Annual Report 2017

Fiscal Year Ended March 31, 2017

Meeting Your Expectations and Earning Your Trust by Both Solving Problems of Society and Expanding Our Business

Focusing on the air-conditioning and fluorochemicals business, Daikin Industries, Ltd. operates in more than 150 countries, contributing to healthy and comfortable lives through the providing of air conditioners and a wide range of other products and services.

Constantly refining the atmosphere- and environment-related technologies that it has developed since its founding, Daikin strives to both solve problems of society and expand its business. That is how Daikin Industries' corporate value is born.

Under the "FUSION 20" strategic management plan started in fiscal 2017, Daikin Industries is working to meet your expectations and earn your trust by contributing to the sustainable development of global society through new value co-created by bringing together not only internal expertise of our Group but also external expertise obtained via open innovation.

Contents

Forward-Looking Statements

This annual review contains statements regarding the future plans and strategies of Daikin Industries, Ltd. (the Company), as well as the Company's future performance. These statements are not statements of past facts but are based on judgments made by the Company on the basis of information known at the time. Therefore, readers should refrain from drawing conclusions based only on these statements regarding the future performance of the Company. The actual future performance of the Company may be influenced by economic trends, strong competition in the industrial sectors where it conducts its operations, foreign currency exchange rates, and changes in taxation and other systems. For these reasons, these forward-looking statements are subject to latent risk and uncertainty.

Our Group Philosophy

1. Create New Value by Anticipating the Future Needs of Customers
2. Contribute to Society with World-Leading Technologies
3. Realize Future Dreams by Maximizing Corporate Value
4. Think and Act Globally
5. Be a Flexible and Dynamic Group

1. Flexible Group Harmony **2.** Build Friendly yet Competitive Relations with Our Business Partners to Achieve Mutual Benefit

6. Be a Company that Leads in Applying Environmentally Friendly Practices
7. With Our Relationship with Society in Mind, Take Action and Earn Society's Trust

1. Be Open, Fair, and Known to Society **2.** Make Contributions that Are Unique to Daikin to Local Communities

8. The Pride and Enthusiasm of Each Employee Are the Driving Forces of Our Group

1. The Cumulative Growth of All Group Members Serves as the Foundation for the Group's Development
2. Pride and Loyalty **3.** Passion and Perseverance

9. Be Recognized Worldwide by Optimally Managing the Organization and its Human Resources, under Our Fast & Flat Management System

1. Participate, Understand, and Act **2.** Offer Increased Opportunities to Those who Take on Challenges
3. Demonstrate Our Strength as a Team Composed of Diverse Professionals

10. An Atmosphere of Freedom, Boldness, and "Best Practice, Our Way"

Process of Value Creation

Environmental Awareness

Air conditioning as a part of society's infrastructure enables the creation of comfortable lives.

When our products are used, a large amount of electricity is consumed.

Reducing the impact on climate change is a top-priority issue for us.

Strategic Assumptions
SWOT

Strengths
- Heat pump technology
- Inverter technology
- Refrigerant control technology
- Sales and service network
- Development and production closest to market

Weaknesses
- Sales skewed towards main products (air conditioners)

Opportunities
- Global cooperation on climate change (Paris Agreement)
- Setting of sustainable development goals (UN SDGs)

Threats
- Changes in de facto standards for air conditioning

Strategy: "FUSION 20"
12 Group Strategies

Basic Approaches

Existing business domains (AC, Chemicals, Filters)
1. AC in North America 2. AC in Asia
3. Chemicals 4. Filters

New business domains/structure (Environment/Energy, IAQ/AE Engineering)
5. New businesses to quickly produce results Heating/Water Heaters, Energy Solutions
6. Strategic business in the long-term Commercial Refrigeration, Next-generation Refrigerants/Gas, IAQ/Air Environment (AE) Engineering

Technologies and *monozukuri*
7. Differentiated technologies/products with the Technology and Innovation Center
8. Enhanced *monozukuri* in the AC business

Corporate management
9. Lean and competitive fixed-cost structure
10. Optimal inventory aiming at cash flow maximization
11. Financial operation standardization and IT integration

Unique corporate philosophy
12. Enhanced HR based on people-centered management

FY2021 Goals

Contribute to solving problems of customers and society while working to achieve sales of ¥3.0 trillion and an operating income margin of 12%

Create new value and contribute to the sustainable development of society through our business

Direction for Group Development

An enterprise group that will "Co-Create New Value in the Air and Environment Fields"

ESG

Corporate Governance, Environment, New Value Creation, Customer Satisfaction, Human Resources, Compliance Risk Management, Risk Management, CSR Promotion System, Respect for Human Rights, Supply Chain Management, Stakeholder Engagement, Regional Society

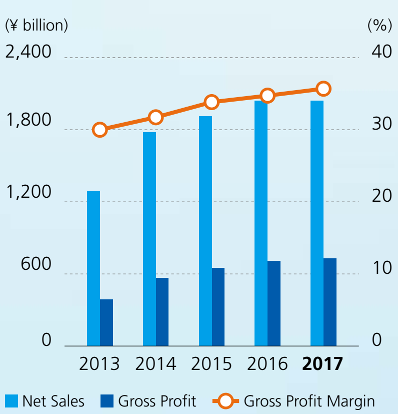
Financial Highlights

Daikin Industries, Ltd. and Consolidated Subsidiaries
Years Ended March 31

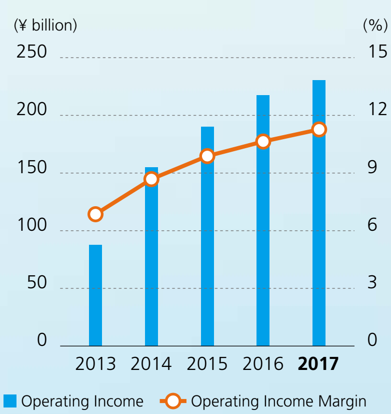
	Millions of Yen	
	2016	**2017**
Operating Results (for the year):		
Net sales	¥2,043,691	**¥2,043,969**
Gross profit	711,576	**730,935**
Operating income	217,872	**230,769**
Net income attributable to owners of parent	136,987	**153,939**
Cash Flows (for the year):		
Net cash provided by operating activities	¥226,186	**¥267,663**
Net cash used in investing activities	(105,493)	**(128,823)**
Free cash flow (Note)	120,693	**138,840**
Net cash used in financing activities	(85,422)	**(73,544)**
Financial Position (at year-end):		
Total assets	¥2,191,105	**¥2,356,149**
Total shareholders' equity	1,014,409	**1,111,636**
Per Share Data (yen):		
Net income (basic)	¥ 469.23	**¥ 526.81**
Shareholders' equity	3,473.54	**3,802.10**
Cash dividends	120.00	**130.00**
Cash flow per share	413	**475**
Ratios (%):		
Gross profit margin	34.82%	**35.76%**
Operating income margin	10.66	**11.29**
Return on shareholders' equity (ROE)	13.44	**14.48**
Shareholders' equity ratio	46.30	**47.18**

Note: Free cash flow = Net cash provided by operating activities + net cash used in investing activities

Net Sales, Gross Profit, and Gross Profit Margin



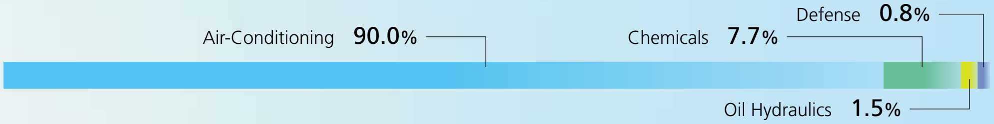
Operating Income and Operating Income Margin



