketing.</p>

Agreement title	ZIPRASIDONE HCL / ZIPRASIDONE MESYLATE MARKETING RIGHTS AGREEMENT
Agreement partner	Pfizer Inc. (U.S.)
Date of execution	June 30, 2008
Term of agreement	From June 30, 2008 until marketing in Japan ceases
Main content of agreement	Pfizer Inc. will license development, commercialization and formulation manufacturing rights and sublicensing rights pertaining to Ziprasidone HCL / Ziprasidone Mesylate in Japan to the Company, and the Company will pay the consideration provided for in the separate INTELLECTUAL PROPERTY TRANSFER & LICENSE AGREEMENT.

Note: The Company sublicensed the development, marketing and formulation manufacturing rights pertaining to ZiprasidoneHCL / Ziprasidone Mesylate in Japan to Meiji Seika Pharma Co., Ltd. on March 14, 2011 in exchange for receipt of certain considerations. Details on the content of the agreement are as described in 5) Agreement relating to sublicense of rights below.

3) Agreements relating to transfer of rights

Agreement title	SALE AND PURCHASE AGREEMENT
Agreement partner	AskAt Inc.
Date of execution	January 29, 2013
Main content of agreement	<p>a) The Company will transfer all intellectual property rights pertaining to the EP4 antagonist (RQ-00000007, grapiprant) to AskAt Inc.</p> <p>b) With the conclusion of this Agreement, the Company will receive a certain rate of the revenue that AskAt Inc. earns from RQ-00000007 (grapiprant) as royalties as the consideration for the conclusion of this Agreement.</p>

Note: Notwithstanding this Agreement, the Company will not transfer to AskAt Inc. its status under each of the out-licensing agreements concluded with Maruishi Pharmaceutical Co., Ltd. dated August 4, 2010 and with Aratana Therapeutics, Inc. dated December 27, 2010. The details of the out-licensing agreement with each company are as described below in "4) Agreements relating to licensing out (A) EP4 antagonist (RQ-00000007, grapiprant)," "LICENSE AGREEMENT," and "EXCLUSIVE IP LICENSE AGREEMENT FOR RQ-00000007," respectively.

Agreement title	SALE AND PURCHASE AGREEMENT
Agreement partner	AskAt Inc.
Date of execution	January 29, 2013
Main content of agreement	<p>a) The Company will transfer all intellectual property rights pertaining to the EP4 antagonist (RQ-00000008) to AskAt Inc.</p> <p>b) With the conclusion of this Agreement, the Company will receive a certain rate of the revenue that AskAt Inc. earns from RG-00000008 as royalties as the consideration for the conclusion of this Agreement.</p>

Agreement title	SALE AND PURCHASE AGREEMENT
Agreement partner	AskAt Inc.
Date of execution	January 29, 2013
Main content of agreement	<p>a) The Company will transfer all intellectual property rights, related data and the relevant compound ingredients pertaining to the cyclooxygenase-2 (COX-2) inhibitor (RQ-00317076) to AskAt Inc.</p> <p>b) With the conclusion of this Agreement, the Company will receive a certain rate of the revenue that AskAt Inc. earns from RQ-00317076 as royalties as the consideration for the conclusion of this Agreement.</p>

Agreement title	SALE AND PURCHASE AGREEMENT
Agreement partner	AskAt Inc.
Date of execution	January 29, 2013
Main content of agreement	<p>a) The Company will transfer data and compounds required for research pertaining to the 5-HT<sub>4</sub> partial agonist (RQ-00000009) to AskAt Inc.</p> <p>b) With the conclusion of this Agreement, the Company will receive a certain rate of the revenue that AskAt Inc. earns from RG-00000009 as royalties as the consideration for the conclusion of this Agreement.</p>

Agreement title	SALE AND PURCHASE AGREEMENT
Agreement partner	AskAt Inc.
Date of execution	November 1, 2015
Main content of agreement	<p>a) The Company will transfer all intellectual property rights and related data and compound ingredients pertaining to the CB2 antagonist project to AskAt Inc.</p> <p>b) With the conclusion of this Agreement, the Company will receive a certain rate of the revenue that AskAt Inc. earns from the said project as royalties as the consideration for the conclusion of this Agreement.</p>

4) Agreements relating to licensing out

(A) EP4 antagonist (RQ-00000007, grapiprant)

This development compound was transferred by Pfizer Inc. Under the INTELLECTUAL PROPERTY TRANSFER & LICENSE AGREEMENT dated June 30, 2008 between the Company and Pfizer Inc., the parties agreed to the effect that in the event that the Company licenses out rights to a third party, the Company will pay Pfizer Inc. an amount calculated by multiplying the revenue obtained through licensing out (upfront payment, milestones and royalties, etc.) by a certain rate. The details of the INTELLECTUAL PROPERTY TRANSFER & LICENSE AGREEMENT are as described in 2) Agreements relating to transfer and license of intellectual property above.

