# MHI REPORT 2016

# FINANCIAL SECTION 2016

For the Year Ended March 31, 2016

MITSUBISHI HEAVY INDUSTRIES, LTD.

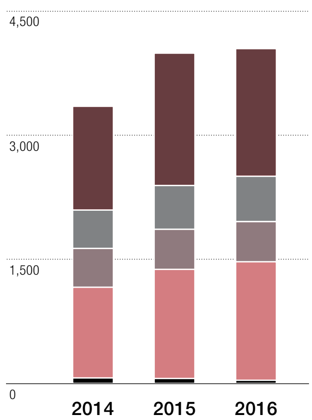
Our Technologies, Your Tomorrow

# SEGMENT INFORMATION

Mitsubishi Heavy Industries, Ltd. and Consolidated Subsidiaries
Fiscal years ended March 31, 2016 and 2015

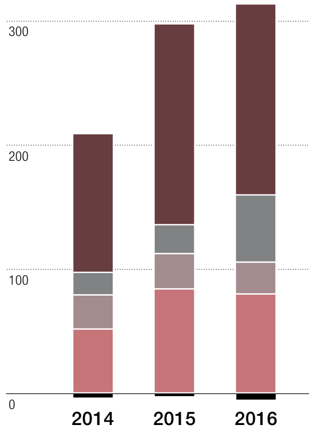
## NET SALES

| Industry Segment | In millions of yen 2016 | 2015 | 2014 | In thousands of U.S. dollars 2016 |
|---|---|---|---|---|
| Energy & Environment | **¥1,542,779** | ¥1,599,527 | ¥1,253,988 | **$13,691,684** |
| Commercial Aviation & Transportation Systems | **548,510** | 529,598 | 463,671 | **4,867,855** |
| Integrated Defense & Space Systems | **485,070** | 483,964 | 469,463 | **4,304,845** |
| Machinery, Equipment & Infrastructure | **1,432,358** | 1,347,463 | 1,096,333 | **12,711,732** |
| Others | **177,335** | 154,935 | 185,056 | **1,573,793** |
| Subtotal | **4,186,054** | 4,115,489 | 3,468,512 | **37,149,929** |
| Eliminations or Corporate | **(139,244)** | (123,378) | (118,913) | **(1,235,747)** |
| Total | **¥4,046,810** | ¥3,992,110 | ¥3,349,598 | **$35,914,181** |



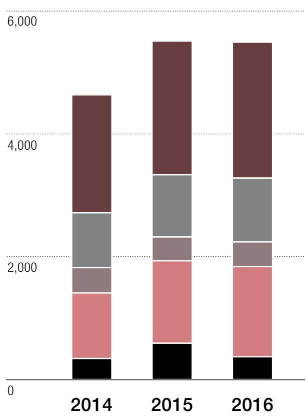

## OPERATING INCOME

| Industry Segment | In millions of yen 2016 | 2015 | 2014 | In thousands of U.S. dollars 2016 |
|---|---|---|---|---|
| Energy & Environment | **¥154,667** | ¥162,681 | ¥112,323 | **$1,372,621** |
| Commercial Aviation & Transportation Systems | **54,511** | 23,452 | 18,319 | **483,768** |
| Integrated Defense & Space Systems | **25,789** | 28,565 | 27,631 | **228,869** |
| Machinery, Equipment & Infrastructure | **80,077** | 87,746 | 51,690 | **710,658** |
| Others | **12,617** | 10,322 | 14,651 | **111,971** |
| Subtotal | **327,664** | 312,769 | 224,616 | **2,907,916** |
| Eliminations or Corporate | **(18,157)** | (16,628) | (18,498) | **(161,137)** |
| Total | **¥309,506** | ¥296,140 | ¥206,118 | **$2,746,769** |




## TOTAL ASSETS

| Industry Segment | In millions of yen 2016 | 2015 | 2014 | In thousands of U.S. dollars 2016 |
|---|---|---|---|---|
| Energy & Environment | **¥2,211,326** | ¥2,176,565 | ¥1,921,411 | **$19,624,831** |
| Commercial Aviation & Transportation Systems | **1,040,626** | 1,013,226 | 892,503 | **9,235,232** |
| Integrated Defense & Space Systems | **401,461** | 388,110 | 412,884 | **3,562,841** |
| Machinery, Equipment & Infrastructure | **1,468,767** | 1,361,145 | 1,066,500 | **13,034,850** |
| Others | **633,659** | 576,205 | 467,344 | **5,623,526** |
| Subtotal | **5,755,841** | 5,515,253 | 4,760,645 | **51,081,301** |
| Eliminations or Corporate | **(264,042)** | 5,103 | 125,389 | **(2,343,290)** |
| Total | **¥5,491,799** | ¥5,520,357 | ¥4,886,035 | **$48,738,010** |



| Industry Segment | CAPITAL EXPENDITURES In millions of yen 2016 | 2015 | In thousands of U.S. dollars 2016 | DEPRECIATION AND AMORTIZATION* In millions of yen 2016 | 2015 | In thousands of U.S. dollars 2016 |
|---|---|---|---|---|---|---|
| Energy & Environment | ¥ 40,264 | ¥ 44,843 | $ 357,330 | ¥ 57,998 | ¥ 64,613 | $ 514,714 |
| Commercial Aviation & Transportation Systems | 45,509 | 27,713 | 403,878 | 25,418 | 23,579 | 225,576 |
| Integrated Defense & Space Systems | 35,921 | 24,088 | 318,787 | 17,828 | 16,758 | 158,217 |
| Machinery, Equipment & Infrastructure | 112,728 | 69,706 | 1,000,425 | 43,132 | 37,340 | 382,783 |
| Others | 3,517 | 3,936 | 31,212 | 3,993 | 4,780 | 35,436 |
| Subtotal | 237,942 | 170,288 | 2,111,661 | 148,371 | 147,073 | 1,316,746 |
| Corporate | 5,309 | 5,755 | 47,115 | 10,335 | 9,937 | 91,719 |
| Total | ¥243,251 | ¥176,043 | $2,158,777 | ¥158,706 | ¥157,010 | $1,408,466 |

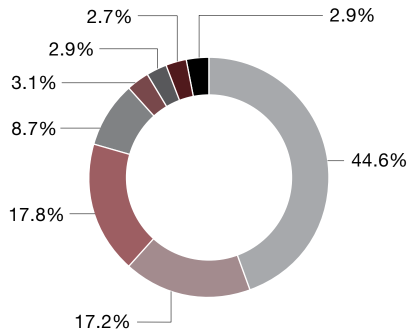
* Amortization of goodwill is not included.

| Industry Segment | AMORTIZATION OF GOODWILL In millions of yen 2016 | 2015 | In thousands of U.S. dollars 2016 | UNAMORTIZED BALANCE OF GOODWILL In millions of yen 2016 | 2015 | In thousands of U.S. dollars 2016 |
|---|---|---|---|---|---|---|
| Energy & Environment | ¥ 8,372 | ¥ 7,985 | $ 74,298 | ¥ 63,511 | ¥68,186 | $ 563,640 |
| Commercial Aviation & Transportation Systems | — | — | — | — | — | — |
| Integrated Defense & Space Systems | — | — | — | — | — | — |
| Machinery, Equipment & Infrastructure | 3,288 | 3,951 | 29,179 | 85,287 | 27,401 | 756,895 |
| Others | 0 | 0 | 0 | 2 | 0 | 17 |
| Subtotal | 11,661 | 11,937 | 103,487 | 148,800 | 95,588 | 1,320,553 |
| Corporate | (245) | — | (2,174) | (3,195) | — | (28,354) |
| Total | ¥11,416 | ¥11,937 | $101,313 | ¥145,605 | ¥95,588 | $1,292,199 |

| Industry Segment | INVESTMENTS IN EQUITY-METHOD AFFILIATES In millions of yen 2016 | 2015 | In thousands of U.S. dollars 2016 |
|---|---|---|---|
| Energy & Environment | ¥ 61,962 | ¥ 65,021 | $ 549,893 |
| Commercial Aviation & Transportation Systems | — | — | — |
| Integrated Defense & Space Systems | — | — | — |
| Machinery, Equipment & Infrastructure | 14,013 | 10,572 | 124,361 |
| Others | 1,736 | 1,805 | 15,406 |
| Subtotal | 77,713 | 77,398 | 689,678 |
| Corporate | 125,504 | 119,668 | 1,113,809 |
| Total | ¥203,218 | ¥197,067 | $1,803,496 |

| Breakdown of Sales by Customer Location | NET SALES In millions of yen 2016 | 2015 | In thousands of U.S. dollars 2016 |
|---|---|---|---|
| Japan | ¥1,804,925 | ¥1,862,140 | $16,018,148 |
| U.S.A. | 697,369 | 607,288 | 6,188,933 |
| Asia | 721,946 | 682,587 | 6,407,046 |
| Europe | 352,706 | 354,020 | 3,130,156 |
| Central and South America | 126,956 | 119,021 | 1,126,695 |
| Middle East | 115,757 | 127,167 | 1,027,307 |
| Africa | 110,635 | 129,814 | 981,851 |
| Others | 116,512 | 110,070 | 1,034,007 |
| Total | ¥4,046,810 | ¥3,992,110 | $35,914,181 |

**Composition of Overseas Net Sales by Geographic Distribution**




Note: U.S. dollar amounts in this annual report are translated from yen, for convenience only, at the rate of ¥112.68 = US$1, the exchange rate prevailing at March 31, 2016.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## ANALYSIS OF OPERATING RESULTS

In fiscal 2015, ended March 31, 2016, the MHI Group recorded consolidated net sales of ¥4,046.8 billion, up ¥54.6 billion, or 1.4%, from the preceding fiscal year, owing to higher sales in the Machinery, Equipment & Infrastructure segment, although sales decreased in the Energy & Environment segment. Operating income grew ¥13.3 billion, or 4.5%, to ¥309.5 billion, as a substantial increase from the Commercial Aviation & Transportation Systems segment made up for declines in the Energy & Environment and Machinery, Equipment & Infrastructure segments. Ordinary income fell ¥2.2 billion, or 0.8%, year on year, to ¥272.5 billion. This decrease stemmed from the recording of a ¥21.9 billion foreign exchange loss as a non-operating expense, which offset an improvement in income from equity method investments.

Extraordinary gain came to ¥14.7 billion, including such factors as a gain on negative goodwill and gain on sales of fixed assets. Extraordinary loss, of ¥154.5 billion included a loss on passenger vessel construction business reserve and business structure improvement expenses. As a result, income before income taxes fell ¥100.0 billion, or 43.0%, year on year, to ¥132.6 billion, and profit attributable to owners of parent declined ¥46.5 billion, or 42.2%, to ¥63.8 billion.

## ANALYSIS OF FINANCIAL POSITION

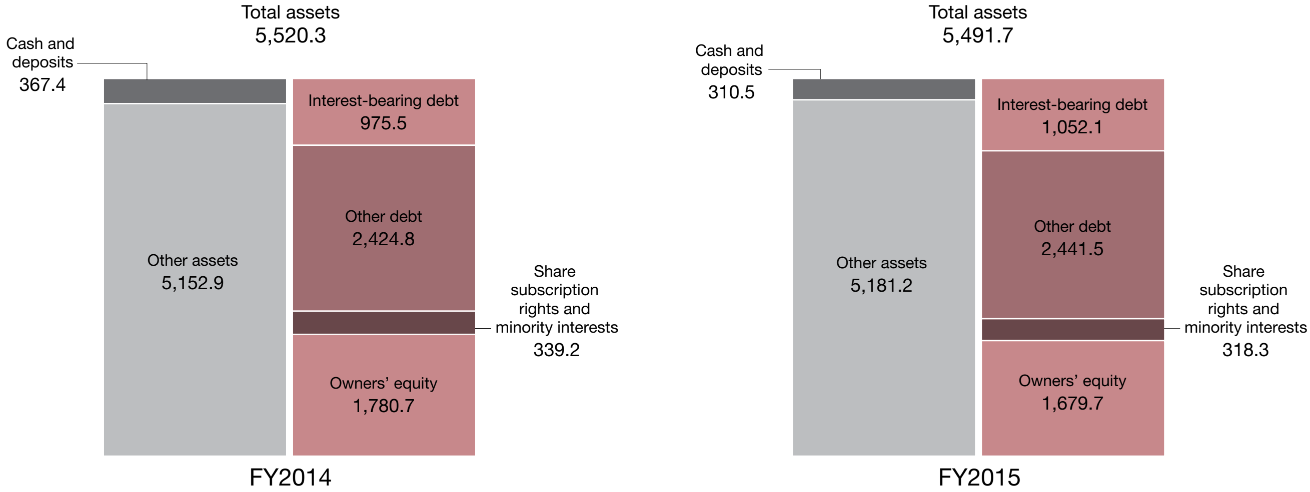
Total assets as of March 31, 2016, amounted to ¥5,491.7 billion, down ¥28.5 billion from one year earlier, reflecting decreases in cash and deposits, trade receivables, and investment securities.

Total liabilities rose ¥93.3 billion, to ¥3,493.7 billion, owing to increases in short-term borrowings and advance payments received on contracts.

Total net assets fell ¥121.9 billion, to ¥1,998.0 billion. Although retained earnings grew as the result of posting net income, accumulated other comprehensive income declined as the result of translation adjustments and unrealized holding gain (loss) on investment securities.

**Consolidated Balance Sheets**

In billions of yen




| | FY2014 | FY2015 |
|---|---|---|
| Shareholders' equity ratio | 32.3% | 30.6% |
| D/E ratio | 0.46 times | 0.53 times |
| ROE | 6.5% | 3.7% |

# SOURCE OF FUNDS AND LIQUIDITY

## Cash flow analysis

Operating activities provided net cash of ¥270.0 billion, an increase of ¥57.1 billion, from the preceding fiscal year. Although profit before income taxes declined, the Group strove to increase production efficiencies and promoted the collection of funds, as the scale of business increased. These efforts led to a decrease in receivables, lower inventories, and other working capital requirements. Income taxes paid also decreased.

Investing activities used net cash of ¥262.4 billion, which was ¥88.3 billion more than in the previous fiscal year. This change was primarily due to the purchase of investments in subsidiaries that result in change in scope of consolidation.

Financing activities used net cash of ¥23.1 billion, a ¥22.7 billion decline from the previous fiscal year. Despite decreases in sources of cash, including short-term borrowings, commercial papers, proceeds from long-term borrowings, and proceeds from issuance of bonds, uses of cash—including the repayment of long-term borrowings and payment for redemption of bonds—also declined.

## Primary funding requirements

The MHI Group primarily requires funds in operating activities for working capital for manufacturing activities (materials, outsourcing, and personnel costs), order preparation costs and other sales expenses related to winning new orders, and funds for R&D activities that enhance the competitiveness of its products and strengthen manufacturing capabilities. In investing activities, funds are required for capital investments to grow businesses and raise productivity as well as for the purchase of investment securities related to the execution of business strategies.

In growth areas, the MHI Group is planning to purchase investment securities and execute necessary capital investments and R&D investment. As a whole, the Group plans to streamline its assets and selectively concentrate on core investment schemes, while anticipating funding requirements in future growth fields and closely monitoring the latest market environments and order trends.

## Breakdown of interest-bearing debt and its applications

The breakdown of interest-bearing debt as of March 31, 2016, was as follows:

In billions of yen

| | Total | Due within one year | Due after one year |
|---|---|---|---|
| Short-term borrowings | 293.1 | 293.1 | – |
| Commercial papers | 45.0 | 45.0 | – |
| Long-term borrowings | 449.0 | 61.7 | 387.3 |
| Bonds | 265.0 | 20.0 | 245.0 |
| **Total** | 1,052.1 | 419.8 | 632.3 |

The MHI Group is involved in various projects with comparatively long construction periods. It also owns numerous manufacturing facilities that employ large-scale machinery facilities. Consequently, the MHI Group must secure a stable level of working capital and funds for capital investments. In recent years, these types of necessary funds for capital investment have been increasing due to the expansion of the MHI Group's business scale. Meanwhile, the Group has continued to work to streamline its assets and has repaid borrowings that have come due. As a result, the total interest-bearing debt of the MHI Group at the end of fiscal 2015 was ¥1,052.1 billion, consisting of ¥419.8 billion due within one year and ¥632.3 billion due after one year.

The interest-bearing debt mentioned above is utilized as working capital and for capital investments required for business activities, and the MHI Group plans to use these funds mainly in key growth fields that are expected to require funds, including Energy & Environment and Commercial Aviation & Transportation Systems.

## Financial policy

The MHI Group funds its working capital and capital investments from its operating cash flows. Any additional requirements can be met with interest-bearing debt. In appropriately determining the amounts and methods of procuring long-term funds through long-term borrowings, bonds, and other means, the MHI Group takes into account the funding requirements of its business plans, interest rate trends and various other factors, and the repayment schedule for its existing debt.

Additionally, in its efforts to reduce interest-bearing debt, the MHI Group strives to efficiently utilize surplus funds within the Group using a cash management system. At the same time, the MHI Group is working to improve asset efficiency by reducing trade receivables and inventories and by raising the utilization rate of its property, plant and equipment.

The MHI Group considers the repurchase of treasury stock by taking into overall account a number of factors, including the state of progress on business plans, the Company's performance outlook, stock price trends, financial condition, and improvements in the financial market environment.