ROE

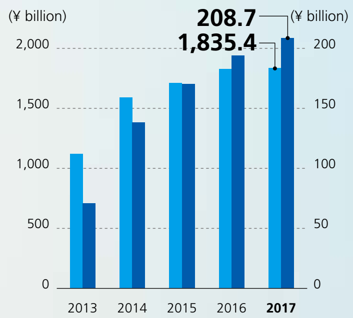
At a Glance

Percentage of Net Sales ▶



Air-Conditioning

Net Sales and Operating Income



Major Products

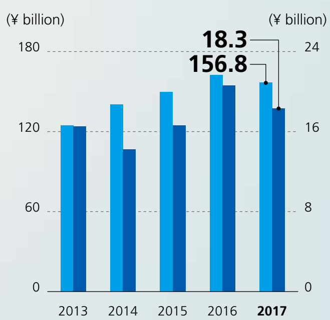
- Room air-conditioning systems
- Air purifiers
- Heat-pump hot-water-supply and room-heating systems
- Packaged air-conditioning systems
- Multiple air-conditioning systems for office buildings
- Air-conditioning systems for facilities and plants
- Absorption refrigerators
- Freezers
- Water chillers
- Turbo refrigerator equipment
- Air-handling units
- Air filters
- Industrial dust collectors
- Marine-type container refrigeration

Description

Since becoming the first in Japan to manufacture packaged air-conditioning systems in 1951, Daikin has supported comfortable living based on the strengths of technologies that it has itself nurtured as the world's sole manufacturer to create a full line of products from refrigerants to air conditioners.

Chemicals

Net Sales and Operating Income



Major Products

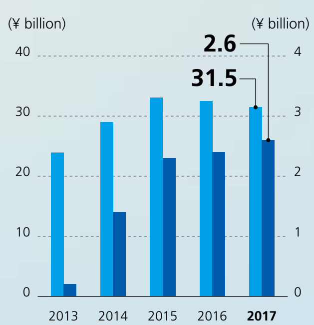
- Fluorocarbons
- Fluoroplastics
- Fluoroelastomers
- Fluoropaints
- Fluoro coating agents
- Semiconductor-etching products
- Water and oil repellent agents
- Pharmaceuticals and intermediates
- Dry air suppliers

Description

In 1933, Daikin was the first in Japan to engage in research on fluorinated refrigerants. Today, our activities range from research and development to commercialization, and we offer a lineup of 1,800 fluorine compounds.

Oil Hydraulics

Net Sales and Operating Income



Major Products

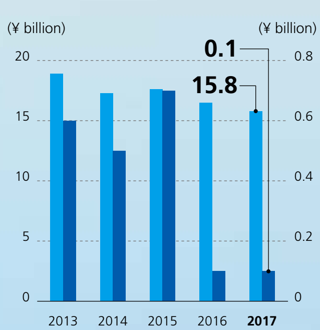
- Oil hydraulic pumps
- Oil hydraulic valves
- Cooling equipment and systems
- Inverter controlled pump motors
- Hydrostatic transmissions
- Centralized lubrication units and systems

Description

Daikin's unique hydraulic technologies offer outstanding energy-conservation performance and are contributing to the development of industry by unleashing the potential of power control.

Defense

Net Sales and Operating Income



Major Products

- Warheads for Japan's Ministry of Defense/ Warhead parts for guided missiles
- Home-use oxygen therapy equipment

Description

Daikin's superior machining and quality control technologies are used in the production of defense-related products and other industries where high levels of precision and performance are critical.

For the success of plan, we will further implement policies of the Group.

In fiscal 2017, we were able to achieve a good performance despite the severe business environment. Maintaining that momentum, we will move forward with the "FUSION 20" priority policies of thoroughly strengthening existing businesses, expanding into new business domains, and transforming our business structure.

June 2017

Masanori Togawa
President and CEO

our "FUSION 20" strategic management strengthen management and steadily leading to new growth and development

In fiscal 2017, the degree of recovery seen varied between countries and regions, but overall the world economy tended to slow, and the business environment was severe due to factors such as the rapid rise of the yen in the first half. Viewing this kind of difficult business environment as a good chance to further strengthen management for the future, Daikin moved ahead with the fundamental reinforcement of sales and marketing capabilities, aggressive introduction of differentiated products, and reduction of total costs. As a result, we were able to greatly raise the level of Group profitability, setting new records for both net sales and income on a consolidated basis for the fourth consecutive year.

Also in fiscal 2017, we started our "FUSION 20" (fiscal 2017 to fiscal 2021) strategic management plan and implemented various policies aimed at new growth and development of the Group.

In our core business of air conditioning, with the goal of becoming a top player in air conditioning in North America, our subsidiary Goodman Global Group, Inc. began full-scale operation of the Daikin Texas Technology Park, which integrates its four factories and two logistics centers. This facility introduced cutting-edge production lines (known as module lines), shortened the production cycle, and introduced a system that can respond immediately to production volume changes. In addition, the utilization of new technology such as AI and IoT has greatly increased production-process efficiency. The start-up of the new factory strengthened our production capacity, cost-competitiveness, and R&D functions, and it enabled us to introduce innovative products not previously seen in the North American market.

In Asia, demand from middle-income classes continues to expand, and, in order to build an organization that can handle the expansion of sales, we are moving forward at a rapid pace with sales network improvements, sales personnel increases, factory expansion, and new factory construction.

We were also able to further strengthen our business bases in filter business and commercial refrigeration business, two areas we are developing as key future income sources. In filter business, we are accelerating efforts to create synergy now that we have acquired Flanders Holdings LLC (of the United States), which is strong in high-performance filters for the pharmaceutical and food industries, and Dinar AB (of Sweden), which manufactures and sells air filters primarily for Northern Europe, the largest filter market in Europe. In commercial refrigeration business, we were able to further expand the range of our European business through the acquisition of Zanotti S.p.A. (of Italy), which is strong in refrigerators and freezers for food distribution.

We have also strengthened our global R&D organization so that we can continue to provide innovative products and services and new value to our customers. We will enhance our Technology and Innovation Center (based in Osaka), which serves as a control tower for global technology and product development and which drives our technology strategy preparation/promotion, differentiated technology search/development, and technical staff acquisition/development, etc. In addition, in order to improve the AI and IoT technology that we need for the coming era, we are establishing a Silicon Valley Technology Office, and we will implement industry-pioneering open innovation strategies, such as actively promoting industry, government, and academia collaboration aimed at merging the technology of different fields.

While the world economy can be expected to expand steadily in fiscal 2018, there is also uncertainty about the future due to factors such as political risk in the United States and Europe and geopolitical risk in the Middle East and Asia. In this operating environment, we will continue to thoroughly strengthen our core business and work to expand into new business domains as specified in our basic strategy "FUSION 20," and we will strive for even greater medium- and long-term growth and development by making forward-looking investments based on careful consideration of priorities.

We look forward to your continuing support and understanding.

For the success of "FUSION 20," Daikin will secure short-term profit, while seeking additional medium- and long-term growth and development through forward-looking investments with carefully defined priorities.

"FUSION 20" proclaimed that Daikin will "Co-Create New Value in the Air and Environment Fields with Wisdom and Passion." Making an all-out effort in pursuit of a number of strategic themes, Daikin will aim for sustainable global growth, while also fulfilling its social responsibilities as a company.

Q1

Could you please review Daikin's fiscal 2017 performance and the progress status of the "FUSION 20" strategic management plan?

Solid results for new growth and development

Togawa: Fiscal 2017 consolidated net sales were ¥2,043,969 million and operating income was ¥230,769 million, so Daikin achieved a record-setting performance for the fourth consecutive year and income and profit increases for the seventh consecutive year. I believe that we were able to further strengthen our management practices by improving our sales and marketing power, by aggressively introducing high-value-added products, and by moving forward with total cost reductions centered in global procurement.

In our main business of air conditioning, we expanded sales in many key regions (Japan, the Americas, China, Asia, and Europe), and in "FUSION 20"'s priority regions of the Americas and Asia, sales (on a local currency basis) grew greatly to 115% and 113% of the previous year's levels, respectively. Along with the strengthening of existing business, using measures that included M&A, Daikin was also able to move forward steadily with another priority strategy, the building of a base for expansion of our business domains and transformation of our business structure.