Agreement title	LICENSE AGREEMENT
Agreement partner	Maruishi Pharmaceutical Co., Ltd.
Date of execution	August 4, 2010
Term of agreement	From the date of execution of the agreement until development, manufacture and marketing of the development compound by Maruishi Pharmaceutical Co., Ltd. or its sublicensees cease
Main content of agreement	<p>a) The Company will grant Maruishi Pharmaceutical Co., Ltd. exclusive license with sublicense rights for the development, marketing and manufacture for the intravenous formulation of EP4 antagonist (RQ-00000007, grapiprant) as a human and animal pharmaceutical in Japan and the East Asia region (South Korea, China and Taiwan).</p> <p>b) Maruishi Pharmaceutical Co., Ltd. has options to add countries in Asia other than Japan and East Asia and countries in Europe and the United States to the region covered by the Agreement.</p> <p>c) The Company has an obligation to provide Maruishi Pharmaceutical Co., Ltd. with the active pharmaceutical ingredient.</p> <p>d) With the conclusion of this Agreement, the Company will receive an upfront payment, milestones corresponding to the stage of development, and royalties in proportion to sales of the product as the consideration for a) through c) above. Furthermore, the Company will receive an incentive payment if the pharmaceutical's sales in Japan exceed a certain amount.</p> <p>e) In the event that Maruishi Pharmaceutical Co., Ltd. sublicenses its rights to a third party outside Japan, the Company will receive a certain rate of the revenue that Maruishi Pharmaceutical Co., Ltd. earns as a result of the sublicense.</p>

- Notes: 1. In conjunction with the partial amendment of the content of the Agreement, the AGREEMENT RELATING TO PARTIAL AMENDMENT OF THE LICENSE AGREEMENT was concluded on December 24, 2010, and the content above reflects the content of the amended agreement.
2. Among the options in b) above, the exclusive license with sublicense rights for development, marketing and manufacture as an animal pharmaceutical was extinguished in conjunction with the conclusion of an out-licensing agreement between the Company and Aratana Therapeutics, Inc. (U.S.) The details of the out-licensing agreement with Aratana Therapeutics, Inc. are as described in EXCLUSIVE IP LICENSE AGREEMENT FOR RQ-00000007 below.

Agreement title	EXCLUSIVE IP LICENSE AGREEMENT FOR RQ-00000007
Agreement partner	Aratana Therapeutics, Inc. (U.S.)
Date of execution	December 27, 2010
Term of agreement	From the date of execution of the agreement until canceled under the conditions provided for in the agreement
Main content of agreement	<p>a) The Company will grant Aratana Therapeutics, Inc. exclusive license with sublicense rights for the worldwide development, marketing and manufacture of an EP4 antagonist (RQ-00000007, grapiprant) as an animal pharmaceutical. (However, the right to the intravenous formulation of animal pharmaceuticals in Japan, South Korea, China and Taiwan is excluded.)</p> <p>b) The Company will supply a certain volume of the active pharmaceutical ingredient and the formulation that it already holds to Aratana Therapeutics, Inc. without compensation for the purpose of clinical trials.</p> <p>c) With the conclusion of this Agreement, the Company will receive an upfront payment, milestones corresponding to the stage of development, and royalties in proportion to sales of the product as the consideration for a) and b) above.</p>

Note: As of December 31, 2016, the Company owns common shares in Aratana Therapeutics, Inc.

(B) Ghrelin receptor agonist (RQ-00000005, capromorelin)

Agreement title	EXCLUSIVE IP LICENSE AGREEMENT FOR RQ-00000005
Agreement partner	Aratana Therapeutics, Inc. (U.S.)
Date of execution	December 27, 2010
Term of agreement	From the date of execution of the agreement until canceled under the conditions provided for in the agreement
Main content of agreement	<p>a) The Company will grant Aratana Therapeutics, Inc. exclusive license with sublicense rights for the worldwide development, marketing and manufacture of the Ghrelin receptor agonist (RQ-00000005, capromorelin) as an animal pharmaceutical.</p> <p>b) The Company will supply a certain volume of the active pharmaceutical ingredient and the formulation that it already holds to Aratana Therapeutics, Inc. without compensation for the purpose of clinical trials.</p> <p>c) With the conclusion of this Agreement, the Company will receive an upfront payment, milestones corresponding to the stage of development, and royalties in proportion to sales of the product as the consideration for a) and b) above.</p>

Note: As of December 31, 2016, the Company owns common shares in Aratana Therapeutics, Inc.

