1. Basis of presenting consolidated financial statements

The accompanying consolidated financial statements of Kawasaki Heavy Industries, Ltd. (the "Company") and its consolidated subsidiaries (together the "Companies") have been prepared from the financial statements filed with the Prime Minister as required by the Financial Instruments and Exchange Act in Japan and in accordance with accounting principles generally accepted in Japan ("Japanese GAAP"), which are different in certain respects as to the application and disclosure requirements from International Financial Reporting Standards. Certain reclassifications have been made in the accompanying consolidated financial statements to facilitate understanding by readers outside Japan. In addition, certain reclassifications have been made in the 2020 consolidated financial statements to conform to the classification used in 2021. The Company and its subsidiaries adopted ASBJ Statement No. 31 "Accounting Standard for Disclosure of Accounting Estimates" (March 31, 2020) to the consolidated financial statements for the current consolidated fiscal year, and therefore significant accounting estimates are disclosed in the note to the consolidated financial-statements. The note does not include information for the prior consolidated fiscal year in accordance with the transitional provision set out in paragraph 11 of the Accounting Standard.

The translations of the Japanese yen amounts into U.S. dollar amounts are included solely for the convenience of readers outside Japan, using the prevailing exchange rate at March 31, 2021, which was ¥110.72 to U.S.$1.00. The translations should not be construed as representations that the Japanese yen amounts have been, could have been or could in the future be converted into U.S. dollars at this or any other rate of exchange. As permitted, fractional amounts have not been adjusted.

2. Significant accounting policies

(a) Principles of consolidation

The accompanying consolidated financial statements include the accounts of the Company and significant companies over which the Company has power of control through majority voting rights or the existence of certain other conditions evidencing control. The consolidated financial statements include the accounts of the Company and 99 subsidiaries (96 in the year ended March 31, 2020). The aggregate amount of total assets, net sales, profit and retained earnings of the excluded subsidiaries would not have had a material effect on the consolidated financial statements if they had been included in the consolidation.

(b) Application of the equity method of accounting

Investments in non-consolidated subsidiaries and affiliates over which the Company has the ability to exercise significant influence over operating and financial policies are accounted for by the equity method. For the year ended March 31, 2021, 19 affiliates (17 in 2020) were accounted for by the equity method. For the year ended March 31, 2021, investments in 11 affiliates (11 in 2020) were stated at cost without applying the equity method of accounting. If the equity method had been applied for these investments, the profit and retained earnings of these excluded subsidiaries and affiliates would not have had a material effect on the consolidated financial statements.

(c) Consolidated subsidiaries' fiscal year-end

For the year ended March 31, 2021, the fiscal year-end of 24 consolidated subsidiaries (30 in 2020) was December 31. These subsidiaries were consolidated as of December 31, and significant transactions for the period between December 31 and March 31, the Company's fiscal year-end, were adjusted for on consolidation.

Effective from the fiscal year ended March 31, 2021, 6 companies of Kawasaki Precision Machinery (Suzhou) Ltd., Kawasaki Precision Machinery Trading (Shanghai) Co., Ltd., Kawasaki Robotics (Tianjin) Co., Ltd., Kawasaki Chunhui Precision Machinery (Zhejiang) Ltd., Kawasaki Robotics (Kunshan) Co., Ltd. and Kawasaki Robotics Korea, Ltd., which previously had December 31 as their fiscal year-end, changed their fiscal year-end to March 31 or changed to a method of having provisional settlement on March 31, which is the consolidated fiscal year-end, in accordance with the final settlement and consolidating it. Accordingly, in the fiscal year ended March 31, 2021, the Company consolidated the financial statements of these consolidated subsidiaries for the 15-month period from January 1, 2020 to March 31, 2021, and the effect of the change in the fiscal year-end was adjusted for on the consolidated statements of profit and loss. These consolidated subsidiaries whose fiscal year-ends were changed recorded net sales of ¥13,522 million ($122,128 thousand), operating profit of ¥1,976 million ($17,847 thousand), ordinary profit of ¥2,447 million ($22,101 thousand) and Profit before income taxes of ¥2,447 million ($22,101 thousand) from January 1, 2021 to March 31, 2021.

(d) Foreign currency translations

Receivables and payables denominated in foreign currencies are translated into Japanese yen at year-end rates. The balance sheets of the consolidated overseas subsidiaries are translated into Japanese yen at year-end rates, except for shareholders' equity accounts, which are translated at historical rates. The income statements of the consolidated overseas subsidiaries are translated at average rates. The Company and its domestic subsidiaries report foreign currency translation adjustments in net assets.

(e) Revenue recognition

<Sales of products and construction contracts>

The percentage-of-completion method is applied to construction contracts if the outcome of the construction activity is deemed certain during the period of the activity. Otherwise, the completed contract method is applied.

(f) Cash and cash equivalents

Cash on hand, readily available deposits and short-term highly liquid and low risk investments with maturities not exceeding three months at the time of purchase are considered to be cash and cash equivalents in preparing the consolidated statements of cash flows.

(g) Allowance for doubtful receivables

An allowance for possible losses from notes and accounts receivable, loans and other receivables is provided based on past experience and the Companies' estimates of losses on collection.

(h) Assets and liabilities arising from derivative transactions

Assets and liabilities arising from derivative transactions are stated at fair value.

(i) Inventories

Inventories are stated mainly at historical cost computed using the specific identification cost method, the moving average cost method or the first-in, first-out method. The ending balance of inventories is measured at the lower of cost or market.

(j) Investment securities

The Company and its consolidated subsidiaries classify securities as (a) debt securities intended to be held to maturity (hereafter, "held-to-maturity debt securities"), (b) equity securities issued by subsidiaries and affiliated companies and (c) all other securities (hereafter, "available-for-sale securities"). There were no trading securities at March 31, 2021 or 2020. Held-to-maturity debt securities are stated mainly at amortized cost. Equity securities issued by subsidiaries and affiliated companies which are not consolidated or accounted for using the equity method are stated at moving average cost. Available-for-sale securities with available fair market values are stated at fair market value. Unrealized gains and unrealized losses on these securities are reported, net of applicable income taxes, as a separate component of net assets. Realized gains and losses on the sale of such securities are computed using moving average cost. Other securities with no available market value are stated at moving average cost.

If the market value of held-to-maturity debt securities, equity securities issued by non-consolidated subsidiaries or affiliated companies or available-for-sale securities declines significantly, such securities are stated at market value, and the difference between the market value and the carrying amount is recognized as loss in the period of the decline. If the market value of equity securities issued by a non-consolidated subsidiary or affiliated company not subject to the equity method is not readily available, the securities should be written down to net asset value with a corresponding charge in the statements of income in the event the net asset value declines significantly. In these cases, the market value or the net asset value will be the carrying amount of the securities at the beginning of the next year.

(k) Property, plant and equipment
Property, plant and equipment are stated at cost. Depreciation is computed mainly by the straight-line method over the estimated useful life of the asset.

(l) Intangible assets
Amortization of intangible assets, including software for the Company's own use, is computed by the straight-line method over the estimated useful life of the asset.

An equivalent amount of goodwill is amortized by the straight-line method over the period the Company benefits from its use. If the amount is not significant, it is expensed when incurred.

(m) Provision for bonuses
Accrued bonuses for employees are provided for based on the estimated amount of payment.

(n) Provision for construction warranties
The provision for construction warranties is based on past experience or provided separately when it can be reasonably estimated.

(o) Provision for loss on construction contracts
A provision for loss on construction contracts at the fiscal year-end is made when substantial loss is anticipated for the next fiscal year and beyond and such loss can be reasonably estimated.

(p) Provision for the in-service issues of commercial aircraft jet engines
Of the costs related to the significant in-service issues of commercial aircraft jet engines that arose in the Rolls-Royce Trent 1000 engine program, in which the Company participates as a risk and revenue sharing partner, the Company has made a provision for the abnormal costs related to the in-service issues which the Company would cover as a member of this program.

(q) Provision for sales promotion expenses
With regard to dealer inventories at the fiscal year-end, a provision is made for sales rebates etc., expected to be paid in the next fiscal year and beyond based on past experience or on separate estimates when this can be reasonably estimated.

(r) Retirement benefit liability
Employees who terminate their services with the Company or some consolidated domestic subsidiaries are generally entitled to lump-sum payments, the amounts of which are determined by reference to basic rates of pay at the time of termination and length of service.

The liabilities and expenses for retirement and severance benefits are determined based on amounts actuarially calculated using certain assumptions. The Company and its consolidated domestic subsidiaries provide the allowance for employees' retirement and severance benefits based on the estimated amounts of projected benefit obligation and the fair value of plan assets, including assets in the retirement benefit trust.

Actuarial gains and losses and prior service costs are charged to income on a straight-line basis primarily over 10 years commencing with the following period and the current period, respectively. With regard to previously unrecognized actuarial gains and losses and unrecognized prior services costs, after adjusting for tax effects, the Company records any accumulated adjustment for retirement benefits as part of accumulated other comprehensive income within net assets.

In calculating retirement benefit obligations, the Company uses a benefit formula basis to attribute expected benefits to periods of service.

Employees of the Company's overseas consolidated subsidiaries are generally covered by various pension plans accounted for in accordance with generally accepted accounting principles in the respective country of domicile.

(s) Hedge accounting
The Company and its consolidated subsidiaries employ deferred hedge accounting. If derivative financial instruments are used as hedges and meet certain hedging criteria, the Company and its consolidated subsidiaries defer recognition of gain or loss resulting from a change in the fair value of the derivative financial instrument until the related loss or gain on the hedged item is recognized.

(t) Finance leases
Lease assets under finance leases that transfer ownership of the lease assets to the lessee are amortized by the same method as that used for property, plant and equipment and intangible assets. Lease assets under finance leases that do not transfer ownership of the lease assets to the lessee are amortized by the straight-line-method over the lease term with zero residual value.

(u) Accounting for consumption taxes
National and local consumption taxes are accounted for based on the net amount.

(v) Application of consolidated tax reporting
The Company and its wholly owned consolidated domestic subsidiaries file a consolidated tax return.