Looking back at fiscal 2017, for our existing core business and for our new businesses, I feel it was a year in which we achieved solid results in preparing for the new growth and development of the Group.

A pressing management issue at the moment is to, first of all, achieve quantitative targets defined for intermediate points (fiscal 2019 medium-term implementation plan) so that we can realize "FUSION 20." Consequently, for the two years of fiscal 2018 and 2019, Daikin will execute forward-looking investments for the purpose of securing short-term profit while also building an infrastructure for the future.

"FUSION 20" Goals and Medium-term Implementation Plan

Goals (FY2021)

To achieve sales of ¥3.0 trillion and an operating income margin of 12%,
- Enhance existing businesses (AC, Chemicals, Filters)
- Expand new businesses (Heating/Water Heaters, Energy Solutions, Commercial Refrigeration, Next-generation Refrigerants/Gas, IAQ/Air Environment (AE) Engineering)

Medium-term implementation plan for FY2019

(¥ billion)

	FY2017 Result	FY2018 Plan	FY2019 Target
Net sales	2,044.0	2,190.0	2,500.0
Operating income	230.8	243.0	270.0
Operating income margin	11.3%	11.1%	10.8%
FCF (3-year cumulative)	—	—	+270.0
ROE	14.5%	—	13.5%
Exchange rates	USD1=JPY108 EUR1=JPY119 RMB1=JPY16.1	USD1=JPY108 EUR1=JPY118 RMB1=JPY16.0	USD1=JPY110 EUR1=JPY125 RMB1=JPY17.0

Investment plan

- Actively make investments mainly in North America and Asia in prioritized order

Investment plan (3-year cumulative)	FY2017–19
	325.0

Q2

What are the main policies you expect to follow for the forward-looking investments?

Three themes for aggressive forward-looking investments

Togawa: Daikin's forward-looking investments can be divided overall into three main themes.

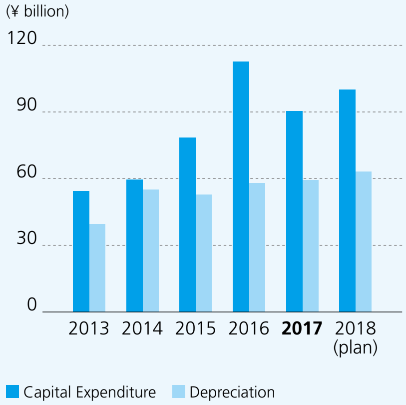
The first theme is to "strengthen the production organization in air-conditioning business." To prepare for further business expansion in the United States, we will build additional production capacity (Daikin Texas Technology Park) at Goodman Global Group, Inc. In Asia, where there is rapidly increasing demand from the growing middle-income classes, we will build a new factory (in Vietnam) and expand existing factories (in Thailand, India, and Malaysia).

The second theme is to "strengthen the global R&D organization." Daikin's main focus here is to further improve underlying technologies and accelerate the development of differentiated products. We will further enhance the functions of our Technology and Innovation Center (TIC) in Osaka, Japan, which serves as the mother facility for global R&D, and we will establish a structure in which the TIC is the technology and product development control tower leading our eight development sites worldwide. In the United States, we are establishing a North American R&D center and a Silicon Valley Technology Office, and we are also working to enhance the applied development center.

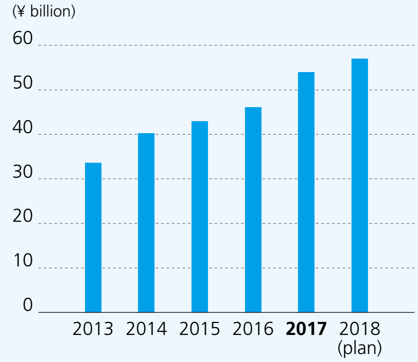
The third theme is to "acquire new technology, such as AI and IoT." To do this, Daikin will accelerate open innovation through the active use of industry, government, and academia collaboration.

Trends in Capital Expenditure, Depreciation, and Research and Development Expenses

Capital Expenditure and Depreciation



Research and Development Expenses



Q3

In the United States, Goodman Global Group, Inc. has begun full-scale operation of the Daikin Texas Technology Park. Please give us an overview.

A productivity increase by approximately 50% over the current level

Togawa: At the Daikin Texas Technology Park, we have introduced a new production line, called the "Module Line," which enables us to flexibly handle demand fluctuations. This line has brought together the best of today's state-of-the-art production technology, including IoT technology and manufacturing know-how accumulated by our Group at production sites worldwide. By the final fiscal year of "FUSION 20," initiatives such as this are expected to increase productivity by about 50% over the current level and also strengthen not only production capacity but also cost-competitiveness. In addition, the new manufacturing know-how and production technology developed by the initiative will raise the productivity of our Group as a whole by being put to good use globally at other new factories now being planned.

Q4

M&A occurred in rapid succession in fiscal 2017. What were the aims of that M&A?

Realizing synergy via business domain expansion

Togawa: In our filter business in fiscal 2017, we acquired the U.S. company Flanders Holdings LLC and the Swedish company Dinar AB. The United States is the world's largest filter market, and Europe is the second largest.

Daikin is seeking to create synergy between these two companies and American Air Filter Company, Inc. (a subsidiary of O.Y.L. INDUSTRIES BHD, which was acquired in 2007) and Nippon Muki Co., Ltd. (acquired in 2009). Our aim is to become the global No. 1 in filter business by having these companies introduce new products that utilize the strengths of each and by raising cost-competitiveness with centralized purchasing and a production system that manufactures products as close to the market as possible.

In our commercial refrigeration business, Daikin acquired the Italian company Zanotti S.p.A. The aim is to expand our business by making mutual use of the sales and service networks of Daikin and Zanotti. There is a high level of environmental awareness in Europe, and customers are looking for the development of refrigerators and freezers that place the smallest possible burden on the environment. We think that incorporating energy-saving technology developed by Daikin for air-conditioning equipment will help expand our business and also be very meaningful as a contribution to society.

In order to expand Daikin's business domains in the future, we will also promote fundamental strengthening measures (M&A and alliances/collaboration with other companies) for our heating business and energy solution business, etc.

Q5

Please give us some background and policy information concerning the need to move quickly in developing and acquiring new technology.

Moving forward aggressively with industry, government, and academia collaboration as well

Togawa: In our air-conditioning business, Daikin did global rollouts of base models developed in Japan, and made adaptations at development sites in each region to handle local needs. However, with changes occurring rapidly in each market, it is critical for Daikin to create differentiated products at a faster pace, and, therefore, it is a pressing need to put in place differentiated technology. At the new Silicon Valley Technology Office mentioned earlier, we will introduce the latest technology (AI, IoT, etc.) at an early stage, and we will also acquire, bolster, and train technical personnel in various fields, including leading-edge fields essential for the coming era.

In addition, in order to lead the industry with an open innovation strategy, we believe that Daikin should move quickly in acquiring new technology by aggressively promoting comprehensive alliances with universities possessing advanced knowledge and by collaborating with leading-edge AI and IoT companies, new business ventures, and the world's top-class research institutions.

Q6

What are your thoughts on returns to shareholders?

Basic policy of using both dividends and enterprise value increases for returns to shareholders

Togawa: Under "FUSION 20," Daikin will further strengthen its position in its core business, and it will concentrate management resources in clearly defined priority areas, such as boldly taking up the challenge of entering new businesses. For future growth and development, there are many themes that we will work on, and in fiscal 2018 we are planning capital investment of ¥100 billion and R&D expenses of ¥57 billion. For total investment (capital investment and loans and other investments) over the three years from fiscal 2017 to 2019, the initial plan was ¥325 billion. We expect to exceed that number, but we will also continue to thoroughly strengthen our financial position with measures such as reducing interest-bearing liabilities and increasing the efficiency of working capital. Through this combination of offense and defense, Daikin will work both to achieve "FUSION 20" goals and to further enhance its enterprise value and returns to shareholders.