## DIVIDEND POLICY

In the 2015 Medium-Term Business Plan, the MHI Group plans to achieve an ROE of above 10% by fiscal 2017, while increasing its owners' equity to ¥2 trillion. In the process of doing so, the Group has set a basic policy of providing returns to shareholders at a dividend payout ratio of around 30%, for the time being, while giving consideration to the balance between investments in future businesses and the strengthening of owners' equity.

As decided in MHI's Articles of Incorporation, the Group pays dividends from retained earnings to shareholders twice a year. These payments consist of an interim dividend with a record date of September 30 and a year-end dividend with a record date of March 31. Decisions on interim dividend payments are made by the Board of Directors, and decisions on year-end dividend payments are made at the General Meeting of Shareholders.

In accordance with the above policy, the total dividend payment for fiscal 2015 was ¥12 per share, comprising the interim dividend of ¥6 per share, paid in December 2015, and the year-end dividend of ¥6 per share.

Internal reserves will be utilized to further strengthen the Group's corporate structure and enhance the Group's business development going forward.

# OPERATIONAL RISKS

The MHI Group, comprising MHI and its consolidated subsidiaries, is exposed to various risk factors, including the following: economic risks, such as currency exchange fluctuation and credit risks; political risks, such as trade restrictions and country risks; legal risks, such as product liability; disaster risks, such as natural disaster and accidents; market risks, such as stock price fluctuation and investment risks; and others. However, of the risks related to the state of our businesses and accounting, the items below are those that have the potential to significantly influence investor judgment. Items relating to the future are based on the judgment of the Group as of the end of fiscal 2015, the year ended March 31, 2016.

## 01 RISKS RELATED TO FINANCIAL POSITION AND OPERATING RESULTS

### i. Economic Conditions

The Group's operating results may be influenced by changes in economic conditions, both in Japan and in other countries and regions around the world. Such changes include movements in Japanese private sector investments and fluctuations in economic conditions overseas in the United States and Europe, as well as in emerging nations, such as China and India. However, as the global economy has become more complex, influences are no longer limited to the economic conditions of the countries and regions where the Group is engaged in business operations.

### ii. Export and Overseas Operations

The Group is working toward the expansion of export and overseas businesses in countries and regions around the world. Therefore, several factors, including unforeseen difficulties in the local procurement of parts or with local construction, claims from contractual partners due to delivery delays or inadequate performance, and contractual partner defaults, have the potential to influence the Group's operating results. Furthermore, although the Group is actively engaged in the creation and expansion of such new business models as comprehensive infrastructure development projects in emerging nations, we cannot guarantee that we will be successful in securing projects when faced with intense competition, such as when other private corporations are supported by governments in securing contracts for large-scale infrastructure development projects.

### iii. Currency Exchange Rate Fluctuations

Most of the Group's export and overseas business transactions are conducted in foreign currencies, such as the U.S. dollar and the euro. Therefore, currency exchange rate fluctuations have the potential to influence our competitiveness. Moreover, changes in the cost competitiveness of overseas competitors due to currency exchange rate fluctuations have the potential to influence our competitiveness in domestic business. In cases where the Group and its domestic competitors are affected differently by currency exchange rate fluctuations, our domestic and overseas competitiveness with the corporations concerned may be affected. When making transactions in foreign currencies, we endeavor to hedge risk by increasing liabilities denominated in foreign currencies by expanding overseas procurement of materials and through forward exchange contracts. Nevertheless, currency exchange rate fluctuations have the potential to influence our operating results.

### iv. Fund-raising

The Group takes trends in interest rates, including future forecasts, into consideration when implementing fund-raising activities, and strives to secure low interest rates and stable funding. However, significant fluctuations in interest rates and changes in the overall state of financial markets have the potential to influence our future operating results.

### v. Retirement Benefit Expenses and Liabilities

Group employee retirement benefit expenses and liabilities are calculated based on actuarial assumptions, the key assumptions for which are the discount rate for retirement benefit liabilities and the expected long-term rate of return on pension assets. These assumptions are judged to be appropriate estimations. Nevertheless, where actual outcomes differ from these assumptions, or should these assumptions change, the Group's future financial position and operating results may be affected. Moreover, changes in the investment yield of pension assets, or in the yield on government bonds, which serves as a basis for deciding the discount rate, may also influence the Group's financial position and operating results.

## 02 RISKS RELATED TO RELIANCE ON PARTICULAR CLIENTS

### i. M&A and Alliances

The Group is engaged in the strengthening and expansion of many of its businesses through M&A and alliances with other companies. However, in the event that we are unable to realize these M&A and alliances due to changes in the market environment, or because of a decline in business competitiveness, revision of management strategies by these companies, or other unforeseen circumstances, the Group's business may be affected.

### ii. Procurement of Materials

Group business activities necessitate the supply of raw materials, parts, machinery, and services from third parties in a timely, appropriate manner, and supplied items must be of sufficient quality and quantity. Due to the specialist nature of certain items, suppliers are limited, and changing suppliers can be difficult. If there is a problem with the quality of an item, a shortage in supply, a delivery delay, a halt in production due to a disaster, or other problem, the Group's businesses may be affected. Moreover, increases in the price of an item due to changes in supply and demand may affect the Group's operating results.

## 03 RISKS RELATED TO SPECIFIC PRODUCTS AND TECHNOLOGIES

### i. Product Competitiveness

The Group strives to achieve high customer evaluations of performance, reliability, and price of its products. We work hard to propose new functions that anticipate market trends, and we are working to strengthen the competitiveness of our products, particularly through R&D and capital investment. However, where the efforts of domestic and overseas competitors to strengthen product competitiveness are more effective than those of the Group, our businesses may be affected.

### ii. Product Quality

The Group continually makes efforts to improve the quality and reliability of its products. However, product performance or delivery issues, or any safety issues that arise in the use of our products, may lead to claims from contractual partners or other third parties, either domestically or overseas, in addition to the possibility of legal action brought against us. Furthermore, in such cases, we cannot guarantee that the compensation amount we may be required to pay will be covered by product liability insurance. In addition, deteriorating costs stemming from factors including changes in product specifications and process delays could affect the Group's operating performance.

In October 2013, Southern California Edison Company of the United States and other parties filed a demand for arbitration against MHI and Mitsubishi Nuclear Energy Systems, Inc., under the dispute resolution procedure specified in the contract for the supply of replacement steam generators for the San Onofre Nuclear Generating Station, also in the United States. In the arbitration, the parties claimed compensation for damages against MHI and Mitsubishi Nuclear Energy Systems alleging breach of contract.

### iii. Intellectual Property

The Group values its intellectual property, which comprises the outcomes of its R&D, as an important management resource. While appropriately preserving these resources through patent rights, we are engaged in the provision of technology to, and the introduction of technology from, third parties. However, we cannot guarantee that we will be able to either acquire or acquire under favorable conditions the technology we need from third parties. Moreover, if competitors took legal action against us regarding the use of intellectual property and we lost, we may become unable to use particular technologies, be liable for damages, or face obstacles in the continuation of our business activities. We cannot guarantee that we will not face legal action from employees or former employees regarding compensation for employee invention.

## 04 RISKS RELATED TO LEGAL REGULATIONS

### i. Laws and Regulations

The Group conducts business in accordance with various domestic and overseas laws and regulations. These include laws and regulations related to taxation, the environment, and labor and occupational health and safety; economic laws and regulations, such as antitrust and anti-dumping laws; laws and regulations related to bribery, and trade and exchange; business-related laws and regulations, such as the construction industry law; and the securities listing regulations at financial instrument exchanges. The Group endeavors to fully comply with these laws and regulations. In accordance with these laws and regulations, the Group may become subject to investigation or examination by the relevant authorities. Furthermore, the Group may be subject to administrative penalties, such as fines, reassessment, determination, the payment of surcharges, suspension of business, or other steps. Moreover, the Group may face legal action from the relevant authorities or other concerned parties for damages incurred.

In September 2013, in a plea agreement entered into with the U.S. Department of Justice, MHI made an admission of the factual basis for a violation of U.S. antitrust laws regarding the sale of compressors and condensers for automobile air-conditioning systems to certain customers. Following the settlement of a plea agreement, legal action was taken against numerous businesses, including MHI and its subsidiaries, requiring them to pay civil damages in North America.

### ii. Environmental Regulations

The Group complies with various domestic and overseas environmental regulations related to air pollution, water pollution, soil and groundwater contamination, waste disposal, the use of toxic substances, energy conservation, and countermeasures to global warming. The Group's financial position and operating results may be affected in the following circumstances: environmental regulations are tightened in the future; the Group faces liabilities based on legal responsibilities related to its business activities in the past, present, or future; or the Group incurs costs when engaging in social responsibility initiatives, such as the voluntary removal of toxic substances.

## 05 RISKS RELATED TO EMPLOYEES AND RELATED COMPANIES

### i. Securing Human Resources

The competitiveness of the Group is supported by the exemplary specialist knowledge and skills of its employees in various areas, such as R&D, design, procurement, manufacturing, and construction. To secure a large number of excellent human resources and further expand our global business activities, we are actively engaged in recruiting activities both domestically and overseas. However, we cannot guarantee that we will be able to secure an adequate number of human resources. We are also working to nurture human resources by strengthening the transfer of technology and technical skills. However, we cannot guarantee that these measures will be sufficiently effective.

### ii. Related Companies

MHI and its consolidated subsidiaries, non-consolidated equity-method subsidiaries, and affiliated companies accounted for by the equity method have established a framework for mutual cooperation. However, due to independent management, trends in business and the business performance of these companies may influence the Group's financial position and operating results.

## 06 OTHER RISKS

### i. Disasters

To minimize the occurrence of damage and the spread of damage in the event of storms, earthquakes, lightening strikes, floods, fires, the global spread of contagious diseases (pandemics), or various other disasters, the Group is engaged in the implementation of inspections and training as well as the establishment of communication systems and a business continuity plan (BCP). However, material and human loss, in addition to the serious damage and loss of functionality experienced by social infrastructure, may influence the Group's activities, particularly manufacturing activities at factories. Moreover, we cannot guarantee that damages will be covered by damage insurance.

### ii. Information Security

The Group comes into contact with large amounts of confidential information, including that of clients, in the execution of its business activities. Furthermore, we possess confidential information regarding our technologies, operations, and other aspects of business. If confidential information is lost or leaked outside the Company due to computer viruses, unauthorized access, or other unforeseen circumstances, the Group's businesses may be affected.

# CONSOLIDATED BALANCE SHEETS

Mitsubishi Heavy Industries, Ltd. and Consolidated Subsidiaries
As of March 31, 2016 and 2015

| | In millions of yen | | In thousands of U.S. dollars (Note 4) |
|---|---|---|---|
| ASSETS | 2016 | 2015 | 2016 |
| **Current assets:** | | | |
| Cash and deposits (Notes 5 and 23) | ¥ 310,523 | ¥ 367,415 | $ 2,755,795 |
| Trade receivables (Note 5) | 1,205,689 | 1,291,278 | 10,700,115 |
| Merchandise and finished products | 184,657 | 182,281 | 1,638,773 |
| Work in process | 991,408 | 985,570 | 8,798,438 |
| Raw materials and supplies | 156,313 | 157,010 | 1,387,229 |
| Deferred income taxes (Note 8) | 137,428 | 150,939 | 1,219,630 |
| Other current assets (Note 13) | 547,848 | 429,027 | 4,861,980 |
| Allowance for doubtful accounts (Note 1) | (7,694) | (11,519) | (68,281) |
| **Total current assets** | 3,526,173 | 3,552,002 | 31,293,690 |
| **Non-current assets:** | | | |
| **Property, plant and equipment, net** (Notes 10 and 25): | | | |
| Buildings and structures | 397,292 | 377,804 | 3,525,843 |
| Machinery and transportation equipment | 257,306 | 259,358 | 2,283,510 |
| Tools, equipment and furniture | 56,570 | 49,451 | 502,041 |
| Land | 197,898 | 184,691 | 1,756,283 |
| Leased assets | 3,334 | 4,856 | 29,588 |
| Construction in progress | 75,497 | 78,635 | 670,012 |
| **Total property, plant and equipment, net** | 987,900 | 954,797 | 8,767,305 |
| **Intangible assets** (Note 1): | | | |
| Goodwill | 145,605 | 95,588 | 1,292,199 |
| Others | 132,468 | 145,925 | 1,175,612 |
| **Total intangible assets** | 278,074 | 241,513 | 2,467,820 |
| **Investments and advances:** | | | |
| Investment securities (Notes 5 and 6) | 534,287 | 583,496 | 4,741,631 |
| Long-term loans | 4,946 | 19,422 | 43,894 |
| Asset for retirement benefit (Notes 1 and 14) | 27,459 | 67,377 | 243,690 |
| Deferred income taxes (Note 8) | 15,808 | 15,495 | 140,291 |
| Others | 125,601 | 97,808 | 1,114,669 |
| Allowance for doubtful accounts (Note 1) | (8,452) | (11,558) | (75,008) |
| **Total investments and advances** | 699,650 | 772,043 | 6,209,176 |
| **Total non-current assets** | 1,965,625 | 1,968,354 | 17,444,311 |
| **Total assets** | ¥5,491,799 | ¥5,520,357 | $48,738,010 |

See accompanying notes to consolidated financial statements.

| | In millions of yen | | In thousands of U.S. dollars (Note 4) |
|---|---|---|---|
| **LIABILITIES AND NET ASSETS** | **2016** | 2015 | **2016** |
| **Liabilities** | | | |
| **Current liabilities:** | | | |
| Trade payables (Note 5) | **¥ 763,761** | ¥ 794,780 | **$ 6,778,141** |
| Electronically recorded obligations (Note 5) | **96,888** | 74,430 | **859,850** |
| Short-term borrowings (Notes 5, 9 and 10) | **293,131** | 177,780 | **2,601,446** |
| Current portion of long-term borrowings (Notes 5, 9 and 10) | **61,715** | 54,985 | **547,701** |
| Commercial papers (Notes 5 and 9) | **45,000** | 95,000 | **399,361** |
| Current portion of bonds (Notes 5 and 9) | **20,000** | — | **177,493** |
| Income taxes payable | **18,091** | 30,113 | **160,552** |
| Reserve for product warranties (Note 1) | **15,128** | 15,796 | **134,256** |
| Reserve for loss on construction contracts (Note 1) | **56,866** | 59,529 | **504,668** |
| Reserve for loss on passenger vessel construction business (Notes 1 and 12) | **72,842** | 105,280 | **646,450** |
| Reserve for stock benefits (Note 1) | **98** | — | **869** |
| Advance payments received on contracts | **749,747** | 663,176 | **6,653,771** |
| Other current liabilities (Notes 8 and 9) | **404,661** | 358,359 | **3,591,240** |
| **Total current liabilities** | **2,597,931** | 2,429,232 | **23,055,830** |
| **Non-current liabilities:** | | | |
| Bonds (Notes 5 and 9) | **245,000** | 245,000 | **2,174,298** |
| Long-term borrowings (Notes 5, 9 and 10) | **387,302** | 402,822 | **3,437,184** |
| Deferred income taxes (Note 8) | **63,903** | 105,536 | **567,119** |
| Reserve for stock benefits (Note 1) | **966** | — | **8,572** |
| Reserve for treatment of PCB waste (Note 1) | **7,258** | 9,845 | **64,412** |
| Liability for retirement benefits (Notes 1 and 14) | **124,890** | 129,008 | **1,108,359** |
| Other non-current liabilities (Note 9) | **66,467** | 78,896 | **589,873** |
| **Total non-current liabilities** | **895,789** | 971,109 | **7,949,849** |
| **Total liabilities** | **3,493,720** | 3,400,342 | **31,005,679** |
| **Net assets:** | | | |
| **Stockholders' equity** (Note 21): | | | |
| Common stock, without par value: | | | |
| Authorized shares: 6,000,000,000 | | | |
| Issued shares: 2016 and 2015–3,373,647,813 | **265,608** | 265,608 | **2,357,188** |
| Capital surplus | **203,951** | 204,039 | **1,810,001** |
| Retained earnings | **1,173,053** | 1,148,268 | **10,410,481** |
| Treasury stock (2016–16,140,149 shares and 2015–17,806,756 shares) at cost | **(4,771)** | (5,249) | **(42,341)** |
| **Total stockholders' equity** | **1,637,842** | 1,612,668 | **14,535,339** |
| **Accumulated other comprehensive income (loss):** | | | |
| Unrealized holding gain (loss) on investment securities | **40,108** | 81,499 | **355,946** |
| Unrealized gain (loss) from hedging instruments | **3,044** | 802 | **27,014** |
| Translation adjustments | **17,762** | 68,413 | **157,632** |
| Retirement benefits liability adjustments (Note 1) | **(18,998)** | 17,383 | **(168,601)** |
| **Total accumulated other comprehensive income (loss)** | **41,917** | 168,100 | **372,000** |
| **Share subscription rights** (Note 22) | **2,616** | 3,129 | **23,216** |
| **Non-controlling interests** | **315,702** | 336,117 | **2,801,757** |
| **Total net assets** | **1,998,078** | 2,120,014 | **17,732,321** |
| **Total liabilities and net assets** | **¥5,491,799** | ¥5,520,357 | **$48,738,010** |