(C) 5-HT<sub>4</sub> partial agonist (RQ-00000010)

Agreement title	LICENSE AGREEMENT
Agreement partner	CJ HealthCare Corporation (South Korea)
Date of execution	July 28, 2011
Term of agreement	From the date of execution of the agreement until CJ HealthCare Corporation's obligation to pay royalties to the Company ceases
Main content of agreement	<p>a) The Company will grant CJ HealthCare Corporation exclusive license with sublicense rights for development, marketing and manufacture of the 5-HT<sub>4</sub> partial agonist (RQ-00000010) as a human pharmaceutical in South Korea, China (includes Hong Kong), Taiwan, India and the Southeast Asia region.</p> <p>b) With the conclusion of this Agreement, the Company will receive an upfront payment, milestones corresponding to the stage of development, and royalties in proportion to sales of the product as the consideration for a) above.</p>

(D) Potassium-competitive acid blocker (RQ-00000004, tegoprazan and RQ-00000774)

Agreement title	LICENSE AGREEMENT
Agreement partner	CJ HealthCare Corporation (South Korea)
Date of execution	September 3, 2010
Term of agreement	From the date of execution of the agreement until CJ HealthCare Corporation's obligation to pay royalties to the Company ceases
Main content of agreement	<p>a) The Company will grant CJ HealthCare Corporation exclusive license with sublicense rights for development, marketing and manufacture of Potassium-competitive acid blocker (RQ-00000004, tegoprazan and RQ-00000774) as human pharmaceuticals in South Korea, China (includes Hong Kong) and Taiwan.</p> <p>b) The Company will grant CJ HealthCare Corporation an option guaranteeing the same rights as in a) above with regard to backup compounds.</p> <p>c) With the conclusion of this Agreement, the Company will receive an upfront payment, milestones corresponding to the stage of development, and royalties in proportion to sales of the product as the consideration for a) and b) above.</p>

Agreement title	LICENSE AGREEMENT FOR RQ-00000004 (CJ-12420) AND RQ-00000774 IN SOUTHEAST ASIAN COUNTRIES
Agreement partner	CJ HealthCare Corporation (South Korea)
Date of execution	November 27, 2014
Term of agreement	From the date of execution of the agreement until CJ HealthCare Corporation's obligation to pay royalties to the Company ceases
Main content of agreement	<ul style="list-style-type: none"> <li>a) The Company will grant CJ HealthCare Corporation exclusive license with sublicense rights for development, marketing and manufacture of Potassium-competitive acid blocker (RQ-00000004, tegoprazan and RQ-00000774) as human pharmaceuticals in Southeast Asian countries.</li> <li>b) The Company will grant CJ HealthCare Corporation an option guaranteeing the same rights as in a) above with regard to backup compounds.</li> <li>c) With the conclusion of this Agreement, the Company will receive an upfront payment and royalties in proportion to sales of the product as the consideration for a) and b) above.</li> </ul>

5) Agreement relating to sublicense of rights

Agreement title	SUBLICENSE AGREEMENT
Agreement partner	Meiji Seika Pharma Co., Ltd.
Date of execution	March 14, 2011
Term of agreement	From the date of execution of the agreement until marketing in Japan ceases, except for termination under the condition provided for in the agreement
Main content of agreement	<ul style="list-style-type: none"> <li>a) The Company grants Meiji Seika Pharma Co., Ltd. exclusive license with sublicense rights for development, marketing and manufacture in Japan of ZIPRASIDONE HCL/ZIPRASIDONE MESYLATE licensed to the Company by Pfizer Inc. under the ZIPRASIDONE HCL / ZIPRASIDONE MESYLATE MARKETING RIGHTS AGREEMENT.</li> <li>b) With the conclusion of this Agreement, the Company will receive an upfront payment, milestones corresponding to the stage of development, and royalties in proportion to sales of the product as the consideration for a) above.</li> </ul>

Note: The milestones and royalties in b) above may change depending on the status of clinical trials.

6) Agreements relating to collaborative research

Agreement title	JOINT RESEARCH AGREEMENT
Agreement partner	EA Pharma Co., Ltd. (Note 1)
Date of execution	October 31, 2012
Term of agreement	Thirty months from the date of execution of the agreement (Note 2)
Main content of agreement	<ul style="list-style-type: none"> <li>a) The Company will conduct joint exploratory research with EA Pharma Co., Ltd. on compounds for a specific ion channel.</li> <li>b) EA Pharma Co., Ltd. will develop and commercialize any compounds that are discovered as a result of the joint research.</li> <li>c) The Company will receive an upfront payment with the conclusion of the Agreement as consideration for commencement of a) above and research grants as consideration for execution of a). The Company will also receive milestones corresponding to the development, regulatory approval and commercialization of any compounds that are discovered as a result of the joint research.</li> <li>d) The Company will receive royalties at a certain rate of sales after any products are brought to market.</li> </ul>

Notes: 1. Effective April 1, 2016, EA Pharma Co., Ltd. was established as a new company that resulted from the integration of a portion of Eisai Co., Ltd.'s gastrointestinal disease treatment business and Ajinomoto Pharmaceuticals Co., Ltd., which was the successor company in the integration. Accordingly, the above-mentioned agreement was succeeded on April 1, 2016, by EA Pharma Co., Ltd. from Ajinomoto Pharmaceuticals Co., Ltd.