(w) Application of tax effect accounting for the transition from the consolidated taxation system to the group tax sharing system
With respect to the transition to the group tax sharing system established under the Act for Partial Amendment of the Income Tax Act, etc. (Act No. 8 of 2020) and the revision of the nonconsolidated taxation system in conjunction with the transition to the group tax sharing system, due to the treatment prescribed in Paragraph 3 of the Practical Solution on the Treatment of Tax Effect Accounting for the Transition from the Consolidated Taxation System to the Group Tax Sharing System (PITF No. 39, March 31, 2020), the Company and some of its consolidated subsidiaries have not adopted the provisions of Paragraph 44 of the Implementation Guidance on Tax Effect Accounting (ASBJ Guidance No. 28, February 16, 2018), and the amount of deferred tax assets and deferred tax liabilities are based on the provisions of pre-amended tax legislation.

3. Significant accounting estimates

Recoverability of deferred tax assets

(a) The ending balance of deferred tax assets recorded in the consolidated financial statements as of March 31, 2021
Deferred tax assets ¥70,452 million ($636,308 thousand)

(b) Information on the content of significant accounting estimates for identified items
(i) Calculation method of estimates
Deferred tax assets are examined for recoverability based on the generation of taxable income and tax planning in certain future periods based on business plans.

(ii) Major assumptions used in calculating estimates

Forecasts of net sales and profits, which are the main elements of the business plan, are based on certain assumptions about future changes in economic conditions and other factors. In addition, the COVID-19 pandemic has had a widespread impact on the business plan for year ended March 31, 2021. Accordingly, the accounting estimates are made on the following assumptions for each business.

- In the Aerospace Systems business, passenger demand has been stagnant globally. Although the demand will gradually recover due to the deregulation of travel regulations, it will take a considerable period of time for a full recovery.
- In other businesses, sales of hydraulic equipment for the Chinese construction machinery market in the precision machinery and robots business, robots for semiconductors, and motorcycles and engines business in developed countries have already recovered to the level before the spread of the COVID-19 pandemic. However while stable demand is expected in the future, it will take time for the recovery in demand of other products.

(iii) Effect on the consolidated financial statements for the following year

Future estimates are affected by future changes in economic conditions, the conditions related to the COVID-19 pandemic and other factors. Although the Company reasonably estimates recoverability, changes in the terms of these estimates for the future could have a significant impact on the amount of deferred tax assets in the consolidated financial statements for subsequent fiscal years.

4.

Accounting standards issued but not yet adopted

The following guidance was issued but not yet adopted.

1. The Company and its affiliated companies

- "Accounting Standard for Revenue Recognition" (ASBJ Statement No. 29, March 31, 2020)
- "Implementation Guidance on Accounting Standard for Revenue Recognition" (ASBJ Guidance No. 30, March 26, 2021)

(a) Overview

This is the comprehensive accounting standard for revenue recognition. Revenue is recognized by applying the following five-step approach outlined in the accounting standard.

(i) Identify the contract with the customers

(ii) Identify the performance obligations in the contract

(iii) Determine the transaction price

(iv) Allocate the transaction price to the performance obligations in the contract

(v) Recognize revenue when or as the company satisfies a performance obligations

(b) Effective date

Effective from the beginning of the fiscal year ending March 31, 2022.

(c) Effects of application of the standards

The Company and its consolidated subsidiaries are currently in the process of determining the effect of "Accounting Standard for Revenue Recognition"on the consolidated financial statements.

- "Accounting Standard for Fair Value Measurement" (ASBJ Statement No. 30, July 4, 2019)
- "Implementation Guidance on Accounting Standard for Fair Value Measurement" (ASBJ Guidance No. 31, July 4, 2019)
- "Accounting Standard for Measurement of Inventories" (ASBJ Statement No. 9, July 4, 2019)
- "Accounting Standard for Financial Instruments" (ASBJ Statement No. 10, July 4, 2019)
- "Implementation Guidance on Disclosures about Fair Value of Financial Instruments" (ASBJ Guidance No. 19, March 31, 2020)

(a) Overview

The "Accounting Standard for Fair Value Measurement" and "Implementation Guidance on Accounting Standard for Fair Value Measurement" (hereinafter "Fair Value Measurement Accounting Standard, etc.") were developed to improve comparability with international accounting standards, and implementation guidance and related standards for fair value measurement have been established under them. The "Fair Value Measurement Accounting Standard, etc." apply to the fair value of the following items:

- Financial instruments specified in the "Accounting Standard for Financial Instruments"
- Inventories held for trading purposes as prescribed in "Accounting Standard for Measurement of Inventories"

Moreover, "Implementation Guidance on Disclosures about Fair Value of Financial Instruments" has been revised and now stipulates the inclusion of explanatory notes providing breakdowns, etc., for each level of fair value of financial instruments.

(b) Effective Date

Scheduled to be applied from the beginning of the fiscal year ending March 31, 2022

(c) Effects of application of the standards

The Company is currently in the process of determining the effects of the application of "Accounting Standard for Fair Value Measurement", etc." on the consolidated financial statements.

2. Subsidiaries and affiliated companies in the United States

- Topic 842 "Leases"

(a) Overview

These accounting standards require a lessee to recognize assets and liabilities generally for all leases on the balance sheet, whereas no significant changes were made in the accounting for a lessor.

(b) Effective date

Scheduled to be applied from the beginning of the fiscal year ending March 31, 2023.

(c) Effects of application of the standards

The Company is currently in the process of determining the effects of the application of Topic 842 "Leases" on the consolidated financial statements.

5.

Work in process

A trust was established for the Company's accounts receivable - trade generated in selling certain work in process using a self-settled trust. The Company has a beneficiary interest in the accounts receivable – trade as trust assets. The work in process related to the trust assets as of March 31, 2020 amounted to ¥4,479 million.

6.

Accumulated depreciation of property, plant and equipment

Accumulated depreciation of property, plant and equipment as of March 31, 2021 and 2020 was as follows:

	Millions of yen		Thousands of U.S. dollars
	2021	2020	**2021**
Accumulated depreciation of property, plant and equipment	**¥891,135**	¥872,337	**$8,048,546**

7.

Securities

(a) Acquisition costs and book values (market values) of available-for-sale securities with available market values as of March 31, 2021 and 2020 were as follows:

	2021			
	Millions of yen			Thousands of U.S. dollars
	Book value	Acquisition cost	Unrealized gains (losses)	Unrealized gains (losses)
Securities with book values exceeding acquisition costs:				
Equity securities	**¥5,248**	**¥1,982**	**¥3,265**	**$29,489**
Other securities:				
Equity securities	**317**	**390**	**(73)**	**(659)**
Total	**¥5,566**	**¥2,373**	**¥3,191**	**$28,820**

	2020		
	Millions of yen		
	Book value	Acquisition cost	Unrealized gains (losses)
Securities with book values exceeding acquisition costs:			
Equity securities	¥4,898	¥1,975	¥2,922
Other securities:			
Equity securities	840	1,145	(304)
Total	¥5,738	¥3,120	¥2,617

(b) Sales amounts of available-for-sale securities and related realized gains and losses for the years ended March 31, 2021 and 2020 were as follows:

	2021					
	Millions of yen			Thousands of U.S. dollars		
	Sales amounts	Gains	Losses	Sales amounts	Gains	Losses
Equity securities:	**¥1,396**	**¥776**	**¥(4)**	**$12,608**	**$7,009**	**$(36)**

	2020		
	Millions of yen		
	Sales amounts	Gains	Losses
Equity securities:	¥1,075	¥552	¥(14)

(c) Investment securities subject to impairment

In the fiscal year ended March 31, 2021, the Company recognized the impairment losses of ¥1,444 million ($13,042 thousand) on investments in securities, which is on shares of subsidiaries and associates of ¥1,444 million ($13,042 thousand).

Impairment losses on investment securities are recognized when there has been a significant decline in the market value. Investment securities for which the market value as of the end of the fiscal year has fallen to below 50% of the acquisition costs are deemed to have no recovery potential and to be impaired. Investment securities for which the market value has fallen to between 30% and 50% of the acquisition costs are deemed to be partially impaired by an amount that takes into consideration the likelihood of recovery and other factors.

8.

Investments in non-consolidated subsidiaries and affiliates

Investments in non-consolidated subsidiaries and affiliates as of March 31, 2021 and 2020 were ¥80,843 million ($730,157 thousand) and ¥79,495 million, respectively.

9.

Claim for damages in overseas LNG tank construction work

The Company sustained losses (approximately ¥51 billion ($460,621 thousand)) due to breach of contract by an overseas construction subcontractor in connection with a certain overseas liquefied natural gas (LNG) tank construction project. The Company has filed a petition for arbitration on this matter with the International Chamber of Commerce (ICC). The Company plans to settle this matter through the arbitration process, and the expected amount recoverable through the arbitration process has been recorded in "Other" under "Investments and other assets."

10.

Uncollected amount relating to gas-fired power generation facility project in Japan

Year ended March 31, 2021

With regard to the gas-fired power generation facility in Japan constructed by the Company but not yet delivered, the client has informed the Company that they are unable to honor their payment as a result of credit insecurity. On the consolidated balance sheet, assets related to this project are recorded in both trade receivables and work in process. The outstanding unpaid amount due to the Company is approximately ¥20 billion ($180,636 thousand), and negotiations aimed at collecting the unpaid amount are under way, including negotiations on a possible sale of the facility to a third party.

Year ended March 31, 2020

In the fiscal year ended March 31, 2020 and with regard to the gas-fired power generation facility in Japan constructed by the Company but not yet delivered, the client has informed the Company that they are unable to honor their payment as a result of credit insecurity. On the consolidated balance sheet, assets related to this project are recorded in both trade receivables and work in process. The outstanding unpaid amount due to the Company is approximately ¥20 billion, and negotiations aimed at collecting the unpaid amount are under way, including negotiations on a possible sale of the facility to a third party.

11.