In view of its favorable performance, in fiscal 2017, Daikin paid a ¥60 interim dividend and a ¥70 final dividend for an annual total of ¥130 per share, which is ¥10 higher than in the previous fiscal year. We plan to pay a total dividend of ¥130 per share for fiscal 2018 (a ¥65 interim dividend and a ¥65 final dividend).

Under a policy of paying dividends on a steady and continuing basis, Daikin will work to maintain its consolidated ratio of dividends on equity (DOE) at a level of 3.0%, while also seeking to further increase its consolidated dividend payout ratio.

Q7

Please tell us your thoughts on CSR and give us a message for stakeholders.

Contribute to the sustainable development of society through environmental protection, compliance, and symbiosis with regional societies

Togawa: Daikin's core business of air conditioning is already indispensable to society's infrastructure. On the other hand, we are also aware that restraining the impact on global warming by reducing air-conditioning power consumption is the social issue that we should give the most attention. We are promoting the spread of the use of air conditioners utilizing R32 refrigerant, which has a lower impact on global warming than other refrigerants, and we are also working to expand global sales of inverter air conditioners, which have higher energy conservation performance. Combined, these initiatives succeeded in reducing fiscal 2017 CO_2 emissions by approximately 45 million tons. Throughout the world, and especially in emerging countries, the use of air conditioners will increase, but Daikin will intensify its efforts to reduce emissions, with a CO_2 emission reduction target of 60 million tons for fiscal 2021.

Daikin supports the United Nations Global Compact, which sets forth 10 principles concerning the four areas of human rights, labor, the environment, and anti-corruption. As we expand our business globally, Daikin will, of course, act in accordance with the laws and ordinances of each country as well as international norms, and we will also maintain high levels of transparency, soundness, and ethics, with the value chain as a whole taken into account.

In addition, at Daikin, the identification of concerns and expectations via a dialogue with stakeholders (i.e., stakeholder engagement) is considered as an important foundation for CSR, and we put into practice management that contributes to the development of all parties involved through symbiosis with each region.

Using atmosphere- and environment-related technology to both solve problems of society and expand our business, Daikin will contribute to the sustainable development of global society. We hope you will look forward to our future progress under "FUSION 20" as we will work to create new value for the atmosphere and the natural environment.

June 2017

Masanori Togawa

Masanori Togawa
President and CEO

Air Conditioning

Current

Record high results on global sales expansion despite negative impact from the strong yen

Net sales in the air-conditioning equipment business rose slightly during fiscal 2017 from the previous fiscal year, with expanded sales in major regions offsetting the negative impact from the strong yen.

Expanded residential unitary lineup of high-efficiency products with inverters

Japan

Sales in Japan rose 4% year on year amid increased industry demand for both residential and commercial units for replacements and upgrades to more energy-efficient systems, as well as the heat wave in western Japan. Daikin achieved record high revenue and earnings on efforts to expand sales of high-value-added products, including the residential Urusara 7 model and commercial FIVE STAR ZEAS system using the R32 refrigerant, as well as variable refrigerant volume (VRV) units for buildings in cold regions.

Americas

Sales in the Americas rose 3% year on year. In a favorable business climate supported by firm consumer spending, Daikin strengthened its sales network, and achieved year-on-year gains in unit sales volume and market share for its mainstay unitary products, both high-volume zone and high-efficiency units. In the growing ductless market, Daikin strengthened relationships with architectural firms and contractors, expanding sales of new VRV products for the high-end, residential-use market. Sales of applied units (commercial-use large-scale air conditioners) also rose from the previous fiscal year on continued efforts to strengthen the sales and service network.

Expanded sales of Urusara 7 products with excellent energy-saving and environmental performance to differentiate from competitors and provide high added value

Daikin PROSHOP specialist retailers provide one-stop solutions, including design, installation, and after-services.

Expanding sales in the growing market of Asia

China

Sales in China declined 5% from the previous fiscal year, but operating income rose due to cost reduction efforts. In residential-use air conditioners, Daikin leveraged the solutions and construction capabilities of its retail/consumer-oriented PROSHOPs to expand sales in the mid- to high-end market, mainly the "New Life Multi Series" residential multi-air units designed to meet varied customer lifestyles. In the commercial-use market, Daikin enhanced its solutions capabilities with a new VRV model, and appealed to architectural firms with further built-in specifications. Sales of applied units increased despite the slowdown in large-scale real estate investment, mainly for small and mid-sized projects due to an expanded product lineup, and strengthened service business.

Europe

Sales in Europe were on a par with the previous fiscal year. In residential-use air conditioners, sales of high-value-added products using the R32 refrigerant increased amid demand growth since the 2015 heat wave. In the commercial-use market, unit sales volume increased as a result of efforts to strengthen sales capabilities by country, and capturing renewal demand with the launch of new VRV products to meet regional needs. In the heater business, sales of heat pump-type water heating units rose in Germany and Italy, with increased sales of combustion heaters (gas boilers) in Turkey.

Asia/Oceania

Sales in the Asia/Oceania region were on a par with the previous fiscal year. In residential-use air conditioners, sales were firm for inverter air conditioners with exceptional energy efficiency. In the commercial-use market, Daikin gained positive results from enhanced efforts for built-in specifications in VRVs, and development of sales offices. Sales growth was particularly high in Vietnam, India, Indonesia, and Thailand for both residential and commercial air conditioners. In Australia, sales expanded for high-end, residential-use VRV units.

Future

Proactive up-front investments mainly in North America and Asia to drive further business expansion

Daikin anticipates revenue and earnings gains in fiscal 2018 as a result of global sales expansion, comprehensive cost reductions, and sales price strategies, offsetting a substantial negative impact from higher material costs.

Shifting production into full gear at our new U.S. plant to aim for further business expansion

Japan

Daikin will work to increase earnings through expanded sales of high-value-added products and comprehensive pricing strategies, as well as fundamentally strengthening sales capabilities by market and sales channel. For residential-use air conditioners, Daikin will increase sales of its uniquely differentiated products, such as the Urusara 7 and multi-air conditioners that offer superior design. In the commercial market, Daikin will work to expand sales of high-value-added systems, and establish eco-related businesses such as inspection services for compliance with CFC emissions regulations. For applied units, Daikin will seek to capture redevelopment demand in the Tokyo metropolitan area ahead of the 2020 Tokyo Olympics, and increase its market share.

Americas

With stable market growth expected as a result of firm consumer spending and capital investment, Daikin will accelerate measures to strengthen competitiveness and expand its business, including enhancing cost-competitiveness with the start of full-fledged operations of its new production plan, developing region-specific products around expanded R&D functions, and building its own wholesale base.

Building a recycling-oriented business that goes beyond simple device sales

Enhancing our ability to supply products to meet increasing middle-class demand

Expanding our business to include commercial freezers and refrigerators

China

Daikin will expand its network of retail and consumer-oriented shops, including the PROSHOPs that handle residential multi-air conditioners, from urban areas to regional cities, and accelerate community-oriented sales activities. For residential-use air conditioners, Daikin will expand its "New Life Multi Series" lineup, and implement new measures such as opening interactive showrooms. In the commercial market, Daikin will launch new energy-efficient variable refrigerant volume (VRV) units, and new types of applied units. Further, Daikin aims to increase profits by increasing the ratio of units made in-house, expanding the number of units procured locally, accelerating cost reduction efforts, and shifting to integrated development, production, sales, and service.

Europe

With demand for air conditioning expected to expand at a moderate pace on the back of firm consumer spending, Daikin will work to increase sales by launching differentiated products utilizing the R32 refrigerant, and strengthening its sales network. In the heater business, Daikin will introduce new types of highly energy-efficient, heat pump-type water heating units, and expand sales of combustion heaters (gas boilers). In the commercial freezer and refrigerator business, Daikin will seek to maximize synergistic benefits with the recently acquired firm Zanotti S.p.A. of Italy.