# CONSOLIDATED STATEMENTS OF INCOME

Mitsubishi Heavy Industries, Ltd. and Consolidated Subsidiaries
For the fiscal years ended March 31, 2016 and 2015

| | In millions of yen | | In thousands of U.S. dollars (Note 4) |
|---|---|---|---|
| | 2016 | 2015 | 2016 |
| Net sales | ¥4,046,810 | ¥3,992,110 | $35,914,181 |
| Cost of sales | 3,184,596 | 3,161,157 | 28,262,300 |
| Gross profit | 862,213 | 830,953 | 7,651,872 |
| Selling, general and administrative expenses (Notes 22 and 24) | 552,707 | 534,812 | 4,905,102 |
| Operating income | 309,506 | 296,140 | 2,746,769 |
| Non-operating income (expense): | | | |
| Interest income | 6,602 | 7,324 | 58,590 |
| Dividend income | 8,975 | 5,539 | 79,650 |
| Income from equity method investments | 5,647 | — | 50,115 |
| Foreign exchange gain | — | 13,862 | — |
| Other income | 6,828 | 3,284 | 60,596 |
| Interest expense | (13,338) | (15,365) | (118,370) |
| Foreign exchange loss | (21,908) | — | (194,426) |
| Loss from equity method investments | — | (14,128) | — |
| Loss on disposal of fixed assets | (12,959) | (6,312) | (115,007) |
| Other expenses (Note 19) | (16,853) | (15,557) | (149,565) |
| Total non-operating income (expense) | (37,006) | (21,352) | (328,416) |
| Ordinary income | 272,500 | 274,787 | 2,418,352 |
| Extraordinary gain (loss): | | | |
| Gain on negative goodwill (Note 15) | 6,867 | — | 60,942 |
| Gain on sales of fixed assets (Note 16) | 5,663 | 3,960 | 50,257 |
| Gain on revision of retirement benefit plan | 2,208 | — | 19,595 |
| Gain on changes in equity interest | — | 17,157 | — |
| Gain on return of assets from retirement benefit trust (Note 14) | — | 11,986 | — |
| Gain on sales of investment securities | — | 10,787 | — |
| Loss on passenger vessel construction business reserve (Notes 1 and 17) | (103,911) | (69,534) | (922,177) |
| Business structure improvement expenses (Notes 18 and 19) | (47,251) | (16,449) | (419,337) |
| Impairment loss (Note 19) | (3,393) | — | (30,111) |
| Total extraordinary gain (loss) | (139,817) | (42,090) | (1,240,832) |
| Profit before income taxes | 132,682 | 232,697 | 1,177,511 |
| Income taxes (Note 8): | | | |
| Current | 50,379 | 73,222 | 447,097 |
| Deferred | 5,651 | 27,921 | 50,150 |
| Total income taxes | 56,031 | 101,143 | 497,257 |
| Profit | 76,650 | 131,553 | 680,244 |
| Profit attributable to non-controlling interests | 12,816 | 21,141 | 113,738 |
| Profit attributable to owners of parent | ¥ 63,834 | ¥ 110,412 | $ 566,506 |

| | In yen | | In U.S. dollars (Note 4) |
|---|---|---|---|
| Per share information of common stock (Note 1): | 2016 | 2015 | 2016 |
| Profit attributable to owners of parent - basic | ¥19.02 | ¥32.90 | $0.169 |
| Profit attributable to owners of parent - diluted | 18.97 | 32.82 | 0.168 |
| Cash dividends | 12.00 | 11.00 | 0.106 |

See accompanying notes to consolidated financial statements.

# CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Mitsubishi Heavy Industries, Ltd. and Consolidated Subsidiaries
For the fiscal years ended March 31, 2016 and 2015

| | In millions of yen | | In thousands of U.S. dollars (Note 4) |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Profit | **¥ 76,650** | ¥131,553 | **$ 680,244** |
| **Other comprehensive income (loss):** | | | |
| Unrealized holding gain (loss) on investment securities | **(42,469)** | 38,632 | **(376,899)** |
| Unrealized gain (loss) from hedging instruments | **418** | 1,111 | **3,709** |
| Translation adjustments | **(51,910)** | 32,988 | **(460,685)** |
| Retirement benefits liability adjustments | **(35,066)** | 48,677 | **(311,199)** |
| Share of other comprehensive income (loss) of entities accounted for by the equity method | **(6,249)** | 4,417 | **(55,457)** |
| **Total other comprehensive income (loss)** (Note 20) | **(135,277)** | 125,827 | **(1,200,541)** |
| **Comprehensive income (loss)** | **¥ (58,626)** | ¥257,381 | **$ (520,287)** |
| **Comprehensive income (loss) attributable to:** | | | |
| Owners of parent | **¥ (62,348)** | ¥230,686 | **$ (553,319)** |
| Non-controlling interests | **3,721** | 26,694 | **33,022** |

See accompanying notes to consolidated financial statements.

# CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS

Mitsubishi Heavy Industries, Ltd. and Consolidated Subsidiaries
For the fiscal years ended March 31, 2016 and 2015

| | In millions of yen | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Stockholders' equity | | | | | Accumulated other comprehensive income | | | | | | | |
| | Common stock | Capital surplus | Retained earnings | Treasury stock | Total stockholders' equity | Unrealized holding gain (loss) on investment securities | Unrealized gain (loss) from hedging instruments | Translation adjustments | Retirement benefits liability adjustments | Total accumulated other comprehensive income | Share subscription rights | Non-controlling interests | Total net assets |
| **Balance as of March 31, 2014** | ¥265,608 | ¥203,978 | ¥1,031,371 | ¥(5,385) | ¥1,495,573 | ¥ 43,188 | ¥(1,001) | ¥ 34,658 | ¥(29,019) | ¥47,825 | ¥2,635 | ¥228,188 | ¥1,774,223 |
| Cumulative effects of changes in accounting policies | | | 49,547 | | 49,547 | | | | | | | | 49,547 |
| **Restated balance** | ¥265,608 | ¥203,978 | ¥1,080,918 | ¥(5,385) | ¥1,545,120 | ¥43,188 | ¥(1,001) | ¥34,658 | ¥(29,019) | ¥47,825 | ¥2,635 | ¥228,188 | ¥1,823,770 |
| Cash dividends (Note 21) | | | (30,199) | | (30,199) | | | | | | | | (30,199) |
| Profit attributable to owners of parent | | | 110,412 | | 110,412 | | | | | | | | 110,412 |
| Changes in scope of consolidation | | | (12,862) | | (12,862) | | | | | | | | (12,862) |
| Changes in scope of equity method | | | | | — | | | | | | | | — |
| Changes in treasury stock of parent arising from transactions with non-controlling shareholders | | | | | — | | | | | | | | — |
| Purchase of treasury stock | | | | (32) | (32) | | | | | | | | (32) |
| Disposal of treasury stock | | 61 | | 168 | 230 | | | | | | | | 230 |
| Net changes in items other than stockholders' equity | | | | | | 38,311 | 1,804 | 33,754 | 46,403 | 120,274 | 493 | 107,929 | 228,696 |
| Subtotal | — | 61 | 67,350 | 136 | 67,547 | 38,311 | 1,804 | 33,754 | 46,403 | 120,274 | 493 | 107,929 | 296,244 |
| **Balance as of March 31, 2015** | ¥265,608 | ¥204,039 | ¥1,148,268 | ¥(5,249) | ¥1,612,668 | ¥ 81,499 | ¥ 802 | ¥ 68,413 | ¥ 17,383 | ¥168,100 | ¥3,129 | ¥336,117 | ¥2,120,014 |
| Cumulative effects of changes in accounting policies | | | | | — | | | | | | | | — |
| **Restated balance** | ¥265,608 | ¥204,039 | ¥1,148,268 | ¥(5,249) | ¥1,612,668 | ¥ 81,499 | ¥ 802 | ¥ 68,413 | ¥ 17,383 | ¥168,100 | ¥3,129 | ¥336,117 | ¥2,120,014 |
| Cash dividends (Note 21) | | | (40,275) | | (40,275) | | | | | | | | (40,275) |
| Profit attributable to owners of parent | | | 63,834 | | 63,834 | | | | | | | | 63,834 |
| Changes in scope of consolidation | | | (461) | | (461) | | | | | | | | (461) |
| Changes in scope of equity method | | | 1,687 | | 1,687 | | | | | | | | 1,687 |
| Changes in treasury stock of parent arising from transactions with non-controlling shareholders | | (211) | | | (211) | | | | | | | | (211) |
| Purchase of treasury stock | | | | (32) | (32) | | | | | | | | (32) |
| Disposal of treasury stock | | 123 | | 509 | 633 | | | | | | | | 633 |
| Net changes in items other than stockholders' equity | | | | | | (41,390) | 2,241 | (50,651) | (36,382) | (126,182) | (512) | (20,415) | (147,110) |
| Subtotal | — | (87) | 24,784 | 477 | 25,174 | (41,390) | 2,241 | (50,651) | (36,382) | (126,182) | (512) | (20,415) | (121,936) |
| **Balance as of March 31, 2016** | ¥265,608 | ¥203,951 | ¥1,173,053 | ¥(4,771) | ¥1,637,842 | ¥ 40,108 | ¥ 3,044 | ¥ 17,762 | ¥(18,998) | ¥ 41,917 | ¥2,616 | ¥315,702 | ¥1,998,078 |

| | In thousands of U.S. dollars (Note 4) | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Stockholders' equity | | | | | Accumulated other comprehensive income | | | | | | | |
| | Common stock | Capital surplus | Retained earnings | Treasury stock | Total stockholders' equity | Unrealized holding gain (loss) on investment securities | Unrealized gain (loss) from hedging instruments | Translation adjustments | Retirement benefits liability adjustments | Total accumulated other comprehensive income | Share subscription rights | Non-controlling interests | Total net assets |
| **Balance as of March 31, 2015** | $2,357,188 | $1,810,782 | $10,190,521 | $(46,583) | $14,311,927 | $ 723,278 | $ 7,117 | $ 607,144 | $ 154,268 | $ 1,491,835 | $27,768 | $2,982,933 | $18,814,465 |
| Cumulative effects of changes in accounting policies | | | | | — | | | | | | | | — |
| **Restated balance** | $2,357,188 | $1,810,782 | $10,190,521 | $(46,583) | $14,311,927 | $ 723,278 | $ 7,117 | $ 607,144 | $ 154,268 | $ 1,491,835 | $27,768 | $2,982,933 | $18,814,465 |
| Cash dividends (Note 21) | | | (357,428) | | (357,428) | | | | | | | | (357,428) |
| Profit attributable to owners of parent | | | 566,506 | | 566,506 | | | | | | | | 566,506 |
| Changes in scope of consolidation | | | (4,091) | | (4,091) | | | | | | | | (4,091) |
| Changes in scope of equity method | | | 14,971 | | 14,971 | | | | | | | | 14,971 |
| Changes in treasury stock of parent arising from transactions with non-controlling shareholders | | (1,872) | | | (1,872) | | | | | | | | (1,872) |
| Purchase of treasury stock | | | | (283) | (283) | | | | | | | | (283) |
| Disposal of treasury stock | | 1,091 | | 4,517 | 5,617 | | | | | | | | 5,617 |
| Net changes in items other than stockholders' equity | | | | | | (367,323) | 19,888 | (449,511) | (322,878) | (1,119,826) | (4,543) | (181,176) | (1,305,555) |
| Subtotal | — | (772) | 219,950 | 4,233 | 223,411 | (367,323) | 19,888 | (449,511) | (322,878) | (1,119,826) | (4,543) | (181,176) | (1,082,144) |
| **Balance as of March 31, 2016** | $2,357,188 | $1,810,001 | $10,410,481 | $(42,341) | $14,535,339 | $ 355,946 | $27,014 | $ 157,632 | $(168,601) | $ 372,000 | $23,216 | $2,801,757 | $17,732,321 |

See accompanying notes to consolidated financial statements.

# CONSOLIDATED STATEMENTS OF CASH FLOWS

Mitsubishi Heavy Industries, Ltd. and Consolidated Subsidiaries
For the fiscal years ended March 31, 2016 and 2015

| | In millions of yen | | In thousands of U.S. dollars (Note 4) |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| **Cash flows from operating activities:** | | | |
| Profit before income taxes | **¥ 132,682** | ¥ 232,697 | **$ 1,177,511** |
| Adjustments to reconcile profit before income taxes to net cash provided by operating activities: | | | |
| Depreciation and amortization | **158,706** | 157,010 | **1,408,466** |
| Impairment loss | **3,393** | — | **30,111** |
| Amortization of goodwill | **11,416** | 11,937 | **101,313** |
| Increase (decrease) in liability for retirement benefits | **(7,820)** | (2,409) | **(69,400)** |
| Interest and dividend income | **(15,577)** | (12,864) | **(138,241)** |
| Interest expense | **13,338** | 15,365 | **118,370** |
| (Income) loss from equity method investments | **(5,647)** | 14,128 | **(50,115)** |
| (Gain) loss on changes in equity interest | **—** | (17,157) | **—** |
| (Gain) loss on sales of investment securities | **—** | (10,787) | **—** |
| (Gain) loss on sales of fixed assets | **(5,663)** | (3,960) | **(50,257)** |
| Loss on disposal of fixed assets | **12,959** | 6,312 | **115,007** |
| Gain on negative goodwill | **(6,867)** | — | **(60,942)** |
| Gain on revision of retirement benefit plan | **(2,208)** | — | **(19,595)** |
| Business structure improvement expenses | **47,251** | 16,449 | **419,337** |
| Loss on passenger vessel construction business reserve | **103,911** | 69,534 | **922,177** |
| Gain on return of assets from retirement benefit trust | **—** | (11,986) | **—** |
| (Increase) decrease in receivables | **75,764** | 29,145 | **672,381** |
| (Increase) decrease in inventories and advances to suppliers | **(116,847)** | (156,049) | **(1,036,980)** |
| (Increase) decrease in other assets | **(202,252)** | (8,798) | **(1,794,923)** |
| Increase (decrease) in payables | **(3,228)** | 5,373 | **(28,647)** |
| Increase (decrease) in advance payments received on contracts | **107,093** | 24,934 | **950,417** |
| Increase (decrease) in other liabilities | **(4,214)** | (17,341) | **(37,397)** |
| Others | **19,090** | 2,507 | **169,417** |
| Subtotal | **315,280** | 344,040 | **2,798,012** |
| Interest and dividends received | **18,393** | 18,905 | **163,232** |
| Interest paid | **(13,800)** | (15,960) | **(122,470)** |
| Income taxes paid | **(49,870)** | (134,151) | **(442,580)** |
| Net cash provided by operating activities | **270,002** | 212,834 | **2,396,183** |
| **Cash flows from investing activities:** | | | |
| Net (increase) decrease in time deposits | **(2,180)** | (2,230) | **(19,346)** |
| Purchases of property, plant, equipment and intangible assets | **(161,160)** | (163,402) | **(1,430,244)** |
| Proceeds from sales of property, plant and equipment and intangible assets | **12,535** | 14,378 | **111,244** |
| Purchases of investment securities | **(13,112)** | (50,319) | **(116,364)** |
| Proceeds from sales and redemption of investment securities | **11,055** | 29,758 | **98,109** |
| Purchase of investments in subsidiaries that result in change in scope of consolidation | **(105,425)** | — | **(935,614)** |
| Proceeds from purchase of investments in subsidiaries that result in change in scope of consolidation | **9,574** | — | **84,966** |
| Proceeds from sales of investments in subsidiaries that result in change in scope of consolidation | **—** | 2,573 | **—** |
| Payment for sales of investments in subsidiaries that result in change in scope of consolidation | **(6,369)** | — | **(56,522)** |
| Payments for transfer of business | **(2,708)** | — | **(24,032)** |
| Disbursement of long-term loans | **(6,240)** | (18,275) | **(55,378)** |
| Collection of long-term loans | **4,259** | 15,498 | **37,797** |
| Others | **(2,706)** | (2,130) | **(24,014)** |
| Net cash used in investing activities | **(262,479)** | (174,149) | **(2,329,419)** |
| **Cash flows from financing activities:** | | | |
| Net increase (decrease) in short-term borrowings and commercial papers | **20,506** | 57,256 | **181,984** |
| Proceeds from long-term borrowings | **44,889** | 97,115 | **398,375** |
| Repayment of long-term borrowings | **(58,859)** | (188,683) | **(522,355)** |
| Proceeds from issuance of bonds | **20,000** | 70,000 | **177,493** |
| Payment for redemption of bonds | **—** | (70,000) | **—** |
| Proceeds from issuance of stock to non-controlling shareholders | **4,144** | 25,228 | **36,776** |
| Dividends paid to stockholders | **(40,269)** | (30,139) | **(357,374)** |
| Dividends paid to non-controlling shareholders | **(10,494)** | (4,133) | **(93,130)** |
| Purchase of investments in subsidiaries that do not result in change in scope of consolidation | **(571)** | — | **(5,067)** |
| Others | **(2,452)** | (2,516) | **(21,760)** |
| Net cash used in financing activities | **(23,106)** | (45,872) | **(205,058)** |
| Effect of exchange rate changes on cash and cash equivalents | **(35,194)** | (945) | **(312,335)** |
| **Net increase (decrease) in cash and cash equivalents** | **(50,778)** | (8,133) | **(450,638)** |
| Cash and cash equivalents at the beginning of the year | **357,349** | 370,710 | **3,171,361** |
| Increase in cash and cash equivalents due to changes in scope of consolidation | **649** | — | **5,759** |
| Decrease in cash and cash equivalents due to changes in scope of consolidation | **(6,953)** | (10,845) | **(61,705)** |
| Increase in cash and cash equivalents from corporate partition | **—** | 5,617 | **—** |
| **Cash and cash equivalents at the end of the year** (Note 23) | **¥ 300,267** | ¥ 357,349 | **$ 2,664,776** |

See accompanying notes to consolidated financial statements.