Short-term debt and long-term debt

Short-term debt and long-term debt as of March 31, 2021 and 2020 comprised the following:

	Millions of yen		Thousands of U.S. dollars
	2021	2020	**2021**
Short-term debt:			
Short-term borrowings, principally bank loans, bearing average interest rates of 0.61% and 0.68% as of March 31, 2021 and 2020, respectively	**¥124,577**	¥143,741	**$1,125,154**
Current portion of long-term borrowings, bearing average interest rates of 0.76% and 0.68% as of March 31, 2021 and 2020, respectively	**17,001**	22,446	**153,549**
Current portion of bonds payable, bearing average interest rates of 0.66% and 0.66% as of March 31, 2021 and 2020, respectively.	**30,000**	20,000	**270,954**
Lease obligations, current	**1,061**	1,542	**9,583**
Total short-term debt	**¥172,640**	¥187,730	**$1,559,249**
Long-term debt:			
Loans from banks and other financial institutions, partly secured by mortgage or other collateral, due from 2021 to 2030, bearing average interest rates of 0.44% and 0.45% as of March 31, 2021 and 2020, respectively.	**¥216,179**	¥211,306	**$1,952,484**
Notes and bonds issued by the Company:			
0.32–0.99% notes due in 2020	**–**	20,000	**–**
0.10–1.42% notes due in 2021	**30,000**	30,000	**270,954**
0.15-1.10% notes due in 2022	**20,000**	20,000	**180,636**
0.06-0.99% notes due in 2023	**40,000**	20,000	**361,272**
0.15-0.79% notes due in 2024	**30,000**	30,000	**270,954**
0.26-0.85% notes due in 2025	**40,000**	10,000	**361,272**
0.40% notes due in 2028	**10,000**	10,000	**90,318**
0.48% notes due in 2030	**10,000**	–	**90,318**
0.82% notes due in 2036	**10,000**	10,000	**90,318**
0.90% notes due in 2037	**10,000**	10,000	**90,318**
0.70-0.82% notes due in 2039	**20,000**	20,000	**180,636**
Long-term lease obligations	**10,594**	2,416	**95,683**
	446,773	393,722	**4,035,161**
Less portion due within one year	**(48,063)**	(43,989)	**(434,095)**
Total long-term debt	**¥398,709**	¥349,733	**$3,601,057**

As of March 31, 2021 and 2020, the following assets were pledged as collateral for short-term debt and long-term debt:

	Millions of yen		Thousands of U.S. dollars
	2021	2020	**2021**
Buildings and structures	**¥ –**	¥ 82	**$ –**
Investment securities	**39**	47	**352**
Other	**80**	80	**723**
Total	**¥119**	¥209	**$1,075**

As of March 31, 2021 and 2020, debt secured by the above pledged assets was as follows:

	Millions of yen		Thousands of U.S. dollars
	2021	2020	**2021**
Notes and accounts payable–trade	**¥ 5**	¥ 3	**$45**
Short-term borrowings and long-term borrowings	**–**	10	**–**
Total	**¥ 5**	¥14	**$45**

The aggregate annual maturities of long-term debt as of March 31, 2021 were as follows:

	Millions of yen	Thousands of U.S. dollars
Year ending March 31		
2022	**¥ 48,063**	**$ 434,095**
2023	**41,486**	**374,693**
2024	**63,848**	**576,662**
2025	**59,773**	**539,857**
2026 and thereafter	**233,600**	**2,109,827**
Total	**¥446,773**	**$4,035,161**

12.

Provision for losses on construction contracts

Inventories for construction contracts with substantial anticipated loss and the provision for loss on construction contracts were not offset. As of March 31, 2021 and 2020, the inventories for the construction contracts for which the provision for loss on construction contracts was provided were ¥10,107 million ($91,284 thousand) and ¥9,313 million, respectively. These amounts were all included in work in process.

13.

Employees' retirement and severance benefits

1. Summary of retirement benefit plans adopted

The Company and its consolidated subsidiaries have severance lump-sum payment plans, defined benefit corporate pension plan, and cash balance plans (pension plans linked to market interest rates) as defined benefit plans and defined contribution pension plan as defined contribution plan. The Company has an employees' retirement benefit trust. Some consolidated subsidiaries apply a simple method including a method, in which an estimated amount required to be paid for voluntary retirement benefits at the end of the fiscal year is deemed as the retirement benefit obligations in the calculations of retirement benefit liability and retirement benefit expenses.

2. Defined benefit plans (including plans that apply a simplified method)

(1) Reconciliation of beginning-of-period and end-of-period balances of retirement benefit obligations

	Millions of yen		Thousands of U.S. dollars
	2021	2020	**2021**
Balance of retirement benefit obligations at beginning of period	**¥217,954**	¥201,484	**$1,968,515**
Service cost	**12,197**	12,034	**110,161**
Interest cost	**1,510**	1,815	**13,638**
Actuarial gains and losses	**(6,174)**	8,449	**(55,762)**
Retirement benefits paid	**(5,050)**	(5,060)	**(45,611)**
Prior service cost	**(3,575)**	(1,907)	**(32,289)**
Other (foreign currency translation difference, etc.)	**2,171**	1,137	**19,608**
Balance of retirement benefit obligations at end of period	**¥219,033**	¥217,954	**$1,978,260**

(2) Reconciliation of beginning-of-period and end-of-period balances of plan assets

	Millions of yen		Thousands of U.S. dollars
	2021	2020	2021
Balance of plan assets at beginning of period	¥ 88,243	¥103,976	$796,992
Expected return on plan assets	1,395	1,239	12,599
Actuarial gains and losses	13,771	(15,412)	124,377
Contributions paid by the employer	4,058	3,879	36,651
Retirement benefits paid	(3,528)	(4,482)	(31,864)
Other (foreign currency translation difference, etc.)	(207)	(957)	(1,870)
Balance of plan assets at end of period	¥103,732	¥ 88,243	$936,886

(3) Reconciliation between end-of-period balance of retirement benefit obligations and plan assets to liabilities and retirement benefit liability and retirement benefit asset presented on the consolidated balance sheets

	Millions of yen		Thousands of U.S. dollars
	2021	2020	2021
Retirement benefit obligations on funded plan	¥185,834	¥192,953	$1,678,414
Plan assets	(103,732)	(88,243)	(936,886)
	82,101	104,710	741,519
Retirement benefit obligations on unfunded plan	33,199	25,000	299,846
Net amount of liabilities and assets presented on the consolidated balance sheets	115,300	129,710	1,041,366
Retirement benefit liability	115,456	129,846	1,042,775
Retirement benefit asset	(155)	(135)	(1,400)
Net amount of liabilities and assets presented on the consolidated balance sheets	¥115,300	¥129,710	$1,041,366

(4) Breakdown of retirement benefit expense

	Millions of yen		Thousands of U.S. dollars
	2021	2020	2021
Service cost	¥12,197	¥12,034	$110,161
Interest cost	1,510	1,815	13,638
Expected return on plan assets	(1,395)	(1,239)	(12,599)
Amortization of actuarial gains and losses	4,015	275	36,263
Amortization of prior service costs	238	191	2,150
Retirement benefit expense related to defined benefit plan	¥16,566	¥13,077	$149,621

(5) Adjustments for retirement benefits

Adjustments for retirement benefits (before tax effects) comprised the following:

	Millions of yen		Thousands of U.S. dollars
	2021	2020	2021
Prior service cost	¥ 3,813	¥ 2,099	$ 34,438
Actuarial gains and losses	23,961	(23,586)	216,411
Total	¥27,775	¥(21,487)	$250,858

(6) Accumulated adjustments for retirement benefits

Accumulated adjustments for retirement benefits (before tax effects) comprised the following:

	Millions of yen		Thousands of U.S. dollars
	2021	2020	2021
Unrecognized prior service cost	¥ 4,430	¥ 616	$ 40,011
Unrecognized actuarial gains and losses	(5,604)	(29,566)	(50,614)
Total	¥(1,174)	¥(28,949)	$(10,603)

(7) Plan assets

(i) Main breakdown of plan assets

The breakdown of main asset categories as a percentage of total plan assets is as follows:

	2021	2020
Bonds	21%	24%
Equities	55%	55%
Cash and deposits	5%	3%
Others	19%	18%
Total	100%	100%

Note: As of March 31, 2021 and 2020, the employees' retirement benefit trust established as part of the retirement benefit plan is included in the plan assets and represented a 47% and 46% portion of the plan assets, respectively.

(ii) Method for setting long-term expected rate of return

To determine the expected rate of return on plan assets, the Company takes into account the current and expected allocation of plan assets and the expected present and future long-term rate of return on the diverse range of assets that makes up the plan assets.

(8) Underlying actuarial assumptions

The main underlying actuarial assumptions as of March 31, 2021 and 2020, respectively, were as follows:

	2021	2020
Discount rate	0.42-3.01%	0.31–3.02%
Long-term expected rate of return on plan assets	0.00-5.50%	0.00–5.50%
Rate of compensation increase	6.10-6.60%	6.10–6.50%

3. Defined contribution plan

As of March 31, 2021 and 2020, the required contribution by the Company and its consolidated subsidiaries to the defined contribution plan was ¥2,597 million ($23,456 thousand) and ¥2,034 million, respectively.

14.

Provision for the in-service issues of commercial aircraft jet engines

The Company participates as a risk and revenue sharing partner on the Rolls-Royce Trent 1000 engine program, which has been impacted by the challenge of managing significant in-service issues. Rolls-Royce continues to work hard to remedy this situation. The Company has made a provision of the cost related to in-service issues which the Company would cover as a member of this program.

15.

Contingent liabilities

Contingent liabilities as of March 31, 2021 and 2020 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2021	2020	**2021**
As guarantor of indebtedness of employees, non-consolidated subsidiaries, affiliates and others	**¥24,086**	¥22,515	**$217,540**

16.

Net assets

Under the Japanese Corporate Law ("the Law"), the entire amount paid for new shares is required to be designated as common stock. However, a company may, by a resolution of the Board of Directors, designate an amount not exceeding one half of the price of the new shares as capital reserve, which is included in capital surplus. Under the Law, if a dividend distribution of surplus is made, the smaller of an amount equal to 10% of the dividend or the excess, if any, of 25% of common stock over the total of capital reserve and legal earnings reserve must be set aside as capital reserve or legal earnings reserve. Legal earnings reserve is included in retained earnings in the accompanying consolidated balance sheets. Under the Law, legal earnings reserve and capital reserve can be used to eliminate or reduce a deficit or capitalized by a resolution of the shareholders' meeting.

Capital reserve and legal earnings reserve may not be distributed as dividends. Under the Law, all capital reserve and all legal earnings reserve may be transferred to other capital surplus and retained earnings, respectively, which are potentially available for dividends.

The maximum amount that the Company can distribute as dividends is calculated based on the non-consolidated financial statements of the Company in accordance with the Law.

17.

Cost of sales

The ending balance of inventories was measured at the lower of cost or market. Loss on the valuation of inventories included in the cost of sales for the year ended March 31, 2021 was ¥3,379 million ($30,518 thousand). Gain on the valuation of inventories included in the cost of sales for the years ended March 31, 2020 was ¥1,941 million.