Asia/Oceania

With demand for air conditioning expected to expand significantly among the growing middle-income classes, Daikin will continue to strengthen its national sales networks and increase the number of sales personnel. In India and Thailand, Daikin will enhance its supply capacity to increase sales. In terms of products, Daikin will strengthen its lineup of air-conditioning inverters, and launch new residential multi-air units to meet the needs of middle-class consumers in Vietnam and Thailand. In the commercial market, Daikin will launch differentiated products such as cooling VRV units in India. For applied units, Daikin will establish a foundation for business expansion by strengthening local production structures, enhancing product lineups, and developing service businesses.

Current

Sales expansion in growth markets and comprehensive cost reductions

Net sales in the Chemicals business during fiscal 2017 declined 3.4% from the previous fiscal year. Despite efforts to expand sales in well-performing sectors, such as fluoroplastics resins for use in semiconductors, fluoroelastomers for automotive applications, and anti-smudge surface coating agents for smartphone touch screens, results were adversely affected by price pressure from competitors in China and the United States, and the negative impact from the strong yen.

In the fluorocarbon gas business, overall sales of refrigerant gas rose from the previous fiscal year on higher sales to the after-sales market in the United States.

In the fluoroplastics resin business, Daikin captured semiconductor-related demand in Japan and the rest of Asia, but overall sales declined as a result of intensifying competition in the U.S. LAN cable market and downward price pressure on commodities in China.

In the fluoroelastomer business, despite a recovery in sales for automotive applications, mainly in Japan and China, overall sales declined as a result of the considerable negative impact from the strong yen.

In the chemical products business, sales of the OPTOOL™ anti-smudge surface coating agent for smartphones were favorable as Daikin captured positive demand in China, but overall sales declined as a result of a slowdown in water and oil repellent agents.

Anti-smudge surface coating agent for smartphones

Future

Revenue and earnings growth expected from the strengthening of sales capacity, new product launches, and application development

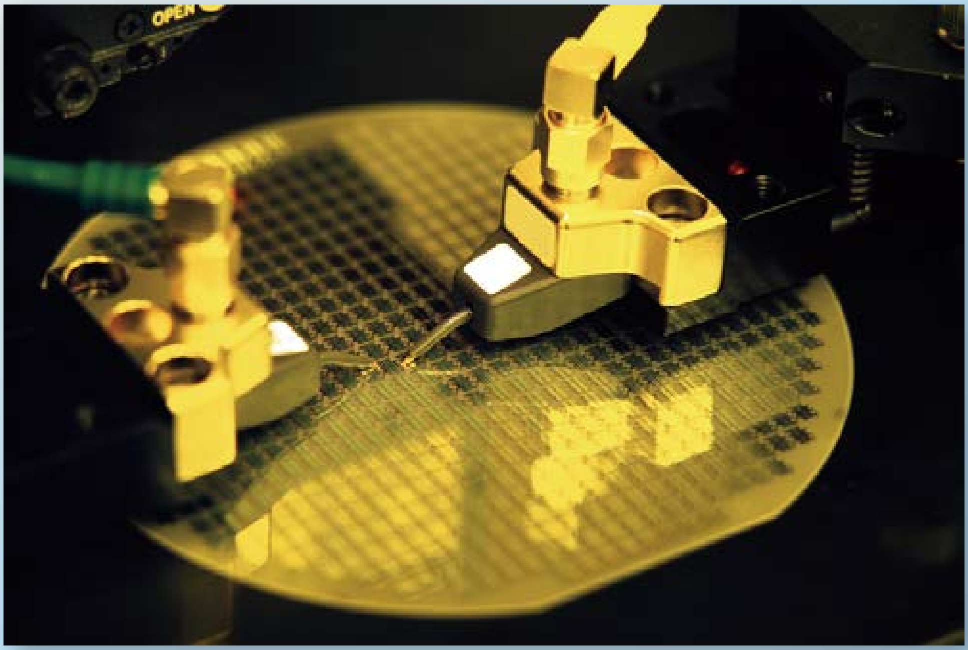
Daikin anticipates a sales increase of 5% in its Chemicals business in fiscal 2018.

Although orders from major customers for the OPTOOL™ anti-smudge surface coating agent are expected to decline, this will be offset by expanded sales of fluoroplastics resin in the continually favorable semiconductor market, a regaining of market share with the launch of new water and oil repellents, and application development tailored to customer needs.

In the semiconductor market in particular, Daikin will capture growing demand from the utilization of the Internet of Things (IoT), strengthen its supply capacity, and promote built-in specifications with the aim of increasing market share.

Concentrating on the United States, the largest market for air conditioning, Daikin will focus on after-sales businesses such as the recovery and recycling of refrigerant gas, and establish a recycling-oriented business encompassing the life cycle of refrigerants and air-conditioning equipment.

Further, in Asian markets where demand for fluorochemicals products is growing, Daikin will conduct detailed marketing and sales activities by industry sector.



Highly chemically resistant fluoroplastics products are essential for semiconductor manufacturing equipment.

Oil Hydraulics

Current

Steady sales and record earnings amid sluggish demand in Japan and China

Oil cooling units adopting energy-saving technology

The oil hydraulics business comprises a range of oil hydraulic equipment to support the smooth movement of various types of machinery, contributing to energy efficiency and electricity savings. Daikin units are used mainly in industrial machinery such as factory processing equipment, construction equipment such as power shovels, and small vehicles such as tractors.

Net sales in the oil hydraulics business declined in fiscal 2017 from the previous fiscal year. Sales of oil hydraulic equipment for construction equipment and vehicles increased to major customers in Japan and the United States, but performance was significantly impacted by a slowdown in demand for products for industrial equipment in Japan and China.

Future

Strengthen the business foundation in the United States and Europe, and accelerate global business expansion

Hydraulic devices to drive construction machinery and automobiles

During fiscal 2018, Daikin will focus on launching new products and strengthening solutions-oriented sales capabilities in order to further strengthen its position in the Japanese market for oil hydraulic equipment used in industrial machinery. Outside Japan, mainly in the United States, Daikin will strengthen the foundations for the maintenance, repair, and operation (MRO) and hydrostatic transmissions (HST) businesses, and accelerate expansion of both businesses. Europe is also being positioned as a priority market, with comprehensive marketing activities conducted in a rapid manner to facilitate full-scale market entry. Daikin will also further strengthen its service structure in Japan and overseas.

Defense

Current

Steady sales of home-use oxygen therapy equipment, mainly in Japan

Daikin designs and manufactures products for Japan's Ministry of Defense based on the defense budget, including various types of artillery shells, warheads, and fuses, as well as aircraft parts. These precision processing technologies are also leveraged for private-sector purposes, including the manufacture and sale of home-use oxygen therapy equipment. Daikin provides patients suffering from chronic respiratory failure with respiration synchronizers and oxygen concentrators, products that require the highest levels of precision, performance, functionality, and quality.

Net sales in this segment declined from the previous fiscal year. Sales of home-use oxygen therapy equipment increased in Japan, but sales of practice ammunition to the Ministry of Defense declined.

Future

Accelerate business expansion in the private sector

With the Japanese government scaling back orders for practice ammunition, Daikin will accelerate its shift to the private sector. In Japan, Daikin will expand sales of the new oxygen concentrator launched at the end of the previous fiscal year. In the Chinese market, Daikin will collaborate with local firms to enhance its sales capabilities, and strengthen product solutions and cost-competitiveness, including the possibility of supplying OEM products.

Corporate Governance

Basic Policy of Corporate Governance

Through its corporate governance, the Daikin Group works to raise corporate value by carrying out its decision making with foresight and by executing business with increasingly greater speed, transparency, and soundness, all in line with Group management challenges and the changing business environment.

Aiming for management with even greater speed, soundness, and transparency, we will continue to boost corporate value by seeking and implementing new ways to achieve optimal corporate governance as we undertake best practices in all facets and at all levels of the Daikin Group.

Regarding Japan's Corporate Governance Code, Daikin has already implemented the principles of "enhancing information disclosure," "making effective use of independent external directors," and "the policy of having constructive dialogue with shareholders." Going forward, Daikin will continue to enhance these initiatives.