2. In accordance with the Memorandum of Understanding, the expiration date of the agreement has been extended to April 30, 2017.



Agreement title	JOINT RESEARCH AGREEMENT
Agreement partner	Asahi Kasei Pharma Corporation
Date of execution	January 1, 2016
Term of agreement	Three years from January 1, 2016
Main content of agreement	<ul style="list-style-type: none"> <li>a) The Company will conduct joint exploratory research with Asahi Kasei Pharma Corporation on compounds developed as pharmaceuticals for a specific ion channel.</li> <li>b) The Company will receive research grants as consideration for execution of the aforementioned a). Furthermore, in the event that compounds developed as pharmaceuticals are generated as a result of this joint research, at that point the Company will receive a completion bonus.</li> <li>c) In the event that compounds developed as pharmaceuticals are generated as a result of this joint research, the Company will conclude a license agreement with Asahi Kasei Pharma Corporation regarding said compounds developed as pharmaceuticals.</li> </ul>

Agreement title	Collaboration Agreement
Agreement partner	XuanZhu Pharma Co., Ltd. (China)
Date of execution	December 22, 2015
Term of agreement	Three years from December 22, 2015
Main content of agreement	<ul style="list-style-type: none"> <li>a) The Company will conduct joint exploratory research with XuanZhu Pharma Co., Ltd. on compounds for a specific ion channel.</li> <li>b) The Company will receive an upfront payment with the conclusion of the Agreement as consideration for commencement of a) above and research grants as consideration for execution of a).</li> <li>d) In the event that compounds are generated as a result of this joint research, the Company will conclude a license agreement with XuanZhu Pharma Co., Ltd. regarding said compounds.</li> </ul>

### 3. Basic rationale for selecting the accounting standard

The Company has adopted Japanese accounting standards to ease the cost, etc., of parallel disclosure of reporting under both Japanese accounting standards and international financial reporting standards (IFRS).

As for the future, we intend to further the consideration on application of IFRS in light of the change in the ratio of foreign shareholders and trends in the application of IFRS by domestic sector peer companies.

#### 4. Non-consolidated financial statements

##### (1) Non-consolidated balance sheet

(Thousands of yen)

	As of December 31, 2015	As of December 31, 2016
<b>Assets</b>		
Current assets		
Cash and deposits	1,840,239	1,427,817
Accounts receivable - trade	72,866	58,265
Securities	503,037	9,128
Supplies	7,148	7,125
Advance payments - trade	179,368	205,236
Prepaid expenses	65,488	55,538
Other	39,639	43,380
Total current assets	2,707,787	1,806,492
Non-current assets		
Property, plant and equipment		
Buildings	140,198	140,568
Tools, furniture and fixtures	394,484	451,833
Accumulated depreciation	(273,392)	(343,662)
Total property, plant and equipment	261,290	248,739
Intangible assets		
Trademark right	2,306	5,546
Software	8,213	6,816
Other	3,708	431
Total intangible assets	14,228	12,794
Investments and other assets		
Investment securities	1,751,779	1,937,383
Long-term prepaid expenses	5,479	3,198
Other	11,545	10,705
Total investments and other assets	1,768,805	1,951,288
Total non-current assets	2,044,324	2,212,822
Total assets	4,752,112	4,019,314

(Thousands of yen)

	As of December 31, 2015	As of December 31, 2016
<b>Liabilities</b>		
Current liabilities		
Accounts payable - other	123,405	125,985
Accrued expenses	57,067	40,188
Income taxes payable	15,071	1,346
Deferred tax liabilities	–	1,192
Advances received	–	13,500
Deposits received	4,663	3,435
Other	–	4,565
Total current liabilities	200,207	190,213
Non-current liabilities		
Asset retirement obligations	11,555	11,649
Deferred tax liabilities	25,985	29,424
Total non-current liabilities	37,540	41,073
<b>Total liabilities</b>	<b>237,748</b>	<b>231,286</b>
<b>Net assets</b>		
Shareholders' equity		
Capital stock	9,806,225	2,237,588
Capital surplus		
Legal capital surplus	5,090,225	2,237,588
Total capital surpluses	5,090,225	2,237,588
Retained earnings		
Other retained earnings		
Retained earnings brought forward	(10,421,274)	(728,117)
Total retained earnings	(10,421,274)	(728,117)
Total shareholders' equity	4,475,176	3,747,058
Valuation and translation adjustments		
Valuation difference on available-for-sale securities	28,170	26,183
Total valuation and translation adjustments	28,170	26,183
Subscription rights to shares	11,017	14,785
<b>Total net assets</b>	<b>4,514,364</b>	<b>3,788,027</b>
<b>Total liabilities and net assets</b>	<b>4,752,112</b>	<b>4,019,314</b>