Provision for loss on construction contracts included in the cost of sales for the years ended March 31, 2021 and 2020 was ¥12,209 million ($110,269 thousand) and ¥8,563 million, respectively.

18.

Research and development expenses

Research and development expenses included in selling, general and administrative expenses were as follows:

	Millions of yen		Thousands of U.S. dollars
	2021	2020	**2021**
Research and development expenses	**¥44,949**	¥52,608	**$405,970**

19.

Payments/Reversal of the provision for the in-service issues of commercial aircraft jet engines

The Company participates as a risk and revenue sharing partner on the Rolls-Royce Trent 1000 engine program, which has been impacted by the challenge of managing significant in-service issues. Rolls-Royce continues to work hard to remedy this situation. The Company has made a provision of the cost related to in-service issues which the Company would cover as a member of this program. The provision was included within the non-operating expenses. The reversal of the provision was included within the non-operating income.

20.

Gain on sale of non-current assets

Fiscal year ended March 31, 2021
Gain on sales of non-current assets for the fiscal year ended March 31, 2021 was due to the sale of dormitories and company housing of the Company and its subsidiary.

Fiscal year ended March 31, 2020
Gain on sales of non-current assets for the fiscal year ended March 31, 2020 was due to the sale of former dormitory/ company housing sites.

21.

Gain on sale of shares of subsidiaries and associates

Gain on sale of shares of subsidiaries and associates for the fiscal year ended March 31, 2021 was due to the sale of shares of affiliates of subsidiaries.

22.

Loss on withdrawal from business

Loss on withdrawal from business for the fiscal year ended March 31, 2020 was due to the withdrawal from certain businesses by the Energy System & Plant Engineering Company.

23.

Impairment losses

(a) Groups of assets for which the Company and its consolidated subsidiaries recognized impairment losses

Year ended March 31, 2021

Location	Use	Type of assets	Millions of yen Amount	Thousands of U.S. dollars	Value of assets
Sakaide City, Kagawa,Japan	Business assets	Buildings and structures	¥ 885	$ 7,993	Net realizable value
		Machinery, equipment and vehicles	2,647	23,907	
		Other	544	4,913	
Hyogo Ward, Kobe City,etc	Business assets	Buildings and structures	¥ 5,978	$ 53,992	Value in use
		Machinery, equipment and vehicles	4,082	36,868	
		Other	1,068	9,646	
Total			¥15,205	$137,328	

Year ended March 31, 2020
Not applicable.

(b) Method of grouping assets
Assets are grouped mainly by units of business, and important assets for lease and idle assets are treated as individual asset groups.

(c) Reasons for recognition of impairment losses

Due to a deterioration in business profit and loss, the Company reduced the book value of certain assets to the recoverable amount.

(d) Methods used to determine recoverable amounts

The recoverable amounts were determined by the net realizable value or value in use. Net realizable value is mainly based on real estate appraisals, and those that are difficult to sell or convert to other are stated at memorandum values. Value in use is calculated by discounting future cash flows at a discount rate of 5.5%

24.

Consolidated statement of comprehensive income

Amounts reclassified to profit (loss) in the current period that were recognized in other comprehensive income in the current or previous periods and the tax effects for each component of other comprehensive income were as follows:

	Millions of yen		Thousands of U.S. dollars
	2021	2020	2021
Unrealized gains (losses) on securities			
Increase (decrease) during the year	¥ 1,135	¥ (887)	$10,251
Reclassification adjustments	(590)	(546)	(5,329)
Subtotal, before tax	544	(1,433)	4,913
Tax (expense) or benefit	(118)	368	(1,066)
Subtotal, net of tax	426	(1,065)	3,848
Deferred gains or losses on hedges			
Increase (decrease) during the year	58	(2,594)	524
Reclassification adjustments	(453)	2,556	(4,091)
Subtotal, before tax	(395)	(38)	(3,568)
Tax (expense) or benefit	110	16	993
Subtotal, net of tax	(284)	(21)	(2,565)
Foreign currency translation adjustments			
Increase (decrease) during the year	6,794	(5,284)	61,362
Reclassification adjustments	(66)	–	(596)
Subtotal, before tax	6,727	(5,284)	60,757
Tax (expense) or benefit	–	–	–
Subtotal, net of tax	6,727	(5,284)	60,757
Remeasurements of defined benefit plans			
Increase (decrease) during the year	23,521	(21,954)	212,437
Reclassification adjustments	4,254	467	38,421
Subtotal, before tax	27,775	(21,487)	250,858
Tax (expense) or benefit	(8,805)	6,469	(79,525)
Subtotal, net of tax	18,969	(15,017)	171,324
Share of other comprehensive income of entities accounted for using equity method			
Increase (decrease) during the year	4,496	(1,936)	40,607
Total other comprehensive income	¥30,335	¥(23,326)	$273,979

25.

Dividends

(a) Dividends paid

Year ended March 31, 2021

Not applicable.

Year ended March 31, 2020

Resolution	Kind of shares	Total amount of dividends paid	Dividends per share	Date of record	Effective date
June 26, 2019 General Meeting of Shareholders	Common stock	¥5,846 million	¥35.0	March 31, 2019	June 27, 2019
October 31, 2019 Board of Directors Meeting	Common stock	¥5,846 million	¥35.0	September 30, 2019	December 2, 2019

(b) Dividend payments for which the record date is in the subject fiscal year but the effective date is in the succeeding consolidated fiscal year

Year ended March 31, 2021

Not applicable.

Year ended March 31, 2020

Not applicable.

26.

Income taxes

Income taxes in Japan applicable to the Company and its consolidated domestic subsidiaries consist of corporate tax (national tax) and enterprise and inhabitants' taxes (local taxes), which, in the aggregate, resulted in a statutory tax rate of approximately 30.5% for the years ended March 31, 2021 and 2020.

(a) The significant differences between the statutory and effective tax rates for the years ended March 31, 2021 and 2020 were as follows:

	2021	2020
Statutory tax rate	–	30.5%
Valuation reserve	–	19.7
Equity in income of non-consolidated subsidiaries and affiliates	–	(1.0)
Tax credit for research and development expenses	–	(1.9)
Elimination of unrealized profits	–	0.3
Retained earnings for foreign subsidiaries	–	0.2
Other	–	0.7
Effective tax rate	–	48.4%

The statutory and effective tax rates are omitted because loss before income taxes is recorded for the fiscal year ended March 31,2021.

(b) Significant components of deferred tax assets and liabilities as of March 31, 2021 and 2020 were as follows:

	Millions of yen 2021	Millions of yen 2020	Thousands of U.S. dollars 2021
Deferred tax assets:			
Provision for bonuses	¥ 6,082	¥ 7,603	$ 54,931
Retirement benefit liability	43,543	48,812	393,271
Loss from inventory revaluation	3,326	3,056	30,040
Unrealized loss on marketable securities, investment securities and other	2,398	1,198	21,658
Loss on valuation of land	769	803	6,945
Allowance for doubtful receivables	1,136	1,177	10,260
Depreciation	13,850	8,591	125,090
Inventories–elimination of intercompany profits	206	1,294	1,861
Fixed assets–elimination of intercompany profits	489	548	4,417
Provision for construction warranties	3,220	3,846	29,082
Provision for losses on construction contracts	4,409	3,534	39,821
Provision for the in-service issues of commercial aircraft jet engines	1,826	4,789	16,492
Net operating loss carryforwards	14,370	3,212	129,787
Other	11,704	16,193	105,708
Gross deferred tax assets	107,336	104,663	969,436
Valuation allowance for tax loss carryforwards (*ii)	(3,892)	(2,672)	(35,152)
Valuation allowance for total deductible temporary differences	(18,322)	(13,221)	(165,480)
Less valuation allowance (*i)	(22,214)	(15,894)	(200,632)
Total deferred tax assets	85,121	88,768	768,795
Deferred tax liabilities:			
Reserve for advanced depreciation of non-current assets	2,374	4,502	21,441
Reserve for special depreciation	845	1,082	7,632
Net unrealized gain on securities	897	777	8,102
Retained earnings for foreign subsidiaries	8,753	7,497	79,055
Other	2,924	5,107	26,409
Total deferred tax liabilities	15,795	18,966	142,657
Net deferred tax assets	¥ 69,326	¥ 69,801	$626,138

*(*i) Valuation allowance increased by ¥6,320million ($57,081 thousand). This increase is due mainly to the additional recognition of valuation allowance for depreciation in the Company.*
*(*ii) Amount of tax loss carryforwards and deferred tax assets by expiration date*

Year ended March 31, 2021

2021 Millions of yen	Within 1 year	Over 1 year but within 2 years	Over 2 years but within 3 years	Over 3 years but within 4 years	Over 4 years but within 5 years	Over 5 years	Total
Net tax loss carried forward (*a)	¥0	¥1	¥4	¥2	¥244	¥14,117	¥14,370
Valuation allowance	(0)	(0)	(1)	(1)	(0)	(3,888)	(3,892)
Deferred tax assets	0	0	2	1	244	10,228	(*b)10,478

*(*a) Tax loss carryforwards are calculated by multiplying the statutory tax rate.*
*(*b) Deferred tax assets of ¥10,478 million ($94,635 thousand) was allocated to tax loss carryforwards of ¥14,370 million ($129,787 thousand) (the amount obtained by multiplying the statutory and effective tax rate). The deferred tax assets were primarily recognized as part of tax loss carryforwards of the Company. The tax loss carryforwards that allocated the deferred tax assets were primarily due to the recording of a net loss before income taxes in the year ended March 31, 2021, and by prospecting future taxable income, the Company has determined that it will be recoverable and has not recognized a valuation allowance.*

Year ended March 31, 2020

2020 Millions of yen	Within 1 year	Over 1 year but within 2 years	Over 2 years but within 3 years	Over 3 years but within 4 years	Over 4 years but within 5 years	Over 5 years	Total
Net tax loss carried forward (*c)	¥93	¥3	¥21	¥26	¥8	¥3,059	¥3,212
Valuation allowance	(93)	(2)	(8)	(22)	(4)	(2,540)	(2,672)
Deferred tax assets	0	0	12	3	3	519	539

*(*c) Tax loss carryforwards are calculated by multiplying the statutory tax rate.*

Year ended March 31, 2021

2021 Thousands of U.S. dollars	Within 1 year	Over 1 year but within 2 years	Over 2 years but within 3 years	Over 3 years but within 4 years	Over 4 years but within 5 years	Over 5 years	Total
Net tax loss carried forward	$0	$9	$36	$18	$2,204	$127,502	$129,787
Valuation allowance	(0)	(0)	(9)	(9)	(0)	(35,116)	(35,152)
Deferred tax assets	0	0	18	9	2,204	92,377	94,635

27.