Management and Operational Execution Systems

Rather than adopting a U.S.-style "committees system" that completely separates decision making from operational execution, the Daikin Group has adopted an "integrated management" system, in view of the special characteristics of the Group's business, judging that this is a more-effective means of accelerating decision making and operational execution. The "integrated management" system is a system that calls for directors to bear responsibility for management duties as well as for operational execution duties through speedy, strategic decision making and sound, appropriate supervision and guidance. Directors also bear responsibility for the execution and completion of their decisions by carrying out their decision making, business execution, and supervision/guidance in an "integrated" manner.

Daikin also appoints multiple external boards of directors who monitor the Group's business execution status from an independent standpoint and gives appropriate guidance and advice on decision making, and are responsible for supporting the "integrated management" system in terms of transparency and sound management. In addition, the Group has introduced an "executive officer system" to accelerate the speed of execution based on autonomous judgments and directions in units handling each region, division, and function.

The Group appoints directors, while giving emphasis to the diversity of directors' backgrounds regarding characteristics such as nationality, gender, and career history.

As of the end of June 2017, there were 11 directors (including one female and one non-Japanese director), ensuring practical and prompt debate through a smaller number.

Daikin's Board of Directors includes three external directors (as of June 2017), conditional upon their being free of any conflict of interest.

Daikin seeks to recruit external directors who can provide supervision and advice from a sophisticated perspective on a broad range of issues, based on their abundant experience and deep insight. Accordingly, we nominate external directors with primarily director and similar experiences in listed companies. None of Daikin's external directors have five or more concurrent posts.

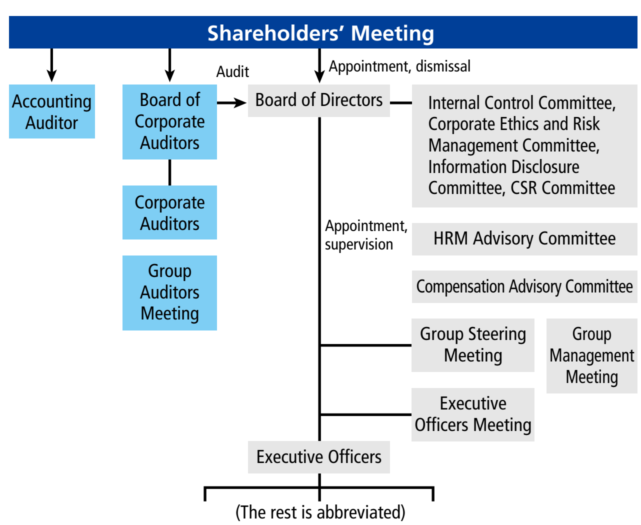
To ensure that the external directors can effectively contribute to Daikin's corporate governance system, assistants to the external directors are assigned in the Management Planning Office. They strive to provide the external directors with Daikin-related information, early notice of Board of Directors meetings, and prior notice of Board of Directors meeting agenda items, as well as implementing prior explanations of particularly important agenda items. In addition, when external directors are unable to attend a Board of Directors meeting, the assistants provide them with related materials and subsequent explanations of meeting proceedings.

Audit System

Daikin employs an Audit and Supervisory Board System. As of June 2017, Daikin's four Audit and Supervisory Board members included two external Audit and Supervisory Board members. The principal nomination criteria for external Audit and Supervisory Board members are the same as those for external directors and include independence from the Company in terms of not having a relationship of interest with the Company.

The Audit and Supervisory Board members attend meetings of the Board of Directors, as well as other important meetings, and receive reports. In addition, they are able to express diverse opinions.

To ensure effective audit functions, the Audit and Supervisory Board receives reports on important issues related to management and performance when necessary and also investigates relevant units, confirms approval of documents, and regularly exchanges opinions with representative directors, executive officers, and the independent auditors. In addition, the Audit and Supervisory Board Member Office has been established to assist the auditors, with the staff performing their duties under the orders and direction of the Audit and Supervisory Board members. The opinions of the Audit and Supervisory Board are respected with regard to personnel transfers, work evaluations, and other matters pertaining to Audit and Supervisory Board Member Office staff members.



External Director/Audit and Supervisory Board Members' Principal Activities

Name	Position	Principal Activities
Chiyono Terada	External Director	Ms. Terada attended 16 of the 16 Board of Directors meetings held during the fiscal year. Based on her abundant experience and deep insight as a corporate manager, she provides appropriate supervision of Company management from an independent perspective; advises management from the consumers' point of view, including the importance of the Company's corporate brand; and makes proactive proposals for measures to further promote achievements of female employees.
Tatsuo Kawada		Mr. Kawada attended 12 of the 13 Board of Directors meetings held during the fiscal year. Based on his abundant experience in management and high-level insight, he is able to provide appropriate supervision of management from an independent perspective and actively provides suggestions, from his broad and sophisticated perspective regarding changes in business models, innovation, and other matters.
Akiji Makino		Mr. Makino attended 13 of the 13 Board of Directors meetings held during the fiscal year. Based on his abundant experience in management and high-level insight, he is able to provide appropriate supervision of the Company's management from an independent perspective and actively provides suggestions from his broad and sophisticated perspective regarding matters in the fields of energy, the natural environment, and service businesses.
Ryu Yano	External Audit and Supervisory Board Member	Mr. Yano attended 12 of the 16 Board of Directors meetings held during the fiscal year as well as 13 of the 15 Board of Auditors meetings held. Based on his abundant experience and deep insight as a corporate manager, he accurately audits the supervision of the conduct of management by the directors. From his broad and advanced perspective developed over many years of experience overseas, he makes necessary statements in a timely fashion.
Toru Nagashima		Mr. Nagashima attended 13 of the 13 Board of Directors meetings held and 10 of the 10 Board of Auditors meetings held during the fiscal year. Based on his abundant experience in management and high-level insight, he makes necessary statements in a timely fashion based especially on his broad and sophisticated experience in the management of global companies and manufacturing enterprises.

Reasons for Election as External Director/Audit and Supervisory Board Member

Name	Position	Reasons for Election
Chiyono Terada	External Director	Ms. Terada has abundant experience and deep insight as a corporate manager, and, drawing on her background, she provides appropriate supervision from an independent perspective. She has an excellent understanding of the consumers' perspective, including the importance of the corporate brand, and makes proactive proposals for measures to further promote achievements of female employees. The Company management wants Ms. Terada to continue to contribute to the Company's corporate value looking forward and, therefore, was elected as external director.
Tatsuo Kawada		Mr. Kawada has served as representative director of SEIREN CO., LTD., and has abundant experience and deep insight as a corporate manager. His experience includes changing his company's business model, innovation creation, and reforming corporate cultures. The Company management wants Mr. Kawada to provide appropriate supervision of the conduct of management from an independent perspective, and, by offering proposals regarding management from his broad and high-level perspective, contribute to increasing Daikin's corporate value. He has, therefore, been elected as external director.
Akiji Makino		Mr. Makino has served as representative director of Iwatani Corporation and has abundant experience and deep insight as a corporate manager, especially in the fields of energy and the natural environment as well as the services business. The Company management wants Mr. Makino to draw on his background and experience to provide appropriate supervision of the conduct of management from an independent point of view, and, offering proposals regarding management from his broad and high-level perspective, contribute to increasing Daikin's corporate value. He has, therefore, been elected as external director.
Ryu Yano	External Audit and Supervisory Board Member	Mr. Yano has served as representative director at Sumitomo Forestry Co., Ltd., and has abundant experience and deep insight as a corporate manager, particularly in the field of expanding business operations overseas. The Company management wants Mr. Yano to draw on his experience to supervise overall management and to significantly upgrade the appropriateness of the audit function. He has, therefore, been elected as external auditor.
Toru Nagashima		Mr. Nagashima has served as representative director at TEIJIN LIMITED, and has abundant experience and deep insight as a corporate manager, particularly in the field of implementing paradigm shifts from manufacturing to services. The Company management wants Mr. Nagashima to draw on his experience to significantly upgrade the appropriateness of the audit function. He has, therefore, been elected as external auditor.