**(2) Non-consolidated statement of income**

(Thousands of yen)

	Fiscal year ended December 31, 2015	Fiscal year ended December 31, 2016
Business revenue	145,500	705,235
Business expenses		
Cost of business revenue	–	117,630
Research and development expenses	*1 1,302,452	*1 796,229
Other selling, general and administrative expenses	*2 707,644	*2 551,252
Total business expenses	2,010,097	1,465,111
Operating loss	(1,864,597)	(759,876)
Non-operating income		
Interest income	4,142	12,654
Interest on securities	77,906	52,329
Dividend income	186	–
Foreign exchange gains	14,323	–
Gain on sales of securities	1,165	–
Subsidy income	–	19,843
Gain on valuation of compound financial instruments	–	8,070
Other	1,074	1,601
Total non-operating income	98,798	94,499
Non-operating expenses		
Foreign exchange losses	–	55,328
Loss on valuation of compound financial instruments	21,487	–
Loss on redemption of securities	1,530	–
Share issuance cost	6,400	–
Total non-operating expenses	29,417	55,328
Ordinary loss	(1,795,216)	(720,705)
Extraordinary income		
Gain on sales of investment securities	65,655	–
Total extraordinary income	65,655	–
Extraordinary losses		
Loss on redemption of investment securities	6,000	2,000
Special retirement expenses	69,483	–
Office transfer expenses	43,416	–
Total extraordinary losses	118,900	2,000
Loss before income taxes	(1,848,460)	(722,705)
Income taxes - current	5,893	1,346
Income taxes - deferred	–	4,065
Total income taxes	5,893	5,411
Loss	(1,854,353)	(728,117)

**(3) Non-consolidated statement of changes in equity**

Fiscal year ended December 31, 2015

(Thousands of yen)

	Shareholders' equity			
	Capital stock	Capital surplus	Retained earnings	Total shareholders' equity
		Legal capital surplus	Other retained earnings	
			Retained earnings brought forward	
Balance at beginning of current period	8,952,367	4,236,367	(8,566,920)	4,621,814
Changes of items during period				
Issuance of new shares	853,858	853,858		1,707,716
Deficit disposition				
Loss			(1,854,353)	(1,854,353)
Net changes of items other than shareholders' equity				
Total changes of items during period	853,858	853,858	(1,854,353)	(146,637)
Balance at end of current period	9,806,225	5,090,225	(10,421,274)	4,475,176

	Valuation and translation adjustments		Subscription rights to shares	Total net assets
	Valuation difference on available-for-sale securities	Total valuation and translation adjustments		
Balance at beginning of current period	198,904	198,904	10,769	4,831,488
Changes of items during period				
Issuance of new shares				1,707,716
Deficit disposition				
Loss				(1,854,353)
Net changes of items other than shareholders' equity	(170,733)	(170,733)	247	(170,485)
Total changes of items during period	(170,733)	(170,733)	247	(317,123)
Balance at end of current period	28,170	28,170	11,017	4,514,364

Fiscal year ended December 31, 2016

(Thousands of yen)

	Shareholders' equity			
	Capital stock	Capital surplus	Retained earnings	Total shareholders' equity
		Legal capital surplus	Other retained earnings	
Retained earnings brought forward				
Balance at beginning of current period	9,806,225	5,090,225	(10,421,274)	4,475,176
Changes of items during period				
Deficit disposition	(7,568,637)	(2,852,637)	10,421,274	-
Loss			(728,117)	(728,117)
Net changes of items other than shareholders' equity				
Total changes of items during period	(7,568,637)	(2,852,637)	9,693,157	(728,117)
Balance at end of current period	2,237,588	2,237,588	(728,117)	3,747,058

	Valuation and translation adjustments		Subscription rights to shares	Total net assets
	Valuation difference on available-for-sale securities	Total valuation and translation adjustments		
Balance at beginning of current period	28,170	28,170	11,017	4,514,364
Changes of items during period				
Deficit disposition				
Loss				(728,117)
Net changes of items other than shareholders' equity	(1,986)	(1,986)	3,768	1,781
Total changes of items during period	(1,986)	(1,986)	3,768	(726,336)
Balance at end of current period	26,183	26,183	14,785	3,788,027