Cash and cash equivalents

Cash and cash equivalents reconciled to the accounts reported in the consolidated balance sheets in the years ended March 31, 2021 and 2020 were as follows:

	Millions of yen 2021	Millions of yen 2020	Thousands of U.S. dollars 2021
Cash and deposits:	¥126,702	¥106,108	$1,144,346
Time deposits with maturities over three months:	(4,536)	(3,562)	(40,968)
Total	¥122,166	¥102,546	$1,103,378

28.

Content of important non-cash transactions

Year ended March 31, 2021
The Company and its subsidiaries have recorded assets and liabilities of ¥9,265 million ($83,680 thousand) for finance leases relating to the dormitories and the company housing.

Year ended March 31, 2020
Not applicable.

29

Profit/loss per share

Per share amounts for the years ended March 31, 2021, and 2020 are set forth in the table below.

	Millions of yen 2021	Millions of yen 2020	Thousands of U.S. dollars 2021
Basic earnings per share:			
Profit (loss) attributable to owners of parent	¥(19,332)	¥18,662	$(174,603)
Profit (loss) allocated to common stock	(19,332)	¥18,662	(174,603)

	Number of shares in millions 2021	Number of shares in millions 2020
Weighted average number of shares of common stock	167	167

Note: As the Company had no dilutive securities at March 31, 2021 or 2020, the Company has not disclosed diluted earnings per share for the years ended March 31, 2021 and 2020.

30.

Derivative transactions

(a) Outstanding positions and recognized gains and losses at March 31, 2021 were as follows:

(Derivative transactions to which the Company did not apply hedge accounting)

	2021				
	Millions of yen				Thousands of U.S. dollars
	Contract amount	Contract amount over 1 year	Fair value	Gain (loss)	Gain (loss)
Currency related contracts:					
Foreign exchange contracts:					
To sell					
USD	**¥ 83,864**	**¥–**	**¥(3,386)**	**¥(3,386)**	**¥(30,582)**
EUR	**5,762**	**–**	**(69)**	**(69)**	**(623)**
Others	**10,427**	**–**	**(477)**	**(477)**	**(4,308)**
To purchase					
USD	**2,082**	**–**	**35**	**35**	**316**
EUR	**164**	**1**	**13**	**13**	**117**
Others	**11,199**	**–**	**396**	**396**	**3,577**
Total	**¥113,501**	**¥1**	**¥(3,487)**	**¥(3,487)**	**¥(31,494)**

Fair value is based on prices provided by financial institutions, etc.

(Derivative transactions to which the Company applied hedge accounting)

	2021			
		Millions of yen		
	Subject of hedge	Contract amount	Contract amount over 1 year	Fair value
Currency related contracts:				
Foreign exchange contracts				
To sell	Accounts receivable–trade			
USD		**¥29,391**	**¥7,802**	**¥(857)**
EUR		**3,345**	**–**	**(47)**
Others		**2,964**	**946**	**(48)**
To purchase	Accounts payable–trade			
USD		**5,460**	**827**	**233**
EUR		**1,784**	**652**	**83**
Others		**5,399**	**568**	**211**
Total		**¥48,346**	**¥10,796**	**¥(424)**

Fair value is based on prices provided by financial institutions, etc.

	2021			
		Thousands of U.S. dollars		
	Subject of hedge	Contract amount	Contract amount over 1 year	Fair value
Currency related contracts:				
Foreign exchange contracts				
To sell	Accounts receivable–trade			
USD		**$265,453**	**$70,466**	**$(7,740)**
EUR		**30,211**	**–**	**(424)**
Others		**26,770**	**8,544**	**(434)**
To purchase	Accounts payable–trade			
USD		**49,314**	**7,469**	**2,104**
EUR		**16,113**	**5,889**	**750**
Others		**48,763**	**5,130**	**1,906**
Total		**$436,651**	**$97,507**	**$(3,829)**

Fair value is based on prices provided by financial institutions, etc.

	2021			
		Millions of yen		
	Subject of hedge	Contract amount	Contract amount over 1 year	Fair value
Interest related contracts:				
Fixed-rate payment/floating-rate receipt	Long-term loans borrowings	**¥19,500**	**¥19,500**	**¥(161)**
		¥19,500	**¥19,500**	**¥(161)**

Fair value is based on prices provided by financial institutions, etc.

	2021			
		Thousands of U.S. dollars		
	Subject of hedge	Contract amount	Contract amount over 1 year	Fair value
Interest related contracts:				
Fixed-rate payment/floating-rate receipt	Long-term loans borrowings	**$176,120**	**$176,120**	**$(1,454)**
		$176,120	**$176,120**	**$(1,454)**

Fair value is based on prices provided by financial institutions, etc.

(b) Outstanding positions and recognized gains and losses at March 31, 2020 were as follows:

(Derivative transactions to which the Company did not apply hedge accounting)

	2020			
	Millions of yen			
	Contract amount	Contract amount over 1 year	Fair value	Gain (loss)
Currency related contracts:				
Foreign exchange contracts:				
To sell				
USD	¥74,350	¥ –	¥(311)	¥(311)
EUR	11,566	–	45	45
Others	7,609	28	259	259
To purchase				
USD	973	–	1	1
EUR	230	–	(13)	(13)
Others	1,903	6	(61)	(61)
Total	¥96,634	¥34	¥ (81)	¥ (81)

Fair value is based on prices provided by financial institutions, etc.

(Derivative transactions to which the Company applied hedge accounting)

	2020			
		Millions of yen		
	Subject of hedge	Contract amount	Contract amount over 1 year	Fair value
Currency related contracts:				
Foreign exchange contracts				
To sell	Accounts receivable–trade			
USD		¥17,491	¥ 905	¥(223)
EUR		2,959	–	13
Others		335	34	(0)
To purchase	Accounts payable–trade			
USD		5,184	1,942	239
EUR		2,499	253	(38)
Others		4,848	308	(12)
Total		¥33,318	¥3,444	¥ (21)

Fair value is based on prices provided by financial institutions, etc.

	Subject of hedge	2020 Millions of yen Contract amount	Contract amount over 1 year	Fair value
Interest related contracts:				
Fixed-rate payment/floating-rate receipt	Long-term loans borrowings	¥17,500	¥17,500	¥(134)
		¥17,500	¥17,500	¥(134)

Fair value is based on prices provided by financial institutions, etc.

31. Financial instruments

Information related to financial instruments as of March 31, 2021 and 2020 was as follows.

(1) Matters related to the status of financial instruments

(a) Policies on the use of financial instruments

The Company meets its long-term operating capital and capital expenditure requirements through bank loans and the issuance of bonds and meets its short-term operating capital requirements through bank loans and the issuance of short-term bonds (electronic commercial paper). Temporary surplus funds are managed in the form of financial assets that have a high level of safety. The Company utilizes derivative financial instruments to hedge the risks described below and does not engage in speculative transactions as a matter of policy.

(b) Details of financial instruments and risks associated with those instruments

Notes and accounts receivable – trade are exposed to the credit risk of customers. The Company operates internationally and has significant exposure to the risk of fluctuation in foreign exchange rates. However, this risk is hedged using exchange contracts, etc., against the net position of foreign currency exposure. Investments in securities comprise mainly equity securities of companies with which the Company conducts business and are held to maintain relationships with these business partners. With such securities, listed stocks are exposed to market fluctuation risk.

Almost all notes and accounts payable – trade and electronically recorded obligations are due within one year. A portion of accounts payable - trade are denominated in foreign currency—specifically those related to payment for imported materials, etc., and are exposed to the risk of foreign currency fluctuation. However, this risk is mitigated principally by the position of accounts payable - trade denominated in foreign currency being less than the position of receivables in the same currency. Borrowings and bonds payable are used mainly to raise operating capital and carry out capital expenditure and are due in a maximum of twenty years from March 31, 2021 (twenty years in 2020). A portion of these instruments is exposed to the risk of interest rate fluctuation. However, such risk is hedged using derivatives (interest rate and currency swaps) as necessary.

In sum, derivatives comprise exchange and currency option contracts used to hedge foreign currency fluctuation risk on receivables and payables in foreign currencies and interest rate swap contracts to hedge interest rate fluctuation risk on debt. With regard to hedge accounting, see Note 2(s), "Hedge accounting."

(c) Risk management system for financial instruments

(i) Management of credit risk, including customer default risk

The Company's sales management functions and those of its consolidated subsidiaries regularly evaluate the financial circumstances of customers and monitor the due dates and balances by customer to identify and limit doubtful accounts.

With regard to derivative transactions, the Company enters into contracts with highly rated financial institutions to reduce counterparty risk. The amount presented in the balance sheet is the maximum credit risk at the fiscal year-end of the financial instruments that are exposed to credit risk.

(ii) Management of market risk (related to foreign currency exchange rates, interest rates, etc.)

The Company and certain of its consolidated subsidiaries hedge foreign currency fluctuation risk on receivables and payables in foreign currencies using mainly exchange contracts, which are categorized by the type of currency and the monthly due date. In principle, the net position of receivables less payables in a foreign currency is hedged mainly with forward exchange contracts. The Company and certain of its consolidated subsidiaries hedge interest rate risk on debt using interest rate swap contracts and currency swap contracts.

With regard to investments in securities, the Company reviews its holding policies through periodic analysis of market prices and the financial condition of the issuers, taking into consideration the relationships with its business partners.

With regard to derivatives, in accordance with rules for the provision of transaction authorization, the Company's finance functions and those of its consolidated subsidiaries manage transactions in accordance with an established set of fundamental policies, such as those covering limitations on transaction amounts, under the authority of the director in charge of finance. Transactions are reported to the director in charge of finance on a monthly basis. Consolidated subsidiaries manage derivatives in accordance with the same rules as those of the Company.

(iii) Management of liquidity risk (risk of the Company being unable to meet its payment obligations by their due dates)

The Company manages liquidity risk through its finance department, maintaining and updating its finance plans based on reports from each business division. Liquidity risk is managed through the diversification of financing methods, taking into consideration the financing environment and balancing long- and short-term financing requirements, securing commitment lines, etc.