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Mitsubishi Heavy Industries, Ltd. and Consolidated Subsidiaries
Fiscal years ended March 31, 2016 and 2015

## 01 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### a) Basis of presenting consolidated financial statements

The accompanying consolidated financial statements of the Mitsubishi Heavy Industries Group (the "Group"), which consists of Mitsubishi Heavy Industries, Ltd. ("MHI") and its consolidated subsidiaries ("Subsidiaries"), have been prepared in accordance with accounting principles generally accepted in Japan, which are different in certain respects as to the application and disclosure requirements of International Financial Reporting Standards, and have been prepared from the consolidated financial statements filed with the Financial Services Agency ("FSA") of Japan.

As permitted by the Financial Instruments and Exchange Act of Japan, amounts of less than one million yen have been omitted. Consequently, the totals shown in the accompanying consolidated financial statements (both in yen and U.S. dollars) do not necessarily agree with the sums of the individual amounts.

### b) Principles of consolidation

The accompanying consolidated financial statements for the fiscal years ended March 31, 2016 and 2015 include the accounts of the Group. All significant inter-company transactions and accounts have been eliminated. Investments in affiliates are accounted for by the equity method.

### c) Foreign currency translation

Foreign currency monetary assets and liabilities are translated into Japanese yen at the exchange rates in effect at the balance sheet date and the resulting translation gains or losses are included in profit.

All assets and liabilities of overseas subsidiaries and affiliates are translated into Japanese yen at the exchange rates in effect at the balance sheet date, revenues and expenses at the average exchange rates during the fiscal year, and stockholders' equity at historical rates. The resulting foreign currency translation adjustments are accounted for as a component of net assets.

### d) Securities

Securities include (1) investments in unconsolidated subsidiaries and affiliates and (2) other securities (available-for-sale securities). Their valuation standards and methods are as follows:

(1) Investments in unconsolidated subsidiaries and affiliates excluding those accounted for by the equity method:
Historical cost (moving average method).

(2a) Other securities with market value:
Market value method based on market prices or other fair values at the balance sheet date. Unrealized holding gains or losses net of tax effect, are accounted for as a component of net assets. The costs of sold securities are computed based on the moving average method.

(2b) Other securities without market value:
Historical cost (moving average method).
As to the presentation of the balance sheet, the Group has classified securities due within one year in "Other current assets" in "Current assets" and the others as "Investment securities" in "Investments and advances."

### e) Inventories

Merchandise and finished products are principally stated at cost determined by the moving average method. (Balance sheet amounts are determined by the method of writing down to reflect a decline in the profitability of the assets.)

Work in process is principally stated at cost determined by the specific identification method. (Balance sheet amounts are determined by the method of writing down to reflect a decline in the profitability of the assets.)

Raw materials and supplies are principally stated at cost determined by the moving average method. (Balance sheet amounts are determined by the method of writing down to reflect a decline in the profitability of the assets.)

### f) Depreciation of property, plant and equipment

Depreciation of property, plant and equipment (excluding leased assets) is principally computed using the straight-line method for buildings (excluding the equipment attached to them) and the declining-balance method for the other items of property, plant and equipment over the assets' useful lives.

Depreciation of leased assets is computed using the straight-line method over the lease terms.

### g) Amortization of intangible assets

Amortization of intangible assets (excluding leased assets) is computed using the straight-line method over the assets' useful lives.

Amortization of leased assets is computed using the straight-line method over the lease terms.

Goodwill is amortized on a straight-line basis over the investment recovery period of up to 20 years.

### h) Allowance for doubtful accounts

Allowance for doubtful accounts is provided for possible losses on the collection of receivables. The amount of the allowance for general receivables is based on the write-off ratio. As for certain receivables such as the ones from the debtors whose solvency is in doubt, the recoverability of each receivable is examined individually and the estimated unrecoverable amounts are recognized as the allowance.

### i) Reserve for product warranties

Reserve for product warranties is provided for the product warranty expenditure after products are delivered. The amounts are estimated based on the past experience.

### j) Reserve for loss on construction contracts

Reserve for loss on construction contracts is provided for the expected total losses to be realized in the following years on the construction contracts if (1) those losses are judged inevitable at current fiscal year-end and (2) reasonable estimation of the amounts of such losses is possible.

With regard to the construction contracts for which this reserve is recognized, if the fiscal year-end balances of their work in process already exceed their respective total contract revenues, the exceeding portion is recognized as the loss on devaluation of the work in process and, accordingly, is not included in the reserve for losses on construction contracts.

### k) Reserve for loss on passenger vessel construction business

Reserve for loss on passenger vessel construction business is provided based on reasonable estimation for the expected loss to be realized in the following fiscal years from the construction project of two large-sized cruise ships for the AIDA Cruises brand.

### l) Reserve for stock benefits

Reserve for stock benefits is provided in relation to the plan to grant MHI stock to the corporate officers and executive management personnel through a trust. The estimated value of the MHI stock corresponding to the Stock Grant Points held by the eligible persons as at the balance sheet date is recognized.

### m) Reserve for treatment of PCB waste

Reserve for treatment of PCB (poly chlorinated biphenyl) waste is provided based on estimated costs of the treatment of PCB products and equipment.

### n) Liability for retirement benefits

Liability for retirement benefits is provided for employees' retirement benefits by deducting the pension assets (including a retirement benefit trust) from the retirement benefit obligations, based on estimated balances at the end of the fiscal year.

Prior service costs are either expensed as incurred or amortized by the straight-line method over a period shorter than the average remaining service period of employees.

Actuarial gains and losses for each fiscal year are amortized by the straight-line method, starting in the following fiscal year of occurrence, over a period shorter than the average remaining service period of employees.

Unrecognized actuarial gains and losses and unrecognized prior service costs after tax are recorded in "Retirement benefits liability adjustments" within the net assets section as a component of accumulated other comprehensive income.

### o) Revenue recognition

With regard to construction contracts, the percentage-of-completion method is applied if reliable estimates of the (1) total costs on and revenues from a contract and (2) percentage of completion at the balance sheet date are available. In applying this method, the percentage of completion at the balance sheet date is estimated based on the costs incurred to date divided by the estimated total costs on the contracts. The completed-contract method is applied when the above conditions are not met.

### p) Hedge Accounting

The principal method in applying the hedge accounting is deferral hedge accounting, where gains or losses on a hedging instrument are deferred (and recognized as a component of net assets, net of tax effect) until the losses or gains on the hedged item are recognized in the income statement.

The Group applies the "exceptional method for interest rate swaps" (hereinafter referred to as the "exceptional method") when the transactions meet the requirements of relevant accounting standards.

The "exceptional method" is applied when an interest rate swap (hedging instrument) with the corresponding conditions (e.g. principal amount, maturity and index) to the hedged item is concluded to fix the interest rate on the hedged item. Under this method, the amounts to be paid or received under the contract are added to or deducted from the interest; the fair value of the hedging instrument is not computed.

The Group evaluates the effectiveness of its hedging activities by reference to the accumulated gains or losses on the hedging instruments and those on the hedged items from the commencement of the hedges.

### q) Tax-effect accounting

Deferred income taxes arise from temporary differences between the financial reporting and tax bases of assets and liabilities. They are accounted for under the asset and liability method, where the amounts of deferred income taxes are calculated using the future tax rates in effect when the temporary differences are recovered or settled.

### r) Cash and cash equivalents

For the purpose of the consolidated statements of cash flows, cash and cash equivalents consist of cash on hand, demand deposits and short-term highly liquid investments with maturities of three months or less when purchased that have insignificant risk of changes in value.

### s) Earnings per share

The computation of basic profit attributable to owners of parent per share is based on the profit attributable to owners of parent available to common stockholders and the weighted average number of shares outstanding during each period.

Diluted profit attributable to owners of parent per share is computed based on the assumption that all the share subscription rights are exercised at the beginning of the fiscal year (or issue date if later).

### t) Fiscal years of consolidated subsidiaries

The financial statements of Shanghai MHI Turbocharger Co., Ltd., etc. (36 companies in total), whose fiscal year end is December 31, 2015, are consolidated by using their financial statements of the parent fiscal year end, which are prepared solely for consolidation purposes. The financial statements of Mitsubishi Hitachi Power Systems Europe GmbH, etc. (7 companies in total), are consolidated by using their financial statements as of their respective fiscal year end, which falls on December 31, and necessary adjustments are made to their financial statements to reflect any significant transactions from January 1 to March 31.

## 02 CHANGE IN ACCOUNTING POLICY

Application of the Accounting Standard for Business Combinations and related accounting standards
The MHI Group has applied the "Revised Accounting Standard for Business Combinations" (ASBJ Statement No. 21, September 13, 2013; hereinafter the "Accounting Standard for Business Combinations"), "Revised Accounting Standard for Consolidated Financial Statements" (ASBJ Statement No. 22, September 13, 2013; hereinafter the "Accounting Standard for Consolidated Financial Statements"), and "Revised Accounting Standard for Business Divestitures" (ASBJ Statement No. 7, September 13, 2013; hereinafter the "Accounting Standard for Business Divestitures"), etc., effective from the fiscal year ended March 31, 2016. As a result, the method of recording the amount of difference caused by changes in MHI's ownership interests in subsidiaries in the case of subsidiaries under ongoing control of MHI was changed to one in which it is recorded as capital surplus, and the method of recording acquisition-related costs was changed to one in which they are recognized as expenses for the fiscal year in which they are incurred. Furthermore, for business combinations carried out on or after the beginning of the fiscal year ended March 31, 2016, the accounting method was changed to one in which the revision of the purchase price allocation due to the finalization of the tentative accounting treatment is reflected in the fiscal year in which the business combination is originally recorded. In addition, a change in the presentation of net income, etc., and a change in the presentation of minority interests to non-controlling interests were adopted.

The application of the Accounting Standard for Business Combinations, etc., is subject to the transitional treatment provided for in Paragraph 58-2(4) of the Accounting Standard for Business Combinations, Paragraph 44-5(4) of the Accounting Standard for Consolidated Financial Statements, and Paragraph 57-4(4) of the Accounting Standard for Business Divestitures. Accordingly, these standards have been applied prospectively from the beginning of the fiscal year ended March 31, 2016.

In the fiscal year ended March 31, 2016, cash flow in relation to the purchase or sales of investments in subsidiaries that do not result in change in scope of consolidation is classified as "Cash flows from financing activities" in the consolidated statements of cash flows. Additionally, cash flow in relation to the cost incurred in purchase or sales of investments in subsidiaries that do not result in change in scope of consolidation and the cost incurred in purchase of investments in subsidiaries that result in change in scope of consolidation is classified as "Cash flows from operating activities".
The impact of these changes on the consolidated financial statements and per share information of common stock is insignificant.

## 03 ADDITIONAL INFORMATION

a) Stock Grant ESOP (Employee Stock Ownership Plan) Trust

From the fiscal year ended March 31,2016 MHI and its main subsidiaries have implemented transactions of delivering MHI stock to its employees who hold an important managerial position (hereinafter, Management Personnel) through a trust.

(1) Overview of transaction

A stock grant ESOP Trust (ESOP Trust) was established by the Group for the purpose of improving the Group's business performance and corporate value in the medium and long terms by promoting the Management Personnel's motivation and willingness to participate in management.

The Group established a trust in which its Management Personnel who meet certain requirements are the beneficiaries and the Group contributes the amount required to purchase MHI stock to ESOP Trust. Based on predetermined regulations of awarding stock, ESOP Trust will acquire the estimated number of MHI stock to be awarded to the Management Personnel from MHI (disposal of treasury stock) or from the stock market.

According to the regulations of awarding stock, eligible Management Personnel are awarded a specific number of points each fiscal year based on their contribution to the Group during the period of ESOP Trust. Subsequently, ESOP Trust delivers MHI stock or a cash benefit to the Management Personnel based on the total number of points awarded to them.

(2) MHI stock in ESOP Trust

MHI stock in ESOP Trust is recorded in treasury stock under net assets based on the book value in ESOP Trust. The book value and the number of these treasury stock as of March 31, 2016, were 148 million yen ($1,313 thousand) and 500,198 shares, respectively.

b) Officer Remuneration BIP (Board Incentive Plan) Trust

From the fiscal year ended March 31, 2016, MHI and its main subsidiaries have implemented transactions of delivering MHI stock to MHI's directors (excluding outside directors and also audit and supervisory committee members), MHI's corporate officers, MHI's main subsidiaries' directors (excluding outside directors) and also MHI's main subsidiaries' corporate officers (hereinafter, collectively referred as Directors and Other Executives) through a trust.

(1) Overview of transaction

An officer remuneration BIP Trust (BIP Trust) was established by the Group for the purpose of improving the Group's business performance and corporate value in the medium and long terms by promoting the Directors and Other Executives motivation and willingness to participate in management.

The Group established a trust in which its Directors and Other Executives who meet certain requirements are the beneficiaries and the Group contributes the amount required to purchase MHI stock to BIP Trust. Based on predetermined regulations of awarding stock, BIP Trust will acquire the estimated number of MHI stock to be awarded to Directors and Other Executives from MHI (disposal of treasury stock) or from the stock market.

According to the regulations of awarding stock, eligible Directors and Other Executives are awarded a specific number of points each fiscal year based on their contribution to the Group during the period of BIP Trust. Subsequently, BIP Trust delivers MHI stock or cash benefit to the Directors and Other Executives based on the total number of points awarded to them.

Based on the qualifications of the beneficiaries, the Group classified BIP Trust as follows:
[BIP Trust I] : available for MHI's directors

[BIP Trust II] : available for MHI's corporate officers and its main subsidiaries' directors and corporate officers

(2) MHI stock in BIP Trust

MHI stock in BIP Trust is recorded in treasury stock under net assets based on the book value in BIP Trust. The book value and the number of these treasury stock as of March 31, 2016 were 1,644 million yen ($14,589 thousand) and 5,551,000 shares, respectively.

## 04 U.S. DOLLAR AMOUNTS

U.S. dollar amounts are included solely for convenience. These translations should not be construed as representations that the Japanese yen actually represent, or have been or could be converted into, U.S. dollars.

As the amounts shown in U.S. dollars are for convenience only, the rate of ¥112.68 = US$1 prevailing at March 31, 2016 is used for the purpose of the presentation of the U.S. dollar amounts in the accompanying consolidated financial statements.

## 05 FINANCIAL INSTRUMENTS

The carrying amounts on the consolidated balance sheets, fair values and the variance between them of financial instruments as of March 31, 2016 and 2015 are shown in the following table. Those whose fair values are extremely difficult to determine are excluded from the following table and shown in Footnote 2. See Note 1 p) for the information on hedge accounting.

| | In millions of yen | | | In thousands of U.S. dollars | | |
|---|---|---|---|---|---|---|
| | **2016** | | | **2016** | | |
| | Carrying amount | Fair value | Variance | Carrying amount | Fair value | Variance |
| (1) Cash and deposits | **¥ 310,523** | **¥ 310,523** | **¥ —** | **$ 2,755,795** | **$ 2,755,795** | **$ —** |
| (2) Trade receivables | **1,205,689** | **1,205,689** | **—** | **10,700,115** | **10,700,115** | **—** |
| (3) Securities and investment securities | **378,429** | **393,995** | **15,565** | **3,358,439** | **3,496,583** | **138,134** |
| **Asset items total** | **¥1,894,641** | **¥1,910,207** | **¥15,565** | **$16,814,350** | **$16,952,493** | **$138,134** |
| (4) Trade payables | **763,761** | **763,761** | **—** | **6,778,141** | **6,778,141** | **—** |
| (5) Electronically recorded obligations | **96,888** | **96,888** | **—** | **859,850** | **859,850** | **—** |
| (6) Short-term borrowings | **293,131** | **293,131** | **—** | **2,601,446** | **2,601,446** | **—** |
| (7) Commercial papers | **45,000** | **45,000** | **—** | **399,361** | **399,361** | **—** |
| (8) Bonds | **265,000** | **271,513** | **6,513** | **2,351,792** | **2,409,593** | **57,800** |
| (9) Long-term borrowings | **449,017** | **471,240** | **22,223** | **3,984,886** | **4,182,108** | **197,222** |
| **Liability items total** | **¥1,912,798** | **¥1,941,535** | **¥28,736** | **$16,975,488** | **$17,230,520** | **$255,023** |
| (10) Derivatives (*) | **¥ 2,774** | **¥ 2,774** | **¥ —** | **$ 24,618** | **$ 24,618** | **$ —** |

(*) The derivatives positions shown are net amounts. The amounts in parentheses show liability balances.

| | In millions of yen | | |
|---|---|---|---|
| | 2015 | | |
| | Carrying amount | Fair value | Variance |
| (1) Cash and deposits | ¥ 367,415 | ¥ 367,415 | ¥ — |
| (2) Trade receivables | 1,291,278 | 1,291,278 | — |
| (3) Securities and investment securities | 433,678 | 483,903 | 50,224 |
| **Asset items total** | ¥2,092,372 | ¥2,142,596 | ¥50,224 |
| (4) Trade payables | 794,780 | 794,780 | — |
| (5) Electronically recorded obligations | 74,430 | 74,430 | — |
| (6) Short-term borrowings | 177,780 | 177,780 | — |
| (7) Commercial papers | 95,000 | 95,000 | — |
| (8) Bonds | 245,000 | 252,309 | 7,309 |
| (9) Long-term borrowings | 457,807 | 483,332 | 25,524 |
| **Liability items total** | ¥1,844,798 | ¥1,877,632 | ¥32,834 |
| (10) Derivatives (*) | ¥ (669) | ¥ (669) | ¥ — |

(*) The derivatives positions shown are net amounts. The amounts in parentheses show liability balances.