**(4) Non-consolidated statement of cash flows**

(Thousands of yen)

	Fiscal year ended December 31, 2015	Fiscal year ended December 31, 2016
<b>Cash flows from operating activities</b>		
Loss before income taxes	(1,848,460)	(722,705)
Depreciation	53,353	79,877
Interest income	(4,142)	(12,654)
Dividend income	(186)	-
Interest income on securities	(77,906)	(52,329)
Foreign exchange losses (gains)	(14,432)	11,664
Loss (gain) on sales of securities	(1,165)	-
Share issuance cost	6,400	-
Loss (gain) on valuation of compound financial instruments	21,487	(8,070)
Loss (gain) on redemption of securities	1,530	-
Subsidy income	-	(19,843)
Loss (gain) on sales of investment securities	(65,655)	-
Loss (gain) on redemption of investment securities	6,000	2,000
Extra retirement payment	69,483	-
Office transfer expenses	43,416	-
Decrease (increase) in notes and accounts receivable - trade	(52,866)	14,601
Decrease (increase) in inventories	1,579	22
Decrease (increase) in advance payments	(121,245)	(25,868)
Decrease (increase) in prepaid expenses	(10,089)	9,950
Decrease (increase) in consumption taxes refund receivable	6,317	-
Increase (decrease) in accounts payable - other	(45,744)	9,329
Other, net	(62,814)	(13,478)
Subtotal	(2,095,143)	(727,505)
Interest and dividend income received	71,238	61,054
Income taxes paid	(5,769)	(1,892)
Extra retirement payments	(37,042)	(32,440)
Proceeds from subsidy income	-	19,843
Payments for removal expenses	(43,416)	-
Other, net	(6,400)	-
Net cash provided by (used in) operating activities	(2,116,533)	(680,939)
<b>Cash flows from investing activities</b>		
Payments into time deposits	-	(323,570)
Purchase of securities	(620,950)	(200,000)
Proceeds from sales of securities	51,089	-
Proceeds from redemption of securities	1,557,256	300,000
Purchase of property, plant and equipment	(195,545)	(35,849)
Purchase of intangible assets	(3,981)	(1,335)
Purchase of investment securities	(853,936)	(426,905)
Proceeds from sales of investment securities	559,942	61,160
Proceeds from redemption of investment securities	150,000	185,000
Proceeds from collection of guarantee deposits	26,243	81
Other, net	(4,201)	-
Net cash provided by (used in) investing activities	665,915	(441,418)

(Thousands of yen)

	Fiscal year ended December 31, 2015	Fiscal year ended December 31, 2016
Cash flows from financing activities		
Proceeds from issuance of subscription rights to shares	15,450	–
Proceeds from issuance of shares resulting from exercise of subscription rights to shares	1,686,260	–
Net cash provided by (used in) financing activities	1,701,710	–
Effect of exchange rate change on cash and cash equivalents	625	(33,561)
Net increase (decrease) in cash and cash equivalents	251,718	(1,155,920)
Cash and cash equivalents at beginning of period	1,991,558	2,243,276
Cash and cash equivalents at end of period	2,243,276	1,087,356



**(5) Notes to non-consolidated financial statements****Non-consolidated statement of income**

\*1 The approximate ratio of expense items recorded under research and development expenses is 64.8% for the fiscal year ended December 31, 2015 and 54.3% for the fiscal year ended December 31, 2016.

Among research and development expenses, significant expense items and their amounts are as follows:

(Thousands of yen)

	Fiscal year ended December 31, 2015	Fiscal year ended December 31, 2016
Salaries and allowances	409,195	281,819
Academic-industrial research collaboration expenses	151,552	163,399
Research and development consignment expenses	192,391	44,665
Clinical research expenses	146,146	19,234
Business consignment expenses	27,057	13,074
Depreciation	41,175	69,490

\*2 The approximate ratio of expense items recorded under other selling, general and administrative expenses is 35.2% for the fiscal year ended December 31, 2015 and 37.6% for the fiscal year ended December 31, 2016.