(d) Supplemental information on the fair value of financial instruments

The fair value of financial instruments includes values based on market price and reasonably estimated values when market price is not available. However, as variables are inherent in these value calculations, the resulting values may differ if different assumptions are used. With regard to the contract amounts, etc., of the derivatives described in Note 30, "Derivative transactions," these amounts do not represent the market risk associated with the corresponding derivative transactions themselves.

(2) Fair values of financial instruments

The book values, the fair values and the differences between these values as of March 31, 2021 were as follows (Financial instruments for which the fair value was extremely difficult to determine were not included, as described in remark (ii)):

	2021 Millions of yen Book value	Fair value	Unrealized gains (losses)	Thousands of U.S. dollars Unrealized gains (losses)
Cash and deposits	**¥126,702**	**¥126,702**	**¥ –**	**$ –**
Notes and accounts receivable—trade	**460,436**	**460,462**	**25**	**226**
Investment securities	**5,566**	**5,566**	**–**	**–**
Total assets	**¥592,705**	**¥592,731**	**¥ 25**	**$226**
Notes and accounts payable—trade	**247,294**	**247,294**	**–**	**–**
Electronically recorded obligations—operating	**107,849**	**107,849**	**–**	**–**
Short-term borrowings and current portion of bonds payable (excluding lease obligations)	**171,579**	**171,579**	**–**	**–**
Long-term debt, less current portion (excluding lease obligations)	**389,177**	**389,161**	**(15)**	**(135)**
Total liabilities	**¥915,900**	**¥915,884**	**¥(15)**	**$(135)**
Derivative transactions (*)	**¥ (4,074)**	**¥ (4,074)**	**¥ –**	**$ –**

(*) Derivative financial instruments are presented as net amounts. Negative amounts stated with parentheses ( ) indicate that the net amount is a liability.

The book values, fair values and the differences between these values as of March 31, 2020 were as follows (Financial instruments for which the fair value was extremely difficult to determine were not included, as described in remark (ii)):

	2020		
	Millions of yen		
	Book value	Fair value	Unrealized gains (losses)
Cash and deposits	¥106,108	¥106,108	¥ –
Notes and accounts receivable–trade	473,204	473,133	(71)
Investment securities	5,738	5,738	–
Total assets	¥585,052	¥584,981	¥ (71)
Notes and accounts payable–trade	261,159	261,159	–
Electronically recorded obligations–operating	110,526	110,526	–
Short-term borrowings and current portion of bonds payable (excluding lease obligations)	186,188	186,188	–
Long-term debt, less current portion (excluding lease obligations)	348,859	348,662	(197)
Total liabilities	¥906,733	¥906,536	¥(197)
Derivative transactions (*)	¥ (237)	¥ (237)	¥ –

(*) Derivative financial instruments are presented as net amounts. Negative amounts stated with parentheses ( ) indicate that the net amount is a liability.

(i) Methods used to calculate the fair value of financial instruments and details of securities and derivative instruments

<Assets>

- Cash and deposits
  The book values are used as the fair values since the settlement periods of these items are short and their fair values are substantially the same as their book values.
- Notes and accounts receivable - trade
  The fair value of notes and accounts payable – trade is stated at present value computed by applying a discount rate reflecting the settlement period and the credit risk.
- Investment securities
  Equity securities are stated at the fair value, and bonds are stated at market price. See Note 2(j), "Investment securities," for the detailed information by classification.

<Liabilities>

- Notes and accounts payable - trade, electronically recorded obligations - operating, short-term borrowings and current portion of bonds payable
  Since the settlement periods of these items are short and their fair values are substantially the same as their book values, the relevant book values are used.

- Long-term debt, less current portion
  The fair value of bonds payable is stated at the market price. The fair value of long-term borrowings is calculated by applying a discount rate to the total principal and interest. That discount rate is based on the interest rates of similar new loans.

<Derivatives>

See Note 30, "Derivative transactions."

(ii) Financial instruments for which the fair value is extremely difficult to determine.

	Millions of yen		Thousands of U.S. dollars
	2021	2020	**2021**
Unlisted equity securities and investments in partnerships	**¥ 6,961**	¥ 6,117	**$ 62,870**
Convertible bonds	**194**	179	**1,752**
Stocks of non-consolidated subsidiaries and affiliates	**11,487**	14,520	**103,748**
Investments in affiliates	**69,355**	64,974	**626,400**
Total	**¥87,999**	¥85,791	**$794,789**

Since no market values are available for these items and since it is extremely difficult to determine their fair values, the items listed in the table above are not included in investment securities.

(iii) Planned redemption amounts after the balance sheet date for monetary receivables and investment securities with maturity dates as of March 31, 2021 and 2020 were as follows:

	2021			
	Millions of yen			
	Within 1 year	Over 1 year but within 5 years	Over 5 years but within 10 years	Over 10 years
Cash and deposits	**¥126,702**	**¥ –**	**¥–**	**¥–**
Notes and accounts receivable–trade	**434,034**	**26,402**	**–**	**–**
Convertible bonds	**–**	**194**	**–**	**–**
Total	**¥560,736**	**¥26,597**	**¥–**	**¥–**

	2021			
	Thousands of U.S. dollars			
	Within 1 year	Over 1 year but within 5 years	Over 5 years but within 10 years	Over 10 years
Cash and deposits	**$1,144,346**	**$ –**	**$–**	**$–**
Notes and accounts receivable–trade	**3,920,105**	**238,457**	**–**	**–**
Convertible bonds	**–**	**1,752**	**–**	**–**
Total	**$5,064,451**	**$240,219**	**$–**	**$–**

	2020			
	Millions of yen			
	Within 1 year	Over 1 year but within 5 years	Over 5 years but within 10 years	Over 10 years
Cash and deposits	¥106,108	¥ –	¥–	¥–
Notes and accounts receivable–trade	438,899	34,305	–	–
Convertible bonds	–	179	–	–
Total	¥545,008	¥34,484	¥–	¥–

(iv) Planned repayment amounts after the balance sheet date for bonds payable and long-term borrowings.

See Note 11, "Short-term debt and long-term debt."

32.

Finance leases

Finance lease transactions without transfer of ownership

(i) Contents of lease assets

Property, plant and equipment Mainly assets relating to dormitories and company housing of the Company and its subsidiaries.

(ii) Depreciation method of leased assets

See Note 2(t),"Finance leases."

33.

Operating leases

The schedule of future minimum lease payments under non-cancellable operating leases as of March 31, 2021 and 2020 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2021	2020	**2021**
Within one year	**¥ 5,631**	¥ 3,853	**$ 50,858**
Over one year	**26,351**	17,170	**237,997**
Total	**¥31,983**	¥21,023	**$288,864**

34.

Segment information

(a) Overview of reportable segments

The Company's reportable segments are components of the Company about which separate financial information is available. These segments are subject to periodic reviews by the Company's board of directors to decide how to allocate resources and assess performance. The Company's operations are divided into internal companies based on product categories. Certain authority is delegated to each of the internal companies, based on which they conduct businesses in Japan and overseas. The Company's operations are therefore segmented based on each internal company's product categories. The Company's seven reportable segments are the Aerospace Systems segment, the Energy System & Plant Engineering segment, the Precision Machinery & Robot segment, the Ship & Offshore Structure segment, the Rolling Stock segment, the Motorcycle & Engine segment, and the Other segment.

Main segment businesses are listed below.

Business segment	Major products
Aerospace Systems	Production and sale of aircraft, jet engines, etc.
Energy System & Plant Engineering	Production and sale of energy-related machinery and system, marine machinery and system, industrial equipment, environmental equipment, ultralow temperature tank, hydrogen-related structures, crushers, etc.
Precision Machinery & Robot	Production and sale of industrial hydraulic products, industrial robots, etc.
Ship & Offshore Structure	Construction and sale of ships and other vessels, etc.
Rolling Stock	Production and sale of rolling stock, snow plows, etc.
Motorcycle & Engine	Production and sale of motorcycles, all-terrain vehicles (ATV), utility vehicles, personal watercraft ("JET SKI"), general-purpose gasoline engines, etc.
Other	Commercial activities, sales/order agency and intermediary activities, administration of welfare facilities, etc.

(b) Method for calculating sales, profit/loss, assets, liabilities, and other items for reportable segments

The accounting methods applied to the reported business segments generally follow the accounting policies used to prepare the consolidated financial statements. The income of reporting segments is based on operating profit. Inter-segment earnings and transfers are based on market prices.

(c) Sales, Profit (loss), assets, liabilities, and other items by reportable segment

Year ended March 31, 2021

	Millions of yen								
	Sales					Other items			
	External sales	Intersegment sales and transfers	Total	Segment profit (loss)	Segment assets	Depreciation/ amortization	Impairment losses	Investment in equity-method affiliates	Increase in property, plant and equipment and intangibles
Aerospace Systems	**¥ 377,720**	**¥ 7,681**	**¥ 385,402**	**¥(31,668)**	**¥ 757,342**	**¥23,043**	**¥ –**	**¥ –**	**¥22,113**
Energy System & Plant Engineering	**240,117**	**20,252**	**260,370**	**13,408**	**342,500**	**3,340**	**–**	**18,080**	**4,162**
Precision Machinery & Robot	**240,864**	**14,853**	**255,717**	**14,086**	**213,792**	**10,071**	**–**	**(24)**	**9,836**
Ship & Offshore Structure	**79,425**	**3,764**	**83,189**	**(3,059)**	**133,932**	**1,407**	**4,076**	**49,841**	**1,030**
Rolling Stock	**133,248**	**7**	**133,256**	**(4,593)**	**215,688**	**2,551**	**11,129**	**148**	**2,424**
Motorcycle & Engine	**336,694**	**730**	**337,424**	**11,758**	**256,997**	**14,904**	**–**	**1,538**	**12,790**
Other	**80,415**	**36,979**	**117,395**	**469**	**73,211**	**947**	**–**	**3,880**	**548**
Total	**¥1,488,486**	**¥84,270**	**¥1,572,757**	**¥ 403**	**¥1,993,465**	**¥56,267**	**¥15,205**	**¥73,464**	**¥52,907**
Adjustments	**–**	**(84,270)**	**(84,270)**	**(5,709)**	**(30,189)**	**4,991**	**–**	**–**	**12,772**
Consolidated total	**¥1,488,486**	**¥ –**	**¥1,488,486**	**¥ (5,305)**	**¥1,963,276**	**¥61,258**	**¥15,205**	**¥73,464**	**¥65,679**