Note: All of the Company's external directors and external auditors meet the qualifications for independence established by the Tokyo Stock Exchange.

Agile Management Support System

Daikin has three main management bodies—the Board of Directors, the Group Steering Meeting, and the Executive Officers Meeting—which minimize the number of directors and ensures speedy decision making based on the virtual discussion.

The Board of Directors is the decision-making institution for all matters related to the Group as a whole that are stipulated by laws and regulations and by the articles of incorporation, and it also performs supervision and guidance to ensure sound and appropriate operational execution. The Board of Directors appropriately makes decisions based on open and active discussions and performs an effective role in increasing corporate value over the medium-to-long term. They also perform self-evaluation on the effectiveness of the Board of Directors on a regular basis. In fiscal 2017, it met 16 times, and the average attendance rates of external directors and external Audit and Supervisory Board members at those meetings were 98% and 88%, respectively.

The top deliberative unit in the Group's management system is the Group Steering Meeting. This unit determines the direction of important management policies and strategies in a rapid and timely manner, thereby accelerating the resolution of issues. In fiscal 2017, it met 12 times.

In principle, all of the Executive Officers attend the Executive Officers Meeting, and it met 11 times in fiscal 2017.

In addition, to respect and protect the interests of diverse stakeholders other than stockholders, Daikin has, based on the Board of Directors, established its Internal Control Committee, Corporate Ethics and Risk Management Committee, Information Disclosure Committee, and CSR Committee.

Corporate Officer Remuneration, Etc.

To ensure the transparent management of its corporate officer personnel and remuneration processes, Daikin has established the HRM Advisory Committee and the Compensation Advisory Committee. These committees engage in discussions and deliberations regarding issues including corporate officer nomination criteria, corporate officer candidates, and remuneration. As of the end of June 2017, the committees consist of five members, including three external directors, one in-house director, and one executive officer, with the committee chairman being chosen from the external directors.

The remuneration of directors and Audit and Supervisory Board members is determined so as to fall within the aggregate remuneration ceiling for directors and Audit and Supervisory Board members as set by a resolution at the general shareholders' meeting. Based on a report from the Compensation Advisory Committee, the directors' remuneration is determined by a resolution of the Board of Directors, while the Audit and Supervisory Board members' remuneration is determined by a resolution of the Audit and Supervisory Board.

Directors' remuneration consists of "fixed compensation," "performance-linked compensation" that reflects the Group's short-term performance (net sales and operating income) and each director's job responsibilities, and "stock options" that reflect the Group's medium- to long-term performance. The remuneration of external directors and corporate auditors consists of "fixed compensation" only.

Compensation levels are determined based on consideration of Daikin's performance and remuneration levels compared to those of other leading manufacturing companies in Japan after analyzing and comparing data from an outside specialized institution on the remuneration of corporate officers active in approximately 200 Japanese companies listed on the First Section of the Tokyo Stock Exchange. In addition, responding to shareholders' expectations, in order to maintain the motivation of in-house directors at a high level continuously over the medium-to-long term towards enhancing the Daikin Group's performance and corporate value, the performance-linked compensation of such directors is given at a somewhat higher ratio than average to ensure the incentive is sufficient.

Total Compensation for Directors and Audit and Supervisory Board Members (Fiscal 2017)

Position	Total Compensation (Millions of yen)	Total Compensation by Type (Millions of yen)			Number of Individuals
		Basic	Stock Options	Bonus	
Directors (excluding external directors)	1,220	750	120	350	11
Audit and Supervisory Board Members (excluding external directors)	66	66	—	—	2
External Directors	70	70	—	—	7

Corporate Officers Receiving Total Compensation and Other Exceeding ¥100 Million (Fiscal 2017)

Name	Total Consolidated Compensation (Millions of yen)	Position	Company Name	Total Consolidated Compensation by Type (Millions of yen)		
				Basic	Stock Options	Bonus
Noriyuki Inoue	380	Director	Daikin Industries, Ltd.	245	26	107
Masanori Togawa	250	Director	Daikin Industries, Ltd.	153	26	70
Ken Tayano	176	Director	Daikin Industries, Ltd.	108	13	43
		Chairman	Consolidated Subsidiary, Daikin (China) Investment Co., Ltd.	10	—	—
Masatsugu Minaka	121	Director	Daikin Industries, Ltd.	7	13	34
		Director	Consolidated Subsidiary, Daikin Europe N.V.	66	—	—
Jiro Tomita	131	Director	Daikin Industries, Ltd.	79	13	38
Takashi Matsuzaki	108	Director	Daikin Industries, Ltd.	65	11	31

Total Compensation and Other for Independent Accounting Auditors (Fiscal 2017)

Audit expense	209 (Millions of yen)

Group Governance

To meet governance needs on a Group basis including M&A-related Group companies, Daikin holds meetings of the Group Steering Meeting. By working to thoroughly ensure that all Group units share the Group's important management policies and basic strategy and by endeavoring to promote and strengthen support for the resolutions of challenges of Group companies, the Group Steering Meeting seeks to make the Group undertake corporate activities based on unified objectives. Principal Group companies appoint Group auditors to participate in Group Auditors' meetings, which seek to strengthen Groupwide auditing and auditing functions by undertaking activities to strengthen the operation of those functions.

To further strengthen corporate governance and Group management as a multinational company, Daikin has appointed a Chief Global Group Officer, who endeavors to further improve the Group's cohesiveness.

Directors, Audit and Supervisory Board Members, and Executive Officers (As of June 29, 2017)