Among other selling, general and administrative expenses, significant expense items and their amounts are as follows:

(Thousands of yen)

	Fiscal year ended December 31, 2015	Fiscal year ended December 31, 2016
Salaries and allowances	215,602	146,049
Business consignment expenses	116,906	130,175
Patent maintenance expenses	139,990	99,660
Depreciation	8,861	8,088

**Non-consolidated statement of changes in equity**

Fiscal year ended December 31, 2015

## 1. Class and total number of issued shares and treasury shares

	Fiscal year ended December 31, 2015 Number of shares at start of period (Shares)	Fiscal year ended December 31, 2015 Increase in number of shares (Shares)	Fiscal year ended December 31, 2015 Decrease in number of shares (Shares)	Fiscal year ended December 31, 2015 Number of shares at end of period (Shares)
Issued shares				
Common shares	14,857,200	3,910,000	–	18,767,200
Total	14,857,200	3,910,000	–	18,767,200
Treasury shares				
Common shares	–	–	–	–
Total	–	–	–	–

Note: The increase of 3,910,000 in the total number of issued shares is an increase resulting from exercise of stock acquisition rights.

## 2. Dividends

No items to report.

### 3. Stock acquisition rights

Category	Breakdown of stock acquisition rights	Class of shares underlying stock acquisition rights	Number of shares underlying stock acquisition rights (shares)				Balance at end of fiscal year ended December 31, 2015 (thousand yen)
			Start of fiscal year ended December 31, 2015	Increase in fiscal year ended December 31, 2015	Decrease in fiscal year ended December 31, 2015	End of fiscal year ended December 31, 2015	
Filing company	3rd series share options (Stock acquisition rights as stock options)	-	-	-	-	-	-
	5th series share options (Stock acquisition rights as stock options)	-	-	-	-	-	-
	7th series share options (Stock acquisition rights as stock options)	-	-	-	-	-	-
	9th series share options (Stock acquisition rights as stock options)	-	-	-	-	-	11,017
	10th series share options (Stock acquisition rights as stock options on the Company's own stock)	-	-	-	-	-	-
	11th series share options (Stock acquisition rights as stock options on the Company's own stock)	-	-	-	-	-	-
Total		-	-	-	-	-	11,017

- Notes: 1. In cases where stock acquisition rights are granted as stock options or stock options on the Company's own stock, the class and number of the shares underlying the stock acquisition rights are not provided.
2. On the grant dates of the 3rd series share options, 5th series share options and 7th series share options, as the Company's shares were not listed, fair unit values on the grant dates were calculated according to a method in which the intrinsic value per unit was estimated. The intrinsic value at the end of the fiscal year ended December 31, 2015 (intrinsic value on grant date) was zero for each of the series and there was no balance as of the end of the fiscal year ended December 31, 2015.
3. There were no 10th series share options issued on July 22, 2014 remaining unexercised at the end of the fiscal year ended December 31, 2015 since all of such share options remaining unexercised were exercised on July 7, 2015.
4. There were no 11th series share options issued on September 14, 2015 remaining unexercised at the end of the fiscal year ended December 31, 2015 since all of such share options remaining unexercised were exercised on November 27, 2015.

Fiscal year ended December 31, 2016

1. Class and total number of issued shares and treasury shares

	Fiscal year ended December 31, 2016 Number of shares at start of period (Shares)	Fiscal year ended December 31, 2016 Increase in number of shares (Shares)	Fiscal year ended December 31, 2016 Decrease in number of shares (Shares)	Fiscal year ended December 31, 2016 Number of shares at end of period (Shares)
Issued shares				
Common shares	18,767,200	–	–	18,767,200
Total	18,767,200	–	–	18,767,200
Treasury shares				
Common shares	–	–	–	–
Total	–	–	–	–

2. Dividends

No items to report.

3. Stock acquisition rights

Category	Breakdown of stock acquisition rights	Class of shares underlying stock acquisition rights	Number of shares underlying stock acquisition rights (shares)				Balance at end of Fiscal year ended December 31, 2016 (thousand yen)
			Start of fiscal year ended December 31, 2016	Increase in fiscal year ended December 31, 2016	Decrease in fiscal year ended December 31, 2016	End of fiscal year ended December 31, 2016	
Filing company	3rd series share options (Stock acquisition rights as stock options)	–	–	–	–	–	–
	5th series share options (Stock acquisition rights as stock options)	–	–	–	–	–	–
	7th series share options (Stock acquisition rights as stock options)	–	–	–	–	–	–
	9th series share options (Stock acquisition rights as stock options)	–	–	–	–	–	11,340
	12th series share options (Stock acquisition rights as stock options)	–	–	–	–	–	3,445
Total		–	–	–	–	–	14,785

Notes: 1. In cases where stock acquisition rights are granted as stock options or stock options on the Company's own stock, the class and number of the shares underlying the stock acquisition rights are not provided.

2. On the grant dates of the 3rd series share options, 5th series share options and 7th series share options, as the Company's shares were not listed, fair unit values on the grant dates were calculated according to a method in which the intrinsic value per unit was estimated. The intrinsic value at the end of the fiscal year ended December 31, 2016 (intrinsic value on grant date) was zero for each of the series and there was no balance as of the end of the fiscal year ended December 31, 2016.