(Footnote 1) The computation method of the fair values of financial instruments:

(1) Cash and deposits
The book values are used as the fair values since all the deposits are short term and the fair values are almost equal to the book values.

(2) Trade receivables
The book values are used as the fair values since a large portion of these are settled in a short period and the fair values could be deemed to be almost equal to the book values.

(3) Securities and investment securities
Market prices are used as the fair values.

(4) Trade payables; (5) Electronically recorded obligations; (6) Short-term borrowings; (7) Commercial papers
The book values are used as the fair values since they are settled in a short period and the fair values are almost equal to the book values.

(8) Bonds
Market prices are used as the fair values.

(9) Long-term borrowings
The present values of the principal and total interest (*) (discounted by the rate assumed to be applied to new borrowings of the same conditions) are used as the fair values.
(*) As for the long-term borrowings to which the "exceptional method" for interest rate swaps is applied, the principal and total interest according to the interest rate under the interest rate swaps are used.

(10) Derivatives
See Note 7.

(Footnote 2) Financial instruments shown below are excluded from the above table because they do not have market prices and it is extremely difficult to determine their fair values.

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Carrying amounts of unlisted securities | **¥157,737** | ¥151,338 | **$1,399,866** |

(Footnote 3) The contractual maturities of monetary receivables and other securities at March 31, 2016 and 2015 were as follows:

| | In millions of yen | | | | In thousands of U.S. dollars | | | |
|---|---|---|---|---|---|---|---|---|
| | **2016** | | | | **2016** | | | |
| | Due within one year | Due after one year through five years | Due after five years through 10 years | Due after 10 years | Due within one year | Due after one year through five years | Due after five years through 10 years | Due after 10 years |
| Cash and deposits | **¥ 302,142** | **¥ —** | **¥ —** | **¥—** | **$ 2,681,416** | **$ —** | **$ —** | **$—** |
| Trade receivables | **1,170,230** | **35,308** | **150** | **—** | **10,385,427** | **313,347** | **1,331** | **—** |
| Securities and investment securities | | | | | | | | |
| Other securities | | | | | | | | |
| Government bonds | **0** | **—** | **—** | **—** | **0** | **—** | **—** | **—** |
| **Total** | **¥1,472,372** | **¥35,308** | **¥150** | **¥—** | **$13,066,844** | **$313,347** | **$1,331** | **$—** |

| | In millions of yen | | | |
|---|---|---|---|---|
| | 2015 | | | |
| | Due within one year | Due after one year through five years | Due after five years through 10 years | Due after 10 years |
| Cash and deposits | ¥ 353,384 | ¥ — | ¥ — | ¥— |
| Trade receivables | 1,263,357 | 26,770 | 1,149 | — |
| Securities and investment securities | | | | |
| Other securities | | | | |
| Government bonds | 0 | — | — | — |
| **Total** | ¥1,616,742 | ¥26,770 | ¥1,149 | ¥— |

## 06 SECURITIES

a) Breakdown of other securities with market value at March 31, 2016 and 2015

| | In millions of yen | | | In thousands of U.S. dollars | | |
|---|---|---|---|---|---|---|
| | **2016** | | | **2016** | | |
| | Carrying amount | Acquisition cost | Unrealized gain (loss) | Carrying amount | Acquisition cost | Unrealized gain (loss) |
| i) Carrying amounts exceed acquisition costs: | | | | | | |
| Equity securities | **¥173,314** | **¥ 87,314** | **¥ 86,000** | **$1,538,107** | **$ 774,884** | **$ 763,223** |
| Debt securities | | | | | | |
| Government bonds | **0** | **0** | **0** | **0** | **0** | **0** |
| Others | **—** | **—** | **—** | **—** | **—** | **—** |
| Subtotal | **¥173,314** | **¥ 87,314** | **¥ 86,000** | **$1,538,107** | **$ 774,884** | **$ 763,223** |
| ii) Acquisition costs exceed carrying amounts: | | | | | | |
| Equity securities | **¥109,466** | **¥144,099** | **¥(34,633)** | **$ 971,476** | **$1,278,833** | **$(307,357)** |
| Debt securities | | | | | | |
| Government bonds | **—** | **—** | **—** | **—** | **—** | **—** |
| Others | **—** | **1** | **(1)** | **—** | **8** | **(8)** |
| Others | **1,575** | **1,616** | **(41)** | **13,977** | **14,341** | **(363)** |
| Subtotal | **¥111,042** | **¥145,718** | **¥(34,676)** | **$ 985,463** | **$1,293,201** | **$(307,738)** |
| **Total (i + ii)** | **¥284,356** | **¥233,032** | **¥ 51,324** | **$2,523,571** | **$2,068,086** | **$ 455,484** |

| | In millions of yen | | |
|---|---|---|---|
| | 2015 | | |
| | Carrying amount | Acquisition cost | Unrealized gain (loss) |
| i) Carrying amounts exceed acquisition costs: | | | |
| Equity securities | ¥249,012 | ¥132,015 | ¥116,996 |
| Debt securities | | | |
| Government bonds | 0 | 0 | 0 |
| Others | 406 | 394 | 11 |
| Subtotal | ¥249,419 | ¥132,410 | ¥117,008 |
| ii) Acquisition costs exceed carrying amounts: | | | |
| Equity securities | ¥ 93,069 | ¥100,972 | ¥ (7,903) |
| Debt securities | | | |
| Government bonds | — | — | — |
| Others | 0 | 1 | (1) |
| Others | 1,198 | 1,198 | — |
| Subtotal | ¥ 94,268 | ¥102,173 | ¥ (7,904) |
| **Total (i + ii)** | ¥343,687 | ¥234,583 | ¥109,103 |

Footnote: If the market values of the securities decline substantially and if the Group judges that they have no chance of recovery, impairment losses on them are recognized and the acquisition costs of them are reduced by the same amounts.

b) Sales amounts of other securities with market value and related gains and losses for the fiscal years ended March 31, 2016 and 2015

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Sales amounts | **¥5,998** | ¥126,729 | **$53,230** |
| Gains | **3,158** | 10,690 | **28,026** |
| Losses | **(210)** | (218) | **(1,863)** |

c) Impairment losses on other securities with market value for the fiscal years ended March 31, 2016 and 2015

Although impairment losses on other securities were recorded for the fiscal years ended March 31, 2016 and 2015, disclosure was omitted as the amounts were immaterial.

Securities with market value are judged as impaired when their market values decline from their book values by (i) 50% or more at the end of a fiscal year, or (ii) between 30% and 50% at four consecutive quarter-ends (Q1-Q4) of a fiscal year.

## 07 DERIVATIVE FINANCIAL INSTRUMENTS

The Group uses derivatives for the purpose of reducing the risks mentioned below and does not enter into derivatives for speculative or trading purposes.

The derivative financial instruments which the Group utilizes are principally foreign currency forward and option contracts and interest rate swaps. The former is to hedge against the exchange rate risks on the receivables or payables denominated in foreign currencies and the latter is to fix the interest rates on certain long-term borrowings. See Note 1 p) for the information on hedge accounting.

The use of the derivatives is subject to the internal control policy; the objective of the derivatives transactions is limited to hedging against such risks as exchange rate risks and interest rate risks and their use is limited to the extent corresponding to actual business. Accordingly, the Group believes that market risks resulting from the change in exchange rates and interest rates are insignificant. The Group also believes that the risk of nonperformance by counterparties is insignificant because all the counterparties are banks with high credit ratings.

Summarized below are the notional amounts and the fair values of the derivative positions outstanding at March 31, 2016 and 2015.

## 1. Derivatives to which hedge accounting is not applied

a) Forward foreign exchange contracts (*1)

| | In millions of yen | | | | In thousands of U.S. dollars | | | |
|---|---|---|---|---|---|---|---|---|
| | 2016 | | | | 2016 | | | |
| | Notional amount | Therein: portion due after one year | Fair value | Unrealized gain (loss) | Notional amount | Therein: portion due after one year | Fair value | Unrealized gain (loss) |
| Sell: | | | | | | | | |
| USD | ¥80,797 | ¥5,109 | ¥ 998 | ¥ 998 | $717,048 | $45,340 | $ 8,856 | $ 8,856 |
| EUR | 23,837 | 1,618 | (730) | (730) | 211,545 | 14,359 | (6,478) | (6,478) |
| Others | 11,541 | 463 | 13 | 13 | 102,422 | 4,108 | 115 | 115 |
| Buy: | | | | | | | | |
| USD | ¥82,111 | ¥4,449 | ¥ 490 | ¥ 490 | $728,709 | $39,483 | $ 4,348 | $ 4,348 |
| EUR | 39,871 | 907 | (271) | (271) | 353,842 | 8,049 | (2,405) | (2,405) |
| Others | 19,288 | 1,058 | 272 | 272 | 171,175 | 9,389 | 2,413 | 2,413 |
| **Total** | ¥ — | ¥ — | ¥ 772 | ¥ 772 | $ — | $ — | $ 6,851 | $ 6,851 |

| | In millions of yen | | | |
|---|---|---|---|---|
| | 2015 | | | |
| | Notional amount | Therein: portion due after one year | Fair value | Unrealized gain (loss) |
| Sell: | | | | |
| USD | ¥71,435 | ¥ — | ¥(232) | ¥(232) |
| EUR | 16,199 | 1,245 | (130) | (130) |
| Others | 25,865 | 6,400 | 541 | 541 |
| Buy: | | | | |
| USD | ¥37,403 | ¥3,849 | ¥ (32) | ¥ (32) |
| EUR | 12,657 | 1,433 | (183) | (183) |
| Others | 32,256 | 4,703 | (480) | (480) |
| **Total** | ¥ — | ¥ — | ¥(518) | ¥(518) |

(*1) The fair values of exchange contracts are based on forward exchange rates.

b) Forward equity contracts (*1)

| | In millions of yen | | | |
|---|---|---|---|---|
| | 2015 | | | |
| | Notional amount | Therein: portion due after one year | Fair value | Unrealized gain (loss) |
| Forward equity contracts (buy) | ¥3,199 | ¥— | ¥34 | ¥34 |

(*1) The fair values of equity contracts are provided by the counterparty of financial institution.

## 2. Derivatives to which hedge accounting is applied

(1) Forward foreign exchange contracts (to which deferral hedge accounting is applied)

| | In millions of yen | | | In thousands of U.S. dollars | | |
|---|---|---|---|---|---|---|
| | 2016 | | | 2016 | | |
| | Notional amount | Therein: portion due after one year | Fair value | Notional amount | Therein: portion due after one year | Fair value |
| Sell: (*1) | | | | | | |
| USD | ¥34,587 | ¥1,975 | ¥1,073 | $306,948 | $17,527 | $ 9,522 |
| EUR | 8,164 | — | (116) | 72,452 | — | (1,029) |
| Others | 11,400 | 3,152 | (549) | 101,171 | 27,973 | (4,872) |
| Buy: (*2) | | | | | | |
| USD | 3,770 | 2,270 | 6 | 33,457 | 20,145 | 53 |
| EUR | 673 | 301 | 1,516 | 5,972 | 2,671 | 13,454 |
| Others | 450 | — | 70 | 3,993 | — | 621 |
| **Total** | ¥ — | ¥ — | ¥2,001 | $ — | $ — | $17,758 |

| | In millions of yen | | |
|---|---|---|---|
| | 2015 | | |
| | Notional amount | Therein: portion due after one year | Fair value |
| Sell: (*1) | | | |
| USD | ¥10,656 | ¥ 2,692 | ¥(235) |
| EUR | 3,228 | — | 614 |
| Others | 14,410 | 14,410 | (534) |
| Buy: (*2) | | | |
| USD | 4,077 | 3,932 | (115) |
| EUR | 1,579 | — | (34) |
| Others | 721 | 721 | 119 |
| **Total** | ¥ — | ¥ — | ¥(185) |

(*1) The hedged items on these derivatives are principally trade receivables.
(*2) The hedged items on these derivatives are principally trade payables.

(2) Interest rate swaps (to which the "exceptional method" for interest rate swaps is applied) (*1)

| | In millions of yen | | | In thousands of U.S. dollars | | |
|---|---|---|---|---|---|---|
| | **2016** | | | **2016** | | |
| Type of transactions | Notional amount | Therein: portion due after one year | Fair value | Notional amount | Therein: portion due after one year | Fair value |
| Fixed payment / variable receipt | **¥207,283** | **¥201,931** | **(*2)** | **$1,839,572** | **$1,792,074** | **(*2)** |

| | In millions of yen | | |
|---|---|---|---|
| | 2015 | | |
| Type of transactions | Notional amount | Therein: portion due after one year | Fair value |
| Fixed payment / variable receipt | ¥206,896 | ¥186,651 | (*2) |

(*1) The hedged items on these derivatives are principally long-term borrowings.
(*2) Since the "exceptional method" for interest rate swaps is applied, the above interest rate swaps are treated as part of the hedged long-term borrowings, thus their fair values are included in those of the long-term borrowings, which are shown in Note 5.

## 08 INCOME TAXES

The Group is subject to corporation income tax, inhabitants' tax and enterprise tax, based on income, which in the aggregate resulted in the statutory tax rates of approximately 32.9% and 35.4% for the fiscal years ended March 31, 2016 and 2015, respectively.

a) Significant components of deferred tax assets and liabilities at March 31, 2016 and 2015, which arose as a result of the recognition of the tax effect mentioned in Note 1 q), were as follows:

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Deferred tax assets: | | | |
| Tax loss carryforwards | **¥ 113,610** | ¥ 78,730 | **$ 1,008,253** |
| Liability for retirement benefits | **75,329** | 64,730 | **668,521** |
| Accrued expenses for product warranties | **32,307** | 48,354 | **286,714** |
| Reserve for loss on passenger vessel construction business | **22,356** | 34,605 | **198,402** |
| Accrued expenses for construction contracts | **22,124** | 23,722 | **196,343** |
| Reserve for loss on construction contracts | **17,156** | 18,545 | **152,254** |
| Depreciation | **12,998** | 11,001 | **115,353** |
| Loss on revaluation of investment securities | **11,127** | 11,765 | **98,748** |
| Write-downs of inventories | **9,686** | 10,896 | **85,960** |
| Others | **140,102** | 149,195 | **1,243,361** |
| Subtotal | **456,799** | 451,547 | **4,053,949** |
| Valuation allowance | **(160,527)** | (134,105) | **(1,424,627)** |
| Total gross deferred tax assets | **296,271** | 317,442 | **2,629,313** |
| Deferred tax liabilities: | | | |
| Reserve for specified business restructuring investment loss | **(40,580)** | (42,607) | **(360,134)** |
| Gain on contribution or return of securities related retirement benefit trust | **(24,416)** | (55,823) | **(216,684)** |
| Identified intangible assets due to business combination | **(24,374)** | (30,363) | **(216,311)** |
| Reserve for reduction in costs of fixed assets | **(22,178)** | (24,627) | **(196,822)** |
| Unrealized holding gain on investment securities | **(16,977)** | (41,806) | **(150,665)** |
| Others | **(78,797)** | (61,785) | **(699,298)** |
| Total gross deferred tax liabilities | **(207,324)** | (257,014) | **(1,839,936)** |
| Net deferred tax assets (liabilities)* | **¥ 88,947** | ¥ 60,428 | **$ 789,376** |

*Net deferred tax assets (liabilities) at March 31, 2016 and 2015 are reflected in the consolidated balance sheets as follows:

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Deferred income taxes in current assets | **¥137,428** | ¥150,939 | **$1,219,630** |
| Deferred income taxes in investments and advances | **15,808** | 15,495 | **140,291** |
| Other liabilities in current liabilities | **(384)** | (470) | **(3,407)** |
| Deferred income taxes in non-current liabilities | **(63,903)** | (105,536) | **(567,119)** |

b) Reconciliation of the statutory tax rate and the income tax rate as a percentage of income before income taxes

| | **2016** | 2015 |
|---|---|---|
| Statutory tax rate | **32.9%** | 35.4% |
| Reconciliation: | | |
| Non-deductible expenses | **0.9** | 2.5 |
| Items excluded from gross income | **1.1** | 0.4 |
| (Income) loss from equity method investments | **(1.4)** | 2.2 |
| Valuation allowance | **6.6** | (1.3) |
| Tax exemption for research and development expenses | **(1.7)** | (0.8) |
| Reduction in deferred tax assets due to changes in statutory tax rate | **4.0** | 5.7 |
| Gain on changes in equity interest | **—** | (2.6) |
| Others | **(0.2)** | 2.0 |
| Income tax rate as a percentage of income before income taxes | **42.2%** | 43.5% |

c) Adjustment to deferred tax assets and deferred tax liabilities due to changes in corporate income tax rate

As the "Law for Partial Amendment of the Income Tax Law, etc." (Law No. 15 of 2016) and the "Law for Partial Amendment of the Local Tax Law, etc." (Law No. 13 of 2016) were enacted in the Japanese National Diet on March 29, 2016, the reduction in the corporate income tax rate became effective for fiscal years beginning on or after April 1, 2016. In conjunction with these changes, the statutory tax rate used to measure deferred tax assets and liabilities for the temporary differences estimated to be resolved in or after the fiscal year beginning on April 1, 2016 has been changed.