Year ended March 31, 2020

	Millions of yen								
	Sales					Other items			
	External sales	Intersegment sales and transfers	Total	Segment profit (loss)	Segment assets	Depreciation/ amortization	Impairment losses	Investment in equity-method affiliates	Increase in property, plant and equipment and intangibles
Aerospace Systems	¥ 532,549	¥ 6,477	¥ 539,027	¥42,777	¥ 745,048	¥22,539	¥–	¥ –	¥25,121
Energy System & Plant Engineering	242,972	30,871	273,843	17,566	314,753	3,362	–	18,621	3,048
Precision Machinery & Robot	217,387	15,529	232,917	12,211	203,525	9,279	–	1,737	12,845
Ship & Offshore Structure	71,680	9,049	80,730	(637)	125,642	1,625	–	44,930	1,355
Rolling Stock	136,553	18	136,571	(3,819)	211,759	2,533	–	135	2,740
Motorcycle & Engine	337,757	772	338,529	(1,948)	282,185	15,963	–	1,601	21,353
Other	102,435	38,927	141,362	1,235	94,174	1,562	–	3,682	745
Total	¥1,641,335	¥101,647	¥1,742,983	¥67,386	¥1,977,089	¥56,866	¥–	¥70,708	¥67,210
Adjustments	–	(101,647)	(101,647)	(5,322)	(19,243)	4,417	–	–	3,284
Consolidated total	¥1,641,335	¥ –	¥1,641,335	¥62,063	¥1,957,845	¥61,283	¥–	¥70,708	¥70,495

Note: Starting from the fiscal year ending March 2022, the Company has integrated its previous reportable segments of the Energy System & Plant Engineering and the Ship & Offshore Structure into the Energy Solutions & Marine. As a result, the reportable segments have been changed to the following six segments, the Aerospace Systems, the Rolling Stock, the Energy Solutions & Marine, the Precision Machinery & Robot, the Motorcycle & Engine and the Other.

Year ended March 31, 2021									
	Thousands of U.S. dollars								
	Sales					Other items			
	External sales	Intersegment sales and transfers	Total	Segment profit (loss)	Segment assets	Depreciation/ amortization	Impairment losses	Investment in equity-method affiliates	Increase in property, plant and equipment and intangibles
Aerospace Systems	$ 3,411,488	$ 69,373	$ 3,480,871	$(286,019)	$6,840,155	$208,120	$ –	$ –	$199,720
Energy System & Plant Engineering	2,168,687	182,912	2,351,608	121,098	3,093,389	30,166	–	163,295	37,590
Precision Machinery & Robot	2,175,434	134,149	2,309,583	127,222	1,930,925	90,959	–	(217)	88,837
Ship & Offshore Structure	717,350	33,996	751,346	(27,628)	1,209,646	12,708	36,814	450,154	9,303
Rolling Stock	1,203,468	63	1,203,540	(41,483)	1,948,049	23,040	100,515	1,337	21,893
Motorcycle & Engine	3,040,950	6,593	3,047,543	106,196	2,321,143	134,610	–	13,891	115,517
Other	726,292	333,987	1,060,287	4,236	661,227	8,553	–	35,043	4,949
Total	$13,443,696	$761,109	$14,204,814	$3,640	$18,004,561	$508,192	$137,328	$663,512	$477,845
Adjustments	–	(761,109)	(761,109)	(51,563)	(272,661)	45,078	–	–	115,354
Consolidated total	$13,443,696	$ –	$13,443,696	$(47,914)	$17,731,900	$553,270	$137,328	$663,512	$593,199

(d) Reconciliation and main components of difference between total for reportable segments and amounts on the consolidated financial statements for the year ended March 31, 2021 and 2020

	Millions of yen		Thousands of U.S. dollars
	2021	2020	2021
Sales			
Total for reportable segments	¥1,572,757	¥1,742,983	$14,204,814
Intersegment transactions	(84,270)	(101,647)	(761,109)
Net sales reported on the consolidated financial statements	¥1,488,486	¥1,641,335	$13,443,696

	Millions of yen		Thousands of U.S. dollars
	2021	2020	2021
Profit			
Total for reportable segments	¥ 403	¥67,386	$ 3,640
Intersegment transactions	36	209	325
Corporate expenses (*)	(5,745)	(5,532)	(51,888)
Operating profit (loss) on the consolidated financial statements	¥(5,305)	¥62,063	$(47,914)

(*) Corporate expenses comprise mainly general and administrative expenses not attributed to reportable segments.

	Millions of yen		Thousands of U.S. dollars
	2021	2020	2021
Assets			
Total for reportable segments	¥1,993,465	¥1,977,089	$18,004,561
Intersegment transactions	(138,978)	(107,921)	(1,255,220)
Corporate assets shared by all segments (*)	108,788	88,678	982,551
Total assets on the consolidated financial statements	¥1,963,276	¥1,957,845	$17,731,900

(*) Corporate assets shared by all segments comprise mainly fixed assets not attributed to reportable segments.

	Millions of yen					
	2021	2020	2021	2020	2021	2020
Other items	Total for reportable segments		Adjustments (*)		Amounts reported on the consolidated financial statements	
Depreciation/amortization	¥56,267	¥56,866	¥ 4,991	¥4,417	¥61,258	¥61,283
Increase in property, plant and equipment and intangible assets	52,907	67,210	12,772	3,284	65,679	70,495

(*) Adjustment is due mainly to fixed assets not attributed to reportable segments.

	Thousands of U.S. dollars		
	2021		
Other items	Total for reportable segments	Adjustments	Amounts reported on the consolidated financial statements
Depreciation/amortization	$508,192	$ 45,078	$553,270
Increase in property, plant and equipment and intangible assets	477,845	115,354	593,199

(e) Related information

(i) Sales by geographic region

Net sales for the years ended March 31, 2021, and 2020 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2021	2020	2021
Japan	¥ 704,163	¥ 699,879	$ 6,359,854
United States	313,607	413,095	2,832,433
Europe	143,402	220,574	1,295,177
Asia	277,266	236,687	2,504,209
Other areas	50,047	71,098	452,014
Total	¥1,488,486	¥1,641,335	$13,443,696

Net sales are based on the clients' location and classified according to country or geographical region.

Property, plant and equipment

	Millions of yen		Thousands of U.S. dollars
	2021	2020	2021
Japan	¥389,640	¥421,567	$3,519,147
North America	29,646	29,134	267,757
Europe	3,065	3,259	27,682
Asia	28,553	28,116	257,885
Other areas	354	493	3,197
Total	¥451,259	¥482,570	$4,075,677

(ii) Information by major clients

Year ended March 31, 2021		
Clients	Net sales	Related segments
Ministry of Defense	¥260,960 million ($2,356,936 thousand)	Aerospace Systems, Energy System & Plant Engineering, Ship & Offshore Structure, etc.

Year ended March 31, 2020		
Clients	Net sales	Related segments
Ministry of Defense	¥256,839 million	Aerospace Systems, Energy System & Plant Engineering, Ship & Offshore Structure, etc.

35.

Related party transactions

(a) Related party transactions for the years ended March 31, 2021 and 2020 were as follows:

	Year ended March 31, 2021
	Non-consolidated subsidiaries and affiliates of the Company
Type	**Affiliate of the Company**
Name	**Commercial Airplane Co., Ltd.**
Location	**Chiyoda-ku, Tokyo**
Capital or investment	**¥10 million ($90 thousand)**
Business or position	**Sales of transportation machinery**
Rate of ownership (%)	**Directly 40%**
Description of relationship	**Sales of Company products and board members**
Details of transactions	**Sales of Company products**
Amount of transactions	**¥58,508 million ($528,432 thousand)**
Account	**Accounts receivable—trade**
Ending balance	**¥36,382 million ($328,595 thousand)**
Account	**Advances received**
Ending balance	**¥48,521 million ($438,232 thousand)**

	Year ended March 31, 2020
	Non-consolidated subsidiaries and affiliates of the Company
Type	Affiliate of the Company
Name	Commercial Airplane Co., Ltd.
Location	Chiyoda-ku, Tokyo
Capital or investment	¥10 million
Business or position	Sales of transportation machinery
Rate of ownership (%)	Directly 40%
Description of relationship	Sales of Company products and board members
Details of transactions	Sales of Company products
Amount of transactions	¥118,869 million
Account	Accounts receivable—trade
Ending balance	¥56,654 million
Account	Advances received
Ending balance	¥52,346 million

(b) A summary of the total financial information of affiliates, which was the basis for calculating the equity in income of the non-consolidated affiliates, including that of Nantong COSCO KHI Ship Engineering Co., Ltd., which is a significant affiliate, for the years ended March 31, 2021 and 2020 is as follows:

	Millions of yen		Thousands of U.S. dollars
	2021	2020	**2021**
Current assets	**¥198,335**	¥161,524	**$1,791,320**
Non-current assets	**146,338**	141,628	**1,321,694**
Current liabilities	**153,614**	108,542	**1,387,410**
Non-current liabilities	**31,822**	37,795	**287,410**
Net assets	**159,236**	156,813	**1,438,186**
Net sales	**243,186**	217,702	**2,196,405**
Profit before income taxes	**4,489**	7,133	**40,544**
Profit	**1,878**	4,708	**16,962**

36.

Subsequent events

(Issuance of Corporate Bonds)

At the Management Committee held on June 15, 2021, it was resolved to issue the following straight bonds (sustainability bonds) as follows:

1. The 58th unsecured straight bond

Issue date	From July 1, 2021 to September 30, 2021
Total amount of issue	¥10 billion ($90,318 thousand)
Issue price	¥100 ($0.90) per face value of ¥100 ($0.90)
Interest rate	0.8% or less per annum
Maturity date	10 years
Type	Unsecured
Usage of funds	Research and development funds, equipment funds, investment and loan funds, and bond redemption and loan repayment funds
Method of offering	Public offering

37.