### Significant subsequent event

Conversion of TMRC Co., Ltd. into a subsidiary through a simplified share exchange

The Company, at its Board of Directors meeting held on December 26, 2016, resolved to conduct a share exchange in which the Company would be the wholly owning parent company resulting from the share exchange and TMRC Co., Ltd. (“TMRC”) the wholly owned subsidiary company resulting from the share exchange (the “Share Exchange”), and the share exchange agreement was entered into by and between both parties on the same day. The Share Exchange took place on February 3, 2017, as planned.

#### (1) Outline of business combination

##### 1) Name and business activities of acquiree

Name of acquiree	TMRC Co., Ltd.
Business activities	Drug discovery business specialized in the field of cancer

##### 2) Primary reasons for business combination

Since its founding in 2008, the Company has been pursuing operations chiefly in two priority areas, namely, pain management and gastrointestinal disease treatment, primarily through small molecule drug discovery endeavors. Starting from 2014, prompted by the transfer in the year of its research function to Nagoya University, the Company has been obtaining opportunities to access a wide range of academia research themes and patient needs, thus examining diverse disease areas.

In this process, the Company has been aiming to further enhance its operations by actively pushing forward with its joint research programs on treatment drugs based on a new mechanism of action that was proposed by academia, and with a focus on the fields of cancer and rare disease, in which patients’ treatment needs have yet to be met sufficiently.

In light of the above-mentioned situation, the Company searched for a corporation through which to fulfill its needs. As a result, upon consideration, the Company has decided to convert TMRC, a firm compatible with the Company in business description and target disease scope, into a wholly owned subsidiary company by using the simplified share exchange method, a step taken with the objective of broadening the Company’s business domains and aggressively expanding into the fields of cancer and rare disease, in particular.

##### 3) Date of business combination

January 1, 2017 (deemed acquisition date)

##### 4) Legal form for the business combination

Share exchange through which the Company became the wholly owning parent company resulting from the share exchange, and TMRC became the wholly owned subsidiary company resulting from the share exchange

##### 5) Company name after combination

There is no change in the company name.

##### 6) Ratio of voting rights acquired

100%

##### 7) Main grounds for determining the acquirer

The Company acquired 100% of the voting rights by share exchange, thereby making that company a wholly owned subsidiary company.

#### (2) Acquisition cost of the acquiree and breakdown thereof by type of consideration

Not confirmed at this stage.

#### (3) Share exchange ratio by share type, calculation method thereof, and number of shares delivered

##### 1) Share exchange ratio

	The Company (wholly owning parent company resulting from the share exchange)	TMRC (wholly owned subsidiary company resulting from the share exchange)
Share exchange ratio for common shares	1	90

Note: In the Share Exchange, the Company allocated and delivered 90 newly issued common shares of the Company in exchange for one common share of TMRC.

##### 2) Method to calculate share exchange ratio

In order to ensure the fairness and appropriateness of the calculation of the share exchange ratio for the Share Exchange, the calculation was entrusted to PLUTUS CONSULTING Co., Ltd. (“PLUTUS”), who is a third-party valuation institution that is independent from the Company and TMRC.

As the Company is listed on the JASDAQ Growth Market of the Tokyo Stock Exchange and it has a market share price, PLUTUS used the average market share price method to calculate the Company’s share value, and as TMRC is an unlisted company, PLUTUS assessed the share value of TMRC by deciding future earnings power through business activities, using the discounted cash flow method to calculate this.

The result of calculating the share exchange ratio for the Share Exchange when the Company’s share value per share is one, based on the above calculation was as follows.

Result of share exchange ratio calculation
64.72-93.88

Giving comprehensive consideration to the above calculation result, and factors such as the financial position of both companies, the asset position, and future outlook, the Company decided on the share exchange ratio through discussions with TMRC, and this was determined through resolutions by the Company's Board of Directors and TMRC's directors, respectively.

There is nothing to report with respect to expected delistings and reasons thereof. In addition, as PLUTUS CONSULTING Co., Ltd. is a third-party valuation institution that is independent from both the Company and TMRC, and as it is not considered a related party, there are no relationships of significant interest that need to be disclosed regarding the Share Exchange.

- 3) Number of shares delivered  
479,250 shares
- (4) Details and amounts of main acquisition-related costs  
Consideration/fees etc. paid for advisory fees, etc.      2,450 thousand yen
- (5) Amount of goodwill recognized, reason for recognition of goodwill, and method and period for amortization of goodwill  
Not confirmed at this stage.
- (6) Amount and breakdown of assets acquired and liabilities assumed as of the date of the business combination  
Not confirmed at this stage.