As a result, "Deferred tax assets (net of deferred tax liabilities)" decreased by 4,886 million yen ($43,361 thousand), while "Income taxes (deferred)", "Unrealized holding gain (loss) on investment securities", "Retirement benefits liability adjustments" and "Unrealized gain (loss) from hedging instruments" increased by 5,271 million yen ($46,778 thousand), 765 million yen ($6,789 thousand), 400 million yen ($3,549 thousand), and 20 million yen ($177 thousand), respectively, as of and for the fiscal year ended March 31, 2016.

## 09 INTEREST-BEARING DEBT AND LEASE OBLIGATIONS

a) Short-term interest-bearing debt at March 31, 2016 and 2015 consisted of the following:

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Short-term loans, principally from banks (with weighted-average interest rate of 0.6% at March 31, 2016) | **¥293,131** | ¥177,780 | **$2,601,446** |
| Current portion of bonds | **20,000** | — | **177,493** |
| Current portion of long-term loans, principally from banks and insurance companies (with weighted-average interest rate of 2.5% at March 31, 2016) | **61,715** | 54,985 | **547,701** |
| Commercial papers (with weighted-average interest rate of 0.0% at March 31, 2016) | **45,000** | 95,000 | **399,361** |
| **Total** | **¥419,846** | ¥327,766 | **$3,726,002** |

b) Bonds at March 31, 2016 and 2015 consisted of the following:

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Unsecured bonds issued by MHI: | | | |
| 2.04% bonds due Sep 2016 (issued in Sep 2006) | **¥ 20,000** | ¥ 20,000 | **$ 177,493** |
| 2.03% bonds due Sep 2017 (issued in Sep 2007) | **60,000** | 60,000 | **532,481** |
| 1.482% bonds due Dec 2019 (issued in Dec 2009) | **50,000** | 50,000 | **443,734** |
| 0.366% bonds due Sep 2018 (issued in Sep 2013) | **30,000** | 30,000 | **266,240** |
| 0.877% bonds due Sep 2023 (issued in Sep 2013) | **15,000** | 15,000 | **133,120** |
| 0.243% bonds due Sep 2019 (issued in Sep 2014) | **15,000** | 15,000 | **133,120** |
| 0.381% bonds due Sep 2021 (issued in Sep 2014) | **25,000** | 25,000 | **221,867** |
| 0.662% bonds due Sep 2024 (issued in Sep 2014) | **30,000** | 30,000 | **266,240** |
| 0.221% bonds due Sep 2020 (issued in Sep 2015) | **10,000** | — | **88,746** |
| 0.630% bonds due Sep 2025 (issued in Sep 2015) | **10,000** | — | **88,746** |
| **Total** | **¥265,000** | ¥245,000 | **$2,351,792** |

The aggregate annual maturities of bonds at March 31, 2016 were as follows:

| Fiscal years ending March 31 | In millions of yen | In thousands of U.S. dollars |
|---|---|---|
| 2017 (= current portion) | **¥ 20,000** | **$ 177,493** |
| 2018 | **60,000** | **532,481** |
| 2019 | **30,000** | **266,240** |
| 2020 | **65,000** | **576,854** |
| 2021 | **10,000** | **88,746** |
| Thereafter | **80,000** | **709,975** |
| Non-current portion subtotal | **245,000** | **2,174,298** |
| **Total** | **¥265,000** | **$2,351,792** |

c) Long-term borrowings at March 31, 2016 and 2015 consisted of the following:

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Non-current portion of long-term loans, principally from banks and insurance companies, due 2017 to 2033 (with weighted-average interest rate of 1.5% at March 31, 2016) | **¥387,302** | ¥402,822 | **$3,437,184** |

The aggregate annual maturities of long-term borrowings at March 31, 2016 were as follows:

| Fiscal years ending March 31 | In millions of yen | In thousands of U.S. dollars |
|---|---|---|
| 2017 (= current portion) | **¥ 61,715** | **$ 547,701** |
| 2018 | **92,680** | **822,506** |
| 2019 | **64,009** | **568,059** |
| 2020 | **40,593** | **360,250** |
| 2021 | **49,233** | **436,927** |
| Thereafter | **140,784** | **1,249,414** |
| Non-current portion subtotal | **387,302** | **3,437,184** |
| **Total** | **¥449,017** | **$3,984,886** |

d) Lease obligations at March 31, 2016 and 2015 consisted of the following:

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Current portion of lease obligations | **¥1,652** | ¥ 2,125 | **$14,660** |
| Non-current portion of lease obligations | **4,770** | 10,525 | **42,332** |
| **Total** | **¥6,423** | ¥12,651 | **$57,002** |

## 10 PLEDGED ASSETS AND RELATED LIABILITIES

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| Assets pledged as collateral | **2016** | 2015 | **2016** |
| Property, plant and equipment | **¥8,638** | ¥ 6,479 | **$76,659** |
| Others | **—** | 5,882 | **—** |
| **Total** | **¥8,638** | ¥12,361 | **$76,659** |

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| Liabilities related to the assets pledged as collateral | **2016** | 2015 | **2016** |
| Short-term borrowings | **¥1,438** | ¥1,477 | **$12,761** |
| Long-term borrowings | **614** | 358 | **5,449** |
| **Total** | **¥2,053** | ¥1,835 | **$18,219** |

## 11 CONTINGENT LIABILITIES

| Contingent liabilities | In millions of yen 2016 | 2015 | In thousands of U.S. dollars 2016 |
|---|---|---|---|
| Guarantee obligations on such debts as borrowings from financial institutions by companies outside the Group | **¥39,794** | ¥57,661 | **$353,159** |

## 12 RESERVE FOR LOSS ON PASSENGER VESSEL CONSTRUCTION BUSINESS

With respect to the passenger vessel construction business, MHI believes that it has already accounted for all provisions for loss estimated to the extent reasonably possible based on the facts already occurred. However, the actual amount of future losses may be different from the current estimate mainly as MHI is still negotiating the construction schedule for the second ship with the customer.

## 13 OTHERS

On February 1, 2014 (the "Effective Date of Company Split"), MHI and Hitachi, Ltd. ("Hitachi") integrated their businesses centered on thermal power generation systems into Mitsubishi Hitachi Power Systems, Ltd. ("MHPS"), a consolidated subsidiary of MHI, through a spin-off in the form of an absorption-type company split.

As part of this business integration, assets and liabilities, contracts with customers and others, and rights and obligations thereunder, related to the boiler construction projects for Medupi and Kusile thermal power stations (the "South African Projects"), for which companies such as Hitachi Power Africa Proprietary Limited ("HPA"), a consolidated subsidiary of Hitachi in the Republic of South Africa, received orders in 2007, were transferred from HPA to Mitsubishi Hitachi Power Systems Africa Proprietary Limited ("MHPS-Africa"), a consolidated subsidiary of MHI (the "South African Asset Transfer").

Under the contract between MHI and Hitachi regarding the South African Asset Transfer, it is agreed that Hitachi and HPA shall be responsible for any contingent liabilities arising from events that had occurred before the Effective Date of Company Split and for any claim that had already accrued as of the said date, while MHPS and MHPS-Africa shall be responsible for the execution of the project from the Effective Date of Company Split, and on that basis, the future project schedule and project cash flow estimation dating back to the Effective Date of Company Split shall be refined, and the definitive price of the South African Asset Transfer shall be determined based on the refined estimate, and the difference from the tentative price shall be adjusted.

MHI and Hitachi have not completed the price adjustment of the South African Asset Transfer at the moment. Meanwhile, MHPS-Africa has the right to receive the price adjustment payments and other payments from Hitachi or HPA in the amount calculated under the contract because it was already expected as of the Effective Date of Company Split that the South African Projects would incur a loss. On March 31, 2016, MHI demanded that Hitachi pay ZAR 48,200 million (equivalent to approximately 379,334 million yen ($3,366,471 thousand) converted at a rate of 7.87 yen to 1 ZAR) to MHPS-Africa as part of the price adjustment and other payments.

An amount corresponding to a portion of said rights to receive payments from Hitachi is included in "Other current assets" in the current assets on the consolidated balance sheet as of March 31, 2016.

## 14 RETIREMENT BENEFITS

The Group has several retirement benefit plans such as non-contributory defined benefit pension plan, contributory defined benefit pension plan and severance indemnity plan. There are also occasions where employees receive special lump-sum payments at retirement. Contributions to the plans are funded in accordance with the applicable laws and regulations. See Note 1 n) for accounting policies and related information.

1. Non-contributory defined benefit pension plan

a) A reconciliation of the beginning and ending balances of the retirement benefit obligations for the fiscal years ended March 31, 2016 and 2015 were as follows:

| | In millions of yen 2016 | 2015 | In thousands of U.S. dollars 2016 |
|---|---|---|---|
| Retirement benefit obligation at beginning of fiscal year | **¥565,722** | ¥642,740 | **$5,020,607** |
| Cumulative effect of change in accounting policies | **—** | (82,473) | **—** |
| Restated balance | **565,722** | 560,266 | **5,020,607** |
| Service cost | **32,793** | 35,075 | **291,027** |
| Interest cost | **5,380** | 5,500 | **47,745** |
| Actuarial loss (gain) | **6,347** | 7,359 | **56,327** |
| Benefits paid | **(58,525)** | (53,185) | **(519,391)** |
| Effect of business combinations | **11,865** | 24,007 | **105,298** |
| Others | **(11,791)** | (13,300) | **(104,641)** |
| Retirement benefit obligations, at end of fiscal year | **¥551,793** | ¥565,722 | **$4,896,991** |

b) A reconciliation of the beginning and ending balances of the fair value of plan assets for the fiscal years ended March 31, 2016 and 2015 were as follows:

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Fair value of plan assets at beginning of fiscal year | **¥504,091** | ¥ 533,271 | **$4,473,651** |
| Expected return on plan assets | **10,233** | 10,934 | **90,814** |
| Actuarial gain (loss) | **(54,961)** | 77,855 | **(487,761)** |
| Employer contributions | **23,564** | 19,799 | **209,123** |
| Benefits paid | **(30,557)** | (33,665) | **(271,183)** |
| Effect of business combinations | **4,183** | 16,412 | **37,122** |
| Return of assets from retirement benefit trust | **—** | (115,486) | **—** |
| Others | **(2,192)** | (5,029) | **(19,453)** |
| Fair value of plan assets at end of fiscal year | **¥454,363** | ¥ 504,091 | **$4,032,330** |

c) A reconciliation of the ending balance of the retirement benefit obligations and the fair value of plan assets to the amounts recognized in the consolidated balance sheets at March 31, 2016 and 2015 were as follows:

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Retirement benefit obligation for funded plans | **¥ 511,243** | ¥ 517,515 | **$ 4,537,122** |
| Fair value of plan assets | **(454,363)** | (504,091) | **(4,032,330)** |
| | **56,879** | 13,423 | **504,783** |
| Retirement benefit obligation for unfunded plans | **40,550** | 48,207 | **359,868** |
| Net amount recognized in consolidated balance sheets | **¥ 97,430** | ¥ 61,631 | **$ 864,660** |
| | | | |
| Liability for retirement benefits | **¥ 124,890** | ¥ 129,008 | **$ 1,108,359** |
| Asset for retirement benefits | **(27,459)** | (67,377) | **(243,690)** |
| Net amount recognized in consolidated balance sheets | **¥ 97,430** | ¥ 61,631 | **$ 864,660** |

d) The components of net periodic retirement benefit expenses for the fiscal years ended March 31, 2016 and 2015 were as follows:

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Service cost | **¥ 32,778** | ¥ 35,019 | **$290,894** |
| Interest cost | **5,380** | 5,500 | **47,745** |
| Expected return on plan assets | **(10,233)** | (10,934) | **(90,814)** |
| Amortization of actuarial loss (gain) | **7,900** | 2,707 | **70,110** |
| Amortization of prior service cost (credit) | **(2,742)** | (616) | **(24,334)** |
| Retirement benefit expense | **¥ 33,082** | ¥ 31,678 | **$293,592** |

e) Retirement benefits liability adjustments

The amounts recognized in other comprehensive income consisted of the following on a pretax basis for the fiscal years ended March 31, 2016 and 2015.

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Prior service (cost) credit | **¥ 1,618** | ¥ 766 | **$ 14,359** |
| Actuarial (loss) gain | **(53,100)** | 73,204 | **(471,246)** |
| **Total** | **¥(51,481)** | ¥73,971 | **$(456,877)** |

f) Retirement benefits liability adjustments (accumulated)

The amounts recognized in accumulated other comprehensive income consisted of the following on a pretax basis at March 31, 2016 and 2015.

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Unrecognized prior service (cost) credit | **¥ 1,978** | ¥ 359 | **$ 17,554** |
| Unrecognized actuarial (loss) gain | **(26,786)** | 26,313 | **(237,717)** |
| **Total** | **¥(24,808)** | ¥26,672 | **$(220,163)** |

g) Information on plan assets

(1) A breakdown of the plan assets by asset class at March 31, 2016 and 2015 were as follows:

| | 2016 | 2015 |
|---|---|---|
| Equity securities | 47% | 52% |
| Debt securities | 40 | 36 |
| Life insurance company general accounts | 5 | 4 |
| Cash and deposits | 4 | 5 |
| Others | 4 | 3 |
| **Total** | **100%** | 100% |

Footnote: 35% of the plan assets consist of a retirement benefit trust which is provided for the severance indemnity plans as of March 31, 2016 and 41% as of March 31, 2015.

(2) Determination of the expected long-term rate of return on plan assets

To determine the expected long-term rate of return on the plan assets, the Group considers the current and expected asset allocation, as well as current and expected future long-term returns on various assets constituting the plan assets.

h) The principal actuarial assumptions at March 31, 2016 and 2015 were as follows:

| | 2016 | 2015 |
|---|---|---|
| Discount rate | mainly 0.9% | mainly 0.9% |
| Expected long-term rate of return on plan assets | mainly 2.1% | mainly 2.1% |

2. Contributory defined benefit pension plan

Contributions made by the Group were 7,675 million yen ($68,113 thousand) in the fiscal year ended March 31, 2016 and 2,369 million yen in the fiscal year ended March 31, 2015.

## 15 GAIN ON NEGATIVE GOODWILL

Gain on negative goodwill for the fiscal year ended March 31, 2016 was due to acquisition of subsidiaries' stocks relating to the Energy & Environment business.

## 16 GAIN ON SALES OF FIXED ASSETS

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | 2016 | 2015 | 2016 |
| Land | ¥5,073 | ¥4,050 | $45,021 |
| Others | 589 | (89) | 5,227 |
| **Total** | **¥5,663** | ¥3,960 | **$50,257** |

## 17 LOSS ON PASSENGER VESSEL CONSTRUCTION BUSINESS RESERVE

The following is a description of the loss on passenger vessel construction business reserve in the fiscal year ended March 31, 2016.

In the passenger vessel construction business, MHI recognized an extraordinary loss of 64,126 million yen ($569,098 thousand) in its consolidated financial statements for the fiscal year ended March 31, 2014 and 69,534 million yen ($617,092 thousand) for the fiscal year ended March 31, 2015 under provision for loss on passenger vessel construction business reserve as a result of a significant cost overrun mainly due to difficulties in construction of the prototype ship.

In the fiscal year ended March 31, 2016, with the assignment of additional manpower, MHI pushed ahead with the works for the first ship in close coordination with the customer. However, due to design changes in the later construction phase, the need to address faults found in the final stages, and the need for modification and responses to adjustment requests of the customer in the finishing stage of interior works, delivery of the first ship was delayed. Consequently, MHI recognized an extraordinary loss of 30,953 million yen ($274,698 thousand) in the second quarter and 22,108 million yen ($196,201 thousand) in the third quarter of the fiscal year ended March 31, 2016.

In the fourth quarter of the fiscal year ended March 31, 2016, MHI made finishing touches to the ship before delivery, installed the ship's control systems and it underwent final inspections. However, the ship is fitted with cutting-edge equipment and resulting work took longer than expected, there were faults in main engines, and in addition to noise reduction measures requested by the customer during sea trials, fires broke out onboard. In the end, the delivery of the ship was completed in the middle of March 2016.

Furthermore, due to the first ship's delayed delivery and adjustments made to the first ship, as well as the customer's feedback regarding the requirements for the second ship, the construction phase of the second ship has been re-examined radically.

As a result, in the fourth quarter of the fiscal year ended March 31, 2016, MHI expected that the amount of expected future losses would exceed the previously recorded amount of provision and booked an additional extraordinary loss of 50,850 million yen ($451,277 thousand) for that quarter for an additional expected loss estimated to the extent reasonably possible as of the end of the fourth quarter. The total amount of provision for loss on passenger vessel construction business reserve recorded as extraordinary loss throughout the fiscal year ended March 31, 2016 amounted to 103,911 million yen ($922,177 thousand).