Other matters

(a) Quarterly financial information

	Millions of yen			
Year ended March 31, 2021	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
Net sales	**¥300,602**	**¥657,325**	**¥1,032,484**	**¥1,488,486**
Profit (loss) before income taxes	**(14,114)**	**(17,385)**	**811**	**(14,688)**
Net loss attributable to owners of parent	**(11,771)**	**(27,267)**	**(13,969)**	**(19,332)**
	Yen			
Loss per share—basic	**¥ (70.47)**	**¥ (163.23)**	**¥ (83.62)**	**¥ (115.73)**

	Thousands of U.S. dollars			
Year ended March 31, 2021	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
Net sales	**$2,714,975**	**$5,936,823**	**$9,325,181**	**$13,443,696**
Profit (loss) before income taxes	**(127,475)**	**(157,018)**	**7,325**	**(132,659)**
Net loss attributable to owners of parent	**(106,313)**	**(246,270)**	**(126,165)**	**(174,603)**
	U.S. dollars			
Loss per share—basic	**$ (0.636)**	**$ (1.474)**	**$ (0.755)**	**$ (1.045)**

(b) Material lawsuits, etc.

<Receipt of customs duty reassessment notification in the Kingdom of Thailand>

KAWASAKI MOTORS ENTERPRISE (THAILAND) CO., LTD. (hereinafter, "KMT"), a consolidated subsidiary of the Company in the Kingdom of Thailand, received a reassessment notification of customs duties for 4,029 million baht (equivalent to approximately ¥14,000 million ($126,445 thousand) when converted at a rate of 0.29 yen to 1 baht) from the Revenue Department of Thailand. KMT had until that time filed its customs duties in accordance with guidance from the Revenue Department. Since the content of the notification of reassessment lacked a legitimate basis and was extremely unreasonable, KMT could not accept it and submitted an appeal of the reassessment to the Commission of Appeal, the appeals body for tax assessments received from the Revenue Department of Thailand. Based on the opinion of attorneys consulted regarding this matter, the Company maintains that there is a strong possibility KMT's assertion will be upheld.

<Claim for damages in overseas LNG tank construction work>

In connection with a certain liquefied natural gas (LNG) tank construction project carried out by the Company overseas, the Company filed a petition for arbitration with The International Chamber of Commerce (ICC) concerning losses sustained by the Company due to the breach of contract by an overseas construction subcontractor. During the arbitration proceedings, the counterparty claimed damages from the Company, but the Company believes that these claims lack legitimate grounds and are thus unjustified. The Company will continue to assert the legitimacy of its claims through the arbitration process.

Independent auditor’s report

To the Board of Directors of Kawasaki Heavy Industries, Ltd.:

Opinion

We have audited the accompanying consolidated financial statements of Kawasaki Heavy Industries, Ltd. (“the Company”) and its consolidated subsidiaries (collectively referred to as “the Group”), which comprise the consolidated balance sheets as at March 31, 2021 and 2020, the consolidated statements of income, comprehensive income, changes in net assets and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at March 31, 2021 and 2020, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with accounting principles generally accepted in Japan.

Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in Japan. Our responsibilities under those standards are further described in the *Auditor’s Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Japan, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Appropriateness of management’s judgment on the recoverability of deferred tax assets of Kawasaki Heavy Industries, Ltd.

The key audit matter	How the matter was addressed in our audit
In the consolidated balance sheet of Kawasaki Heavy Industries, Ltd. (hereinafter, the “Company”) and its consolidated subsidiaries as of March 31, 2021, deferred tax assets of ¥70,452 million were recognized. As described in Note 26. “Income taxes” to the consolidated financial statements, the amount of gross deferred tax assets before being offset by deferred tax liabilities amounted to ¥85,121 million. Of this amount, the gross deferred tax assets held by the Company that files a consolidated tax return with its wholly owned domestic subsidiaries amounted to ¥67,306 million, representing approximately 3.4% of total assets in the consolidated financial statements. Deferred tax assets are recognized to the extent that tax loss carryforwards and deductible temporary differences are expected to reduce future taxable income. When significant tax loss carryforwards exist, a more deliberate consideration is required to assess the recoverability of deferred tax assets. The future taxable income to be generated by the Company, which was used to determine the recoverability of its deferred tax assets, was primarily estimated based on the business plan prepared by management. This business plan involved uncertainty due to the reasons set forth below, and had a significant effect on the assessment of the recoverability of deferred tax assets. ・ Forecasts of revenue and profit, which are the key elements of the business plan, may be affected by changes in economic conditions in the future, and other factors. ・ Estimates related to the effect of COVID-19 incorporated into the business plan, including the forecasts of global passenger travel demands, involved significant management judgment. We, therefore, determined that our assessment of the appropriateness of management’s judgement on the recoverability of deferred tax assets of the Company was one of the most significant matters in our audit of the consolidated financial statements for the current fiscal year, and accordingly, a key audit matter.	The primary procedures we performed to assess whether management's judgment on the recoverability of deferred tax assets of the Company was appropriate included the following: **(1) Internal control testing** We tested the design and operating effectiveness of certain of the Company's internal controls relevant to the judgment on the recoverability of deferred tax assets. In this assessment, we focused our testing on internal controls over the preparation of the business plan used to estimate the Company's future taxable income. **(2) Assessment of the reasonableness of the estimated future taxable income** In order to assess the reasonableness of key assumptions adopted in preparing the business plan, that served as the basis for estimating future taxable income, we: ・ evaluated the process of preparing the business plan that served as the basis for estimating future taxable income by inquiring of management and each company president and inspecting the minutes of Management Committee of the Company; ・ assessed the consistency of the estimated future taxable income used to determine the recoverability of deferred tax assets with the business plan approved by Management Committee of the Company; ・ assessed the reasonableness of key assumptions, which formed the basis for the sales forecasts used for the estimates incorporated into the business plan of Aerospace Systems Company, by comparing them with information provided by major customers and the market forecast reports published by the International Air Transport Association; and evaluated the reasonableness of the scheduling of deductible temporary differences and tax-return adjustments included in the calculation of future taxable income by comparing them with the taxable income calculation for the current fiscal year.

Management’s assessment of the amount recoverable related to a loss sustained due to a breach of contract by an overseas construction subcontractor that failed to fulfill the contract on a certain overseas LNG tank construction work (Energy System & Plant Engineering Company)	
The key audit matter	**How the matter was addressed in our audit**
As described in Note 9. “Claim for damages in overseas LNG tank construction work,” Kawasaki Heavy Industries, Ltd. (hereinafter, the “Company”) sustained a loss of approximately ¥51billion due to a breach of contract by an overseas construction subcontractor that failed to fulfill the contract on a certain overseas LNG tank construction work. In connection with this issue, the Company filed a petition for arbitration with the International Chamber of Commerce (“ICC”). The Company plans to settle this dispute through the arbitration process, and recognized an asset for the expected amount recoverable as a result of the arbitration within Other under Investments and other assets in the consolidated balance sheet. The amount recoverable through the arbitration was assessed considering the progress of the arbitration proceedings at the ICC and the prospect for an award of the arbitral tribunal, as well as the business environment and the financial conditions of the overseas construction subcontractor. These estimates included subjective assumptions requiring significant management judgment, such as an award of the arbitral tribunal related to the subject and amount of damages, the Company alleged, caused by the breach of contract by the overseas construction subcontractor, as well as the ability of the overseas construction subcontractor to make payment for any monetary award to be determined by the arbitral tribunal, which involved uncertainty. We, therefore, determined that our assessment of the appropriateness of management’s assessment of the amount recoverable related to a loss sustained due to a breach of contract by an overseas construction subcontractor that failed to fulfill the contract on a certain overseas LNG tank construction project was one of the most significant matters in our audit of the consolidated financial statements for the current fiscal year, and accordingly, a key audit matter.	The primary procedures we performed to assess the reasonableness of management's assumptions used for assessing the amount recoverable through the arbitration included the following: **(1) Internal control testing** We tested the design and operating effectiveness of certain of the Company's internal controls relevant to management's assessment of the amount recoverable through the arbitration. In the assessment, we focused on internal controls in which the personnel responsible for the accounting division assess the estimates of the recoverability of each item of damages alleged, giving consideration to the opinion of the Company's legal counsel. **(2) Assessment of the reasonableness of the estimated amount recoverable through the arbitration** ・ We inspected the minutes of Management Committee of the Company related to the result of management’s assessment of the amount recoverable. In addition, we inquired of several personnel, such as management (including the president of Energy System & Plant Engineering Company) and those responsible for the administration division and the accounting division, and then assessed the reasonableness of their respective responses. ・ We circularized, through a written legal confirmation, directly with the legal counsel engaged by the Company to assess the amount recoverable, and assessed the consistency of the opinion of the legal counsel with the result of management’s assessment of the amount recoverable. We inspected the annual reports issued by the overseas construction subcontractor and the monthly research reports on the financial conditions, order booking status and other information of the overseas construction subcontractor submitted by the Company’s legal counsel, and evaluated the consistency of the information with the result of management’s assessment of the overseas construction subcontractor’s ability to make payment.

Responsibilities of Management and the Audit and Supervisory Committee for the Consolidated Financial Statements

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

In preparing the consolidated financial statements, management is responsible for assessing the Group’s ability to continue as a going concern, disclosing, as applicable, matters related to going concern in accordance with accounting principles generally accepted in Japan.

The audit and supervisory committee is responsible for overseeing the directors’ performance of their duties with regard to the design, implementation and maintenance of the Group’s financial reporting process.

Auditor’s Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor’s report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with auditing standards generally accepted in Japan will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of our audit in accordance with auditing standards generally accepted in Japan, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, while the objective of the audit is not to express an opinion on the effectiveness of the Group’s internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management’s use of the going concern basis of accounting and based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group’s ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor’s report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor’s report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate whether the presentation and disclosures in the consolidated financial statements are in accordance with accounting standards generally accepted in Japan, the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the audit and supervisory committee regarding, among other matters, the planned scope and timing of the audit, significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the audit and supervisory committee with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the audit and supervisory committee, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Convenience Translation

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended March 31, 2021 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 1 to the consolidated financial statements.

Interest required to be disclosed by the Certified Public Accountants Act of Japan

We do not have any interest in the Group which is required to be disclosed pursuant to the provisions of the Certified Public Accountants Act of Japan.

Matsuyama Kazuhiro

Designated Engagement Partner

Certified Public Accountant

Narumoto Koji

Designated Engagement Partner

Certified Public Accountant

Seishi Kyoichi

Designated Engagement Partner

Certified Public Accountant

KPMG AZSA LLC

Kobe Office, Japan

June 25, 2021