MHI recognizes the loss associated with its passenger vessel construction business which will be incurred in the future as extraordinary loss because it does not regard such loss as a loss incurred as ongoing operations.

With respect to the passenger vessel construction business, MHI believes that it has already accounted for all provisions for loss estimated to the extent reasonably possible based on the facts already occurred. However, the actual amount of future losses may be different from the current estimate mainly as MHI is still negotiating the construction schedule for the second ship with the customer.

The following is a description of the loss on passenger vessel construction business reserve in the fiscal year ended March 31, 2015.

In November 2011, MHI received an order for two large-sized cruise ships for the AIDA Cruises brand. In the course of the project, difficulties involved in the construction of a prototype became evident. Moreover, the volume of design work relating to the cruise ship cabins and other areas increased and significant design changes were made, resulting in a delay in the design work. This delay not only increased design costs but also had negative effects on the subsequent material procurement, construction process and other works, with adverse impact on the project costs. Under such circumstances, a significant loss on construction was anticipated and therefore at the end of fiscal year 2013 an extraordinary loss of 64,126 million yen was recognized as an amount of provision reasonably estimated for loss expected to be incurred in fiscal year 2014 and subsequent fiscal years.

As for the ship construction, MHI set up a new project management structure in March 2014 and pressed ahead with the construction work. In fiscal year 2014, however, as advanced specifications required for the ships were discussed and pursued with the customer, circumstances emerged involving the need for reviewing the basic ship design, including the overall layout plan of the public area, the cabins and other areas, as well as related fixtures and equipment, causing extensive redesigning and significant delay in the design work schedules.

Despite the additional design resources mobilized and other measures taken, in the second quarter of fiscal year 2014, the construction work process of the first ship had to be revised because the completion of release of the drawings was expected to be delayed from the planned date. The delay in the design work for the first ship led to another delay in the release of the drawings for the second ship, which in turn affected adversely the construction work process of the second ship.

Consequently, in the second quarter of fiscal year 2014, an extraordinary loss of 39,841 million yen was recorded as an amount of provision reasonably estimated for additional loss expected from increases in design rework costs, in construction costs due to backtrack works at later work stages and rush work required to make up delays, as well as in procurement costs associated with changes in design specifications and increases in volume of materials.

Amid such circumstances, in order to reinforce the project execution structure further, MHI brought in top-class managers such as senior general managers and their equivalents from other departments, employed foreign expert personnel, and mobilized a large number of direct workers both from inside and outside MHI. Also, by further improving the relationship of trust and enhancing communication with the customer, we are currently working closely together with the customer on the construction aiming at the completion of the first ship in September 2015.

Meanwhile, the design work ran behind the schedule planned at the close of the second quarter of fiscal year 2014. Specifically, while we expected that the overall layout plan would be approved by the customer by the end of December 2014, an agreement on specifications for the overall layout plan with the customer was actually delayed until March 2015 due to design challenges associated with the installation of an enormous quantity of pipes and electric wires in a small and narrow space inside the ship. In addition, detailed changes in the design were necessary after the construction process started in order to reflect the actual situation of the construction work site.

The ships are designed to be equipped with very high-density, interrelated complex systems and nearly 4,000 people are working in a small and narrow space inside the ship to deal with the enormous workload required. Therefore, any design change affects the entire process and gives rise to major reworks and decrease in work efficiency, resulting in more than estimated cost increase.

In addition, on-site construction cost is also expected to increase as additional resources have been mobilized for rush work in order to recover delays in the construction schedule caused by above reasons.

Consequently, in the fourth quarter of fiscal year 2014, MHI came to expect that the amount of expected future loss would exceed the amount of the provision recorded at the end of fiscal year 2013 and in the second quarter of fiscal year 2014. MHI therefore recorded at the end of the fourth quarter of fiscal year 2014 an extraordinary loss of 29,693 million yen as an amount of provision for additional loss estimated to the extent reasonably possible.

As a result, the amount of “Loss on passenger vessel construction business reserve” recorded under extraordinary loss in fiscal year 2014 totaled 69,534 million yen.

MHI recognizes future loss expected to incur associated with its cruise ship business as extraordinary loss because it does not regard such loss as a loss incurred as ongoing operations.

As most of the design-related challenges and issues concerning the construction of a prototype ship have been resolved as of the end of fiscal year 2014, MHI believes that it has already accounted for all provisions for loss related to its cruise ship business estimated to the extent reasonably possible based on the facts already occurred. However, should any new events occur in the future such as unexpected changes to specifications, the actual amount of loss may be different from the amount of provision recorded.

## 18 BUSINESS STRUCTURE IMPROVEMENT EXPENSES

Business structure improvement expenses for the fiscal year ended March 31, 2016 consisted of business reorganization expenses relating to the Energy & Environment business and the Machinery, Equipment & Infrastructure business.

Business structure improvement expenses for the fiscal year ended March 31, 2015 consisted of business reorganization expenses relating to the Energy & Environment business, Machinery, Equipment & Infrastructure business, and Others.

## 19 IMPAIRMENT LOSS

The following is a description of the impairment loss recognized in the fiscal year ended March 31, 2016.

a) Description of the impaired asset group
The impaired asset group consisted mainly of "Machinery and transportation equipment" for operating purposes which were located in Kanagawa, etc.

b) Method of asset grouping
The principal unit of asset grouping is business units under the strategic evaluation system. Basically, assets for rental purpose, idle assets and assets to be disposed of due to termination or transfer of some operations are each treated as separate asset groups.

c) Reason to recognize the impairment
The book values of some business assets were written down to their recoverable amounts since a short-term recovery of performance cannot be expected due to the deterioration of profitability, and the future cash flows to be derived from the assets have become less than their book values.

For some assets to be disposed of, their book values were written down to their recoverable amounts since they are being phased out in line with the reorganization of operations.

d) Calculation method of recoverable amount
The recoverable amount is the higher of its fair value less costs to sell and its value in use. The value in use is computed by discounting the future cash flows to be derived from the assets to the present value with the rate of mainly 8%.

e) Impairment loss amount and the breakdown

| | In millions of yen | In thousands of U.S. dollars |
|---|---|---|
| Breakdown by the income statement accounts | **2016** | **2016** |
| "Impairment loss" under extraordinary loss | **¥3,393** | **$30,111** |
| "Business structure improvement expenses" under extraordinary loss | **2,138** | **18,974** |
| **Total** | **¥5,532** | **$49,094** |

| | In millions of yen | In thousands of U.S. dollars |
|---|---|---|
| Breakdown by the category of assets | **2016** | **2016** |
| Machinery and transportation equipment | **¥3,381** | **$30,005** |
| Goodwill | **1,257** | **11,155** |
| Land, etc. | **892** | **7,916** |
| **Total** | **¥5,532** | **$49,094** |

The following is a description of the impairment loss recognized in the fiscal year ended March 31, 2015.

a) Description of the impaired asset group
The impaired asset group consisted mainly of "Machinery and transportation equipment" and "Buildings and structures" for operating purposes which were located in Hiroshima, Nagasaki, etc.

b) Method of asset grouping
The principal unit of asset grouping is business units under the strategic evaluation system. Basically, assets for rental purposes, idle assets and assets to be disposed of due to termination or transfer of some operations are each treated as separate asset groups.

c) Reason to recognize the impairment
The book values of some business assets were written down to their recoverable amounts since a short-term recovery of performance cannot be expected due to the deterioration of profitability, and the future cash flows to be derived from the assets have become less than their book values.

For some assets to be disposed of, their book values were written down to their recoverable amounts since they are being phased out in line with the reorganization of operations.

d) Calculation method of recoverable amount
The recoverable amount is the higher of its fair value less costs to sell and its value in use. The value in use is computed by discounting the future cash flows to be derived from the assets to the present value with the rate of mainly 8%.

e) Impairment loss amount and the breakdown

| | In millions of yen |
|---|---|
| Breakdown by the income statement accounts | 2015 |
| "Business structure improvement expenses" under extraordinary loss | ¥1,378 |
| "Other expenses" under non-operating expense | 806 |
| **Total** | ¥2,184 |

| Breakdown by the category of assets | In millions of yen 2015 |
|---|---|
| Machinery and transportation equipment | ¥1,581 |
| Buildings and structures | 442 |
| Tools, equipment and furniture, etc. | 161 |
| **Total** | ¥2,184 |

## 20 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Reclassification adjustments and tax effect on other comprehensive income (loss) for the fiscal years ended March 31, 2016 and 2015 were as follows:

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Unrealized holding gain (loss) on investment securities | | | |
| Gain (loss) arising during the fiscal year | **¥ (54,988)** | ¥ 60,744 | **$ (488,001)** |
| Reclassification adjustments | **(3,118)** | (7,577) | **(27,671)** |
| Unrealized holding gain (loss) on investment securities, before tax | **(58,107)** | 53,166 | **(515,681)** |
| Deferred taxes relating to net unrealized gain (loss) on investment securities | **15,637** | (14,534) | **138,773** |
| Unrealized holding gain (loss) on investment securities, net of tax | **(42,469)** | 38,632 | **(376,899)** |
| Unrealized gain (loss) from hedging instruments | | | |
| Gain (loss) arising during the fiscal year | **1,110** | 1,779 | **9,850** |
| Reclassification adjustments | **(589)** | (256) | **(5,227)** |
| Unrealized gain (loss) from holding instruments, before tax | **520** | 1,522 | **4,614** |
| Deferred taxes relating to unrealized gain (loss) from hedging instruments | **(102)** | (411) | **(905)** |
| Unrealized gain (loss) from hedging instruments, net of tax | **418** | 1,111 | **3,709** |
| Translation adjustments | | | |
| Gain (loss) arising during the fiscal year | **(52,822)** | 33,242 | **(468,778)** |
| Reclassification adjustments | **830** | (160) | **7,365** |
| Translation adjustments, before tax | **(51,992)** | 33,081 | **(461,412)** |
| Deferred taxes relating to translation adjustments | **82** | (92) | **727** |
| Translation adjustments, net of tax | **(51,910)** | 32,988 | **(460,685)** |
| Retirement benefits liability adjustments | | | |
| Gain (loss) arising during the fiscal year | **(56,966)** | 71,879 | **(505,555)** |
| Reclassification adjustments | **5,485** | 2,091 | **48,677** |
| Retirement benefits liability adjustments, before tax | **(51,481)** | 73,971 | **(456,877)** |
| Deferred taxes relating to retirement benefits liability adjustments | **16,414** | (25,293) | **145,669** |
| Retirement benefits liability adjustments, net of tax | **(35,066)** | 48,677 | **(311,199)** |
| Share of other comprehensive income (loss) of entities accounted for by the equity method | | | |
| Gain (loss) arising during the fiscal year | **(5,095)** | 6,053 | **(45,216)** |
| Reclassification adjustments | **(1,153)** | (1,636) | **(10,232)** |
| Share of other comprehensive income (loss) of entities accounted for by the equity method, net of tax | **(6,249)** | 4,417 | **(55,457)** |
| Other comprehensive income (loss) , net of tax | **¥(135,277)** | ¥125,827 | **$(1,200,541)** |

## 21 CONSOLIDATED STATEMENTS OF CHANGES IN NET ASSETS

a) Total number of shares issued and treasury stock at March 31, 2016 and 2015 were as follows:

| | Type of shares | At March 31, 2015 | Increase by March 31, 2016 | Decrease by March 31, 2016 | At March 31, 2016 |
|---|---|---|---|---|---|
| Total number of shares issued | Common stock | 3,373,647,813 | — | — | 3,373,647,813 |
| Treasury stock | Common stock | 17,806,756 | 54,040 | 1,720,647 | 16,140,149 |

(1) The number of treasury stock at March 31, 2016 includes 6,051,198 shares held by the Stock Grant ESOP Trust and the Officer Remuneration BIP Trust I & II.

(2) Reason for increase of treasury stock

| | |
|---|---|
| Repurchasing of shares that were less than the minimum trading unit | 45,761 |
| Portion of MHI's shares that equity method investees hold which is treated as treasury stock for the purpose of consolidation | 8,279 |
| **Total** | 54,040 |

(3) Reason for decrease of treasury stock

| | |
|---|---|
| Disposal resulting from the exercise of share subscription rights, which were issued for the purpose of providing stock options | 1,586,000 |
| Disposal resulting from purchase request from shareholders with shares that were less than the minimum trading unit | 2,845 |
| Disposal resulting from the implementation of the Stock Grant ESOP Trust and the Officer Remuneration BIP Trust I & II | 131,802 |
| **Total** | 1,720,647 |

b) Cash dividends

(1) Cash dividends paid

| | | | | Cash dividends per share | | Total cash dividends paid | |
|---|---|---|---|---|---|---|---|
| Resolution | Type of shares | Record date | Effective date | In yen | In U.S. dollars | In millions of yen | In thousands of U.S. dollars |
| June 26, 2015 | | | | | | | |
| Ordinary General Meeting of Shareholders | Common stock | March 31, 2015 | June 29, 2015 | ¥6 | $0.0532 | ¥20,135 | $178,691 |
| October 30, 2015 | | | | | | | |
| Board of Directors | Common stock | September 30, 2015 | December 3, 2015 | ¥6 | $0.0532 | ¥20,177 | $179,064 |
| **Total** | | | | | | ¥40,312 | $357,756 |

Note: Total cash dividends paid in accordance with the resolution by the Board of Directors held on October 30, 2015 include 37 million yen ($328 thousand) of cash dividends for the stocks held by the Stock Grant ESOP Trust and the Officer Remuneration BIP Trust I & II.

(2) Dividends of which record date is within this fiscal year but the effective date is within next fiscal year

| | | | | Cash dividends per share | | Total cash dividends paid | |
|---|---|---|---|---|---|---|---|
| Resolution | Type of shares | Record date | Effective date | In yen | In U.S. dollars | In millions of yen | In thousands of U.S. dollars |
| June 23, 2016<br>Ordinary General Meeting of Shareholders | Common stock | March 31, 2016 | June 24, 2016 | ¥6 | $0.0532 | ¥20,181 | $179,100 |

Note: Total cash dividends to be paid in accordance with the resolution by the Ordinary General Meeting of Shareholders held on June 23, 2016 include 36 million yen ($319 thousand) of cash dividends for the stocks held by the Stock Grant ESOP Trust and the Officer Remuneration BIP Trust I & II.

## 22 SHARE-BASED COMPENSATION PLANS

MHI has the following share-based compensation plans for the directors and corporate executive officers.

The share-based compensation expenses, which amounted to 24 million yen ($212 thousand) in the fiscal year ended March 31, 2016 and 679 million yen in the fiscal year ended March 31, 2015, are included in selling, general and administrative expenses.

a) Conditions for issue of stock options

| | Stock options (4th grant) | Stock options (5th grant) | Stock options (6th grant) | Stock options (7th grant) | Stock options (8th grant) | Stock options (9th grant) |
|---|---|---|---|---|---|---|
| Grantee (Number of individuals) | Directors & executive officers (25) | Directors & executive officers (30) | Directors & executive officers (33) | Executive officers (2) | Directors & executive officers (33) | Directors & executive officers (35) |
| Number of shares | 663,000 | 400,000 | 806,000 | 46,000 | 1,109,000 | 1,259,000 |
| Type of share | Common stock | Common stock | Common stock | Common stock | Common stock | Common stock |
| Grant date | Aug 17, 2006 | Aug 16, 2007 | Aug 18, 2008 | Feb 20, 2009 | Aug 17, 2009 | Aug 17, 2010 |
| Exercise period (from) | Aug 18, 2006 | Aug 17, 2007 | Aug 19, 2008 | Feb 21, 2009 | Aug 18, 2009 | Aug 18, 2010 |
| (to) | Jun 28, 2036 | Aug 16, 2037 | Aug 18, 2038 | Feb 20, 2039 | Aug 17, 2039 | Aug 17, 2040 |

| | Stock options (10th grant) | Stock options (11th grant) | Stock options (12th grant) | Stock options (13th grant) | Stock options (15th grant) | Stock options (16th grant) |
|---|---|---|---|---|---|---|
| Grantee (Number of individuals) | Directors & executive officers (38) | Directors & executive officers (40) | Directors & executive officers (37) | Executive officer (1) | Directors, executive officers & ex-executive officer (37) | Executive officer (1) |
| Number of shares | 1,364,000 | 1,632,000 | 800,000 | 41,000 | 1,328,000 | 42,000 |
| Type of share | Common stock | Common stock | Common stock | Common stock | Common stock | Common stock |
| Grant date | Dec 15, 2011 | Aug 16, 2012 | Aug 19, 2013 | Dec 13, 2013 | Aug 18, 2014 | May 11, 2015 |
| Exercise period (from) | Dec 16, 2011 | Aug 17, 2012 | Aug 20, 2013 | Dec 14, 2013 | Aug 19, 2014 | May 12, 2015 |
| (to) | Dec 15, 2041 | Aug 16, 2042 | Aug 19, 2043 | Dec 13, 2043 | Aug 18, 2044 | May 11, 2045 |

b) Activities of stock options in the fiscal year ended March 31, 2016

| | Number of shares | | | | | |
|---|---|---|---|---|---|---|
| | Stock options (4th grant) | Stock options (5th grant) | Stock options (6th grant) | Stock options (7th grant) | Stock options (8th grant) | Stock options (9th grant) |
| Unexercised at March 31, 2015 | 373,000 | 270,000 | 615,000 | 33,000 | 1,000,000 | 1,176,000 |
| Granted | — | — | — | — | — | — |
| Vested | — | — | — | — | — | — |
| Exercised | 171,000 | 152,000 | 236,000 | 10,000 | 216,000 | 250,000 |
| Expired | — | — | — | — | — | — |
| Unexercised at March 31, 2016 | 202,000 | 118,000 | 379,000 | 23,000 | 784,000 | 926,000 |

| | Number of shares | | | | | |
|---|---|---|---|---|---|---|
| | Stock options (10th grant) | Stock options (11th grant) | Stock options (12th grant) | Stock options (13th grant) | Stock options (15th grant) | Stock options (16th grant) |
| Unexercised at March 31, 2015 | 1,263,000 | 1,605,000 | 786,000 | 41,000 | 1,328,000 | — |
| Granted | — | — | — | — | — | 42,000 |
| Vested | — | — | — | — | — | 42,000 |
| Exercised | 242,000 | 282,000 | 27,000 | — | — | — |
| Expired | — | — | — | — | — | — |
| Unexercised at March 31, 2016 | 1,021,000 | 1,323,000 | 759,000 | 41,000 | 1,328,000 | 42,000 |

c) Price per share

| | In yen | | | | | |
|---|---|---|---|---|---|---|
| | Stock options (4th grant) | Stock options (5th grant) | Stock options (6th grant) | Stock options (7th grant) | Stock options (8th grant) | Stock options (9th grant) |
| Weighted-average exercise price | ¥ 1 | ¥ 1 | ¥ 1 | ¥ 1 | ¥ 1 | ¥ 1 |
| Weighted-average market share price when the share subscription rights were exercised in the fiscal year ended March 31, 2016 | 570 | 593 | 594 | 737 | 583 | 555 |
| Grant date fair value | 443 | 644 | 471 | 194 | 294 | 258 |

| | In yen | | | | | |
|---|---|---|---|---|---|---|
| | Stock options (10th grant) | Stock options (11th grant) | Stock options (12th grant) | Stock options (13th grant) | Stock options (15th grant) | Stock options (16th grant) |
| Weighted-average exercise price | ¥ 1 | ¥ 1 | ¥ 1 | ¥ 1 | ¥ 1 | ¥ 1 |
| Weighted-average market share price when the share subscription rights were exercised in the fiscal year ended March 31, 2016 | 548 | 558 | 543 | — | — | — |
| Grant date fair value | 267 | 260 | 453 | 521 | 512 | 592 |

| | In U.S. dollars | | | | | |
|---|---|---|---|---|---|---|
| | Stock options (4th grant) | Stock options (5th grant) | Stock options (6th grant) | Stock options (7th grant) | Stock options (8th grant) | Stock options (9th grant) |
| Weighted-average exercise price | $0.01 | $0.01 | $0.01 | $0.01 | $0.01 | $0.01 |
| Weighted-average market share price when the share subscription rights were exercised in the fiscal year ended March 31, 2016 | 5.06 | 5.26 | 5.27 | 6.54 | 5.17 | 4.93 |
| Grant date fair value | 3.93 | 5.72 | 4.18 | 1.72 | 2.61 | 2.29 |

| | In U.S. dollars | | | | | |
|---|---|---|---|---|---|---|
| | Stock options (10th grant) | Stock options (11th grant) | Stock options (12th grant) | Stock options (13th grant) | Stock options (15th grant) | Stock options (16th grant) |
| Weighted-average exercise price | $0.01 | $0.01 | $0.01 | $0.01 | $0.01 | $0.01 |
| Weighted-average market share price when the share subscription rights were exercised in the fiscal year ended March 31, 2016 | 4.86 | 4.95 | 4.82 | — | — | — |
| Grant date fair value | 2.37 | 2.31 | 4.02 | 4.62 | 4.54 | 5.25 |

d) Estimate method of fair value of stock options

The fair value of stock options granted in the fiscal year ended March 31, 2016 was estimated using the Black-Scholes option-pricing model with the following assumptions.

| | Stock options (16th grant) |
|---|---|
| Expected volatility (*1) | 35.474% |
| Expected life of option (*2) | 15 years |
| Expected dividends (*3) | ¥9 ($0.079) per share |
| Risk-free interest rate (*4) | 0.808% |

(*1) Estimated based on the actual share prices of 15 years (April 22, 2000 - April 22, 2015).
(*2) Calculated on the assumption that the share subscription rights would be exercised at the middle point of the exercise period.
(*3) Actual cash dividends in June and December 2014.
(*4) Yield of Japanese government bonds with the same years to maturity as the above expected life of option.

e) Estimate method of the number of vested share subscription rights

All of the share subscription rights were vested when granted.

## 23 CASH AND CASH EQUIVALENTS

"Cash and cash equivalents at end of year" in the statements of cash flows for the fiscal years ended March 31, 2016 and 2015 consisted of the following:

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Cash and deposits | **¥310,523** | ¥367,415 | **$2,755,795** |
| Time deposits with maturities over three months | **(12,135)** | (11,587) | **(107,694)** |
| Cash equivalents included in "Other current assets" | **1,879** | 1,521 | **16,675** |
| **Total** | **¥300,267** | ¥357,349 | **$2,664,776** |

## 24 RESEARCH AND DEVELOPMENT EXPENSES

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Research and development expenses | **¥150,690** | ¥145,572 | **$1,337,326** |

## 25 ACCUMULATED DEPRECIATION

| | In millions of yen | | In thousands of U.S. dollars |
|---|---|---|---|
| | **2016** | 2015 | **2016** |
| Accumulated depreciation of property, plant and equipment | **¥2,045,300** | ¥1,962,875 | **$18,151,402** |

## 26 ASSET RETIREMENT OBLIGATIONS

When the Group disposes of certain assets belonging to the nuclear energy business, those assets are required to be treated with a special care as radioactive waste. In principle, the Group recognizes asset retirement obligations on those assets. With regard to some of those assets, however, the Group does not recognize asset retirement obligations because an estimation of necessary costs to dispose of them is not available due to the fact that the technology necessary to dismantle or dispose of them and the legislation on how they should be disposed of have been developed only partially. Those assets include the facilities conducting nuclear fuel manufacturing, research and development concerning the safety of the constituting materials of reactors and so on.

## 27 BUSINESS COMBINATION AND BUSINESS DIVESTITURE

### 1. Business Combination by Acquisition

(1) Outline of the business combination
a) Name of the acquired company and its business
Name of the acquired company: UniCarriers Holdings Corporation
Description of business: Development, manufacture and sale of material handling equipment, such as forklift trucks, container carriers and transfer cranes
b) Major reasons for the business combination
In today's forklift industry, amid intensifying global competition, scale expansion is becoming increasingly important for securing profitability. Scale expansion has also become indispensable in the realm of research and development, including new technologies, as the industry increasingly faces the need to respond to global environmental issues.

Through acquisition of UniCarriers, MHI and Mitsubishi Nichiyu Forklift Co., Ltd. will achieve a full lineup of product offerings giving them greater response capacity to customers' diverse needs. The move is also targeted at enhancing the companies' R&D capabilities and boosting their product competitiveness. Furthermore, through mutually complementary sales networks, MHI's and Mitsubishi Nichiyu Forklift's global expansion opportunities will be enhanced, thereby strengthening their business foundations and enabling expansion in business scale. In addition, by aggregating the cutting-edge innovative technologies of the MHI Group companies, the acquisition of Unicarriers is aimed at creating products of high added value and a business model transcending the conventional parameters of the logistics machinery and equipment industry.
c) Date of the business combination
March 31, 2016
d) Legal form of the business combination
Acquisition of shares in exchange for cash
e) Name of the acquired company after the business combination
Unchanged
f) Percentage of voting rights acquired
100%
Shareholding ratio of acquired shares (%):
Mitsubishi Heavy Industries Forklift & Engine Turbocharger Holdings, Ltd.: 65%
Mitsubishi Nichiyu Forklift Co., Ltd.: 35%
g) Major reason for the decision on acquiring the company
Due to the acquisition of shares in exchange for cash

(2) Period of operating results of the acquired company included in the consolidated financial statements
The operating results of the acquired company were not included in consolidated financial statements of the Group because it was acquired on March 31, 2016.

(3) Purchase price of the acquired company
115,672 million yen ($1,026,553 thousand) in cash

(4) Major acquisition-related costs and their amounts
Remuneration, fees, etc., to external advisors, etc.: 819 million yen ($7,268 thousand)

(5) Amount and the cause of the resulting goodwill and the applicable amortization method and period
a) Amount of the resulting goodwill
63,147 million yen ($560,410 thousand)
The amount of goodwill is calculated on a tentative basis as the purchase price allocation is not finalized.
b) Cause of the goodwill
The excess earnings potential for future periods is expected from the development of the acquired business going forward.
c) Method and term of amortization
To be amortized over a reasonable period on a straight-line basis, based on an estimation of the period over which the effect of the investment will be materialized.

(6) Amount and breakdown of assets acquired and liabilities assumed on the business combination date

| | |
|---|---|
| Current assets | 73,651 million yen ($653,629 thousand) |
| Non-current assets | 73,572 million yen ($652,928 thousand) |
| **Total assets** | 147,224 million yen ($1,306,567 thousand) |

| | |
|---|---|
| Current liabilities | 94,771 million yen ($841,063 thousand) |
| Non-current liabilities | 11,951 million yen ($106,061 thousand) |
| **Total liabilities** | 106,722 million yen ($947,124 thousand) |

(7) Purchase price allocation

As of the end of the fiscal year ended March 31, 2016, purchase price adjustments and the calculation of the fair value of assets and liabilities that are identifiable as of the business combination date have not been completed and the purchase price allocation has not been finalized. Therefore, the purchase price is allocated on a tentative basis based on reasonable information that is available as of the end of the fiscal year ended March 31, 2016.

(8) Estimation of the impact on consolidated statement of income assuming the business combination had been carried out on April 1, 2015

| | |
|---|---|
| Net sales | 196,210 million yen ($1,741 million) |
| Operating income | 5,993 million yen ($53 million) |

This impact estimation has not been audited by the independent auditors of the Group.

## 2. Business Divestiture

(1) Outline of the business divestiture

Mitsubishi Agricultural Machinery Co., Ltd., a former subsidiary company of MHI, formed a capital alliance with Mahindra & Mahindra Ltd. on October 1, 2015 by allocation of new stocks to a third party, mainly to strengthen domestic and international competitiveness. The company changed its name to Mitsubishi Mahindra Agricultural Machinery Co., Ltd. on the same date.

Due to this business divestiture, this company was reclassified from a consolidated subsidiary to an affiliated company accounted for by the equity method in the third quarter of the fiscal year ended March 31, 2016.

(2) Outline of the accounting procedures

The decrease in equity due to the third-party allocation was recognized as loss on sales of shares, and it was included in business structure improvement expenses.

(3) Name of reporting segment which included the separated business

Machinery, Equipment & Infrastructure

(4) Net sales and operating income related to the separated business recorded on the consolidated financial statements of the Group in the fiscal year ended March 31, 2016

| | |
|---|---|
| Net sales | 26,888 million yen ($238,622 thousand) |
| Operating income | 1,062 million yen ($9,424 thousand) |

(5) Outline of continuous engagement

The balance of the loan receivable from MHI to this affiliated company is 3,095 million yen ($27,467 thousand) as of March 31, 2016.

## 28 SIGNIFICANT AFFILIATES

Disclosure of condensed consolidated financial statements of significant affiliates under statutory criteria is required. Mitsubishi Motors Corporation was a significant affiliate in the fiscal year ended March 31, 2016.

| Mitsubishi Motors Corporation (As of and for the fiscal year ended March 31, 2016) | In millions of yen<br>2016 | In thousands of U.S. dollars<br>2016 |
|---|---|---|
| Total current assets | ¥ 914,183 | $ 8,113,090 |
| Total non-current assets | 519,541 | 4,610,764 |
| Total current liabilities | ¥ 622,731 | $ 5,526,544 |
| Total non-current liabilities | 109,137 | 968,556 |
| Total net assets | ¥ 701,856 | $ 6,228,753 |
| Net sales | ¥2,267,849 | $20,126,455 |
| Profit before income taxes | 125,346 | 1,112,406 |
| Profit | 94,326 | 837,113 |

## 29 SUBSEQUENT EVENTS

On April 20, 2016, Mitsubishi Motors Corporation ("MMC"), an equity-method affiliate of MHI, reported to the Japanese Ministry of Land, Infrastructure, Transport, and Tourism, that regarding the fuel consumption testing data, MMC conducted the testing improperly to present better fuel consumption rates than the actual rates. Related with this issue, subsequently MMC announced an amendment of its consolidated financial results for fiscal year 2015 and also its financial results forecast for fiscal year 2016. The impact of these announcements on MHI's financial results are as follows.

### 1. Impact on MHI's financial results for the fiscal year ended March 31, 2016

MMC announced its consolidated and non-consolidated financial results for fiscal year 2015 on April 27, 2016, reflecting a portion of the loss related to the improper conduct in fuel consumption testing. Furthermore, on May 25, 2016, MMC announced the amendments to its consolidated financial results due to the additional recording of such loss.

MHI's consolidated financial statements for fiscal year 2015 were prepared based on MMC's consolidated financial results announced on April 27, 2016, and an impact of the increase in such loss announced on May 25, 2016 was not reflected. As a result, assuming that MHI had reflected MMC's additional loss in MHI's income (loss) from equity method investments, "Ordinary income" and "Profit before income taxes" would have decreased by 2.1 billion yen ($0.018 billion). The amendments of MMC's financial results will be reflected in MHI's consolidated financial statements for the first quarter of fiscal year 2016.

### 2. Impact on MHI's financial results forecast for the fiscal year ending March 31, 2017

On June 17, 2016, besides the announcement of MMC's submission of additional investigation report regarding the past records of its sales, MMC also announced an extraordinary loss of approximately 50 billion yen ($0.443 billion) in its consolidated financial statements for fiscal year 2016 as the payments to its customers. Furthermore, on June 22, 2016, MMC disclosed that included the above mentioned 50 billion yen, MMC expects to record a total of 150 billion yen ($1.331 billion) of extraordinary loss related to the fuel consumption testing. The future impact (fiscal year 2016) of this extraordinary loss on MHI's financial position, operating results, and also cash flows is still under evaluation.

Additionally, the issuance of MMC's new shares to Nissan Motor Co., Ltd. ("Nissan") through a third-party allotment passed the resolutions at the MMC's board of directors meeting held on May 12, 2016, and on May 25, 2016, MMC and Nissan executed a basic agreement for a strategic alliance.

At this stage, it is difficult for MHI to make an appropriate estimation of the future impact (fiscal year 2016 and after) of the above matters on MHI's financial position, operating results, and also cash flows.

# INDEPENDENT AUDITOR'S REPORT

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## Independent Auditor's Report

The Board of Directors
Mitsubishi Heavy Industries, Ltd.

We have audited the accompanying consolidated financial statements of Mitsubishi Heavy Industries, Ltd. and its consolidated subsidiaries, which comprise the consolidated balance sheet as at March 31, 2016, and the consolidated statements of income, comprehensive income, changes in net assets, and cash flows for the year then ended and a summary of significant accounting policies and other explanatory information, all expressed in Japanese yen.

*Management's Responsibility for the Consolidated Financial Statements*

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in Japan, and for designing and operating such internal control as management determines is necessary to enable the preparation and fair presentation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error.

*Auditor's Responsibility*

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in Japan. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. The purpose of an audit of the consolidated financial statements is not to express an opinion on the effectiveness of the entity's internal control, but in making these risk assessments the auditor considers internal controls relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

*Opinion*

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Mitsubishi Heavy Industries, Ltd. and its consolidated subsidiaries as at March 31, 2016, and their consolidated financial performance and cash flows for the year then ended in conformity with accounting principles generally accepted in Japan.

*Emphasis of Matter*

1. We draw attention to Note 17 "LOSS ON PASSENGER VESSEL CONSTRUCTION BUSINESS RESERVE" to the Consolidated Financial Statements, which describes, the actual amount of future losses may be different from the current estimate mainly as Mitsubishi Heavy Industries, Ltd. ("MHI") is still negotiating the construction schedule for the second ship with the customer.
2. We draw attention to Note 13 "OTHERS" to the Consolidated Financial Statements, which describes, MHI demanded that Hitachi, Ltd. ("Hitachi") pay ZAR 48,200 million (equivalent to approximately 379,334 million yen ($3,366,471 thousand) converted at a rate of 7.87 yen to 1 ZAR) to MHPS-Africa as part of the price adjustment and other payments.

Meanwhile, MHI and Hitachi have not completed the price adjustment of the South African Asset Transfer at the moment.

Our opinion is not qualified in respect of these matters.

*Convenience Translation*

We have reviewed the translation of these consolidated financial statements into U.S. dollars, presented for the convenience of readers, and, in our opinion, the accompanying consolidated financial statements have been properly translated on the basis described in Note 4.

Ernst & Young ShinNihon LLC

June 23, 2016

MITSUBISHI HEAVY INDUSTRIES, LTD.

Our Technologies, Your Tomorrow

**K130-MRFS16E1-A-0,** (1.0)16-10, F

Printed in Japan