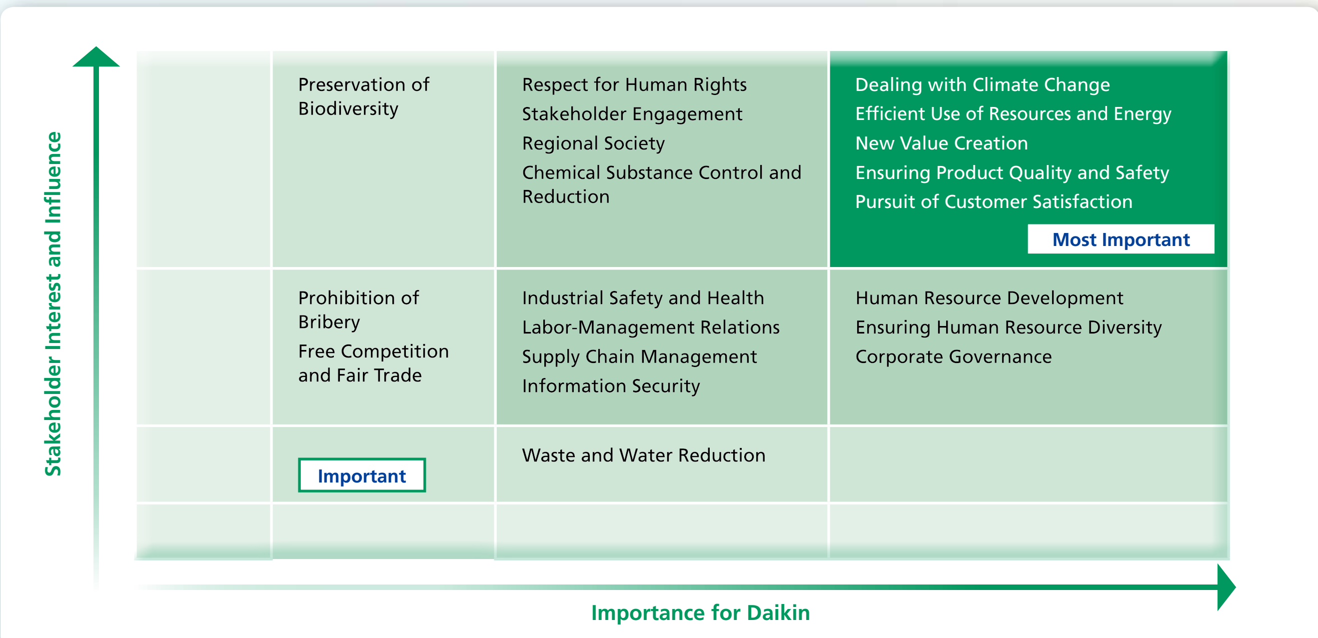
Position(s)	Name	Responsibilities & Principal Jobs
Chairman of the Board and Chief Global Group Officer	**Noriyuki Inoue**	
President and CEO, Member of the Board	**Masanori Togawa**	Chairman of Internal Control Committee
Member of the Board (external)	**Chiyono Terada**	President of Art Corporation
Member of the Board (external)	**Tatsuo Kawada**	Chairman and CEO of SEIREN CO., LTD.
Member of the Board (external)	**Akiji Makino**	Chairman and CEO at Iwatani Corporation
Member of the Board and Senior Executive Officer	**Ken Tayano**	Responsible for Domestic Air-Conditioning Business, Representative of China Region, Chairman and President of Daikin (China) Investment Co., Ltd., Chairman of Daikin Fluorochemicals (China) Co., Ltd., and Member of Global Air-Conditioning Committee
Member of the Board and Senior Executive Officer	**Masatsugu Minaka**	Representative of Air-Conditioning Operations in the Europe/Middle East/Africa Region, President of Daikin Europe N.V., and Member of Global Air-Conditioning Committee
Member of the Board and Senior Executive Officer	**Jiro Tomita**	Responsible for Global Operations Division, Manufacturing Technology and Promoting PD Alliances
Member of the Board and Senior Executive Officer	**Takashi Matsuzaki**	Responsible for North America Research and Development and Applied R&D Center and General Manager of Silicon Valley Technology Office
Member of the Board and Senior Executive Officer	**Koichi Takahashi**	Responsible for Accounting, Finance, Budget Operations and IT Development, General Manager of the Finance and Accounting Division
Member of the Board (non-resident)	**Yuan Fang**	Regional General Manager of Air-Conditioning Business in emerging nations in the ASEAN and Oceania Regions of Global Operations Division, Vice Chairman and Vice President of Daikin (China) Investment Co., Ltd., Chairman of Daikin Airconditioning (Hong Kong) Limited
Audit and Supervisory Board Member (external)	**Ryu Yano**	Chairman of the Board of Sumitomo Forestry Co., Ltd.
Audit and Supervisory Board Member (external)	**Toru Nagashima**	Advisor of TEIJIN LIMITED
Audit and Supervisory Board Member	**Kenji Fukunaga**	
Audit and Supervisory Board Member	**Kosei Uematsu**	
Senior Executive Officer	**Junichi Sato**	Representative of Air-Conditioning Operations in Central America and South America (including American Air Filter) and Member of Global Air-Conditioning Committee
Senior Executive Officer	**Yukio Hayashi**	Responsible for Liaison Business and Defense Systems Business and General Manager of Tokyo Office
Senior Executive Officer	**Shigeki Hagiwara**	Responsible for Applied Solution Business, Service Operations and Training
Senior Executive Officer	**Yoshikazu Tayama**	General Manager of Budget and Administration Group, Finance and Accounting Division
Senior Executive Officer	**Masayuki Moriyama**	Responsible for Applied Solution Business in China, ASEAN and Oceania Regions, Director and Vice President of Daikin (China) Investment Co., Ltd., COO of McQuay China
Senior Executive Officer	**Yoshihiro Mineno**	General Manager of Global Operations Division, Director (non-resident) of Goodman Global Group, Inc., Director of Daikin Holdings (Houston), Inc.
Senior Executive Officer	**Satoshi Funada**	General Manager of Air-Conditioning Sales Division
Senior Executive Officer	**Yasushi Yamada**	Responsible for Safety
Executive Officer	**Katsuyuki Sawai**	Responsible for Corporate Communication, Human Resources, and General Affairs and General Manager of Shiga Plant
Executive Officer	**Hitoshi Jinno**	Responsible for PL/Quality, Air-Conditioning/Applied/Refrigeration, Responsible for Alliance Promotion with Gree Electric Appliances Inc., General Manager of Air-Conditioning Manufacturing Division, and General Manager of Sakai Plant
Executive Officer	**Kota Miyazumi**	Responsible for Corporate Planning, General Manager of Marketing Research Division, Director of Planning Group in Marketing Research Division
Executive Officer	**Tsutomu Morimoto**	Responsible for Executive Secretarial Department, Goodman Group Business
Executive Officer	**Yuji Yoneda**	Responsible for Air-Conditioning Research and Development (including Applied Solution Business and Refrigeration Business) and General Manager of Technology and Innovation Center
Executive Officer	**Masaki Saji**	General Manager of Human Resources Division and Department Manager of Diversity Promotion Group
Executive Officer	**Masafumi Yamamoto**	Responsible for CSR, Global Environment Affairs, Corporate Ethics, Compliance, Legal Affairs, General Manager of the Legal Affairs, Compliance and Intellectual Property Center, Chairman of CSR Committee, Chairman of Corporate Ethics and Risk Management Committee and Chairman of Information Disclosure Committee
Executive Officer	**Makio Takeuchi**	Responsible for Global Procurement, Deputy Manager of Air-Conditioning Manufacturing Division (Research and Development), Responsible for Refrigeration Division, Research and Development, Co-Creation Projects member of Technology and Innovation Center
Executive Officer	**Yoshiyuki Hiraga**	Responsible for Chemical Business and Chemical Environment/Safety
Executive Officer	**Toshio Ashida**	General Manager of Corporate Planning

ESG Summary

The Daikin Group's core business of air conditioning is essential for economic development and a comfortable lifestyle, and demand for air conditioning continues to expand in developing nations and around the world. As an industry-leading specialized manufacturer, the Daikin Group sets CSR priority themes for the sustainable development of society. By evaluating the overall impact on society, Daikin provides people around the world with comfortable and rich lifestyles, while working to limit environmental impact by leveraging its accumulated technologies.

Materiality

In fiscal 2016, along with the establishment of a strategic management plan known as "FUSION 20," the Group's relevance has been evaluated. In the course of this evaluation, priority themes were selected according to two core topics: "The interests of stakeholders and what impacts on them," which includes stakeholder engagement and global guidelines and requirements from the SRI research institution, and the "Importance of Daikin" based on management philosophy as well as mid-and-long-term management strategies.



Nine Priority Initiatives

With the Group's relevance established as the CSR priority for sustainable development of both the corporation and society, the Group has focused on four "Value Delivery" themes and five "Grounding" themes. Attention to these initiatives in management activities is incorporated into our strategic management plan, "FUSION 20."

Daikin Group CSR

CSR for Value Provision	
We aim to provide a healthy, comfortable air environment to all across the world, through efforts to minimize environmental impact.	● Environment ● New Value Creation ● Customer Satisfaction ● Human Resources

Fundamental CSR	
We are responding to societal demands for greater transparency and more open business practices.	● Corporate Governance ● Respect for Human Rights ● Supply Chain Management ● Stakeholder Engagement ● Communities

ESG Positioning/Objectives

Environmental (E)

Environment p. 24

Introduce state-of-the-art technologies to the market in order to address environmental and energy issues

- Promote spread of the use of environmentally friendly products worldwide

Through the global spread of environmentally friendly products, reduce greenhouse gas emissions by 60 million tons of CO_2 in fiscal 2021

- By fiscal 2021, reduce the Group's production-time greenhouse gas emissions to one-fourth of the fiscal 2006 level (75% reduction)
- Implement and expand environmental activities carried out in collaboration with stakeholders

Social (S)

New Value Creation p. 25

Share dreams and ambitions inside and outside Daikin to realize a healthy, comfortable lifestyle through air

- Provide value to the Earth
- Provide value to cities
- Provide value for people's health and comfort

Customer Satisfaction p. 26

Provide peace of mind and reliability through a focus on customer orientation, experience, performance, and advanced technologies

- Build a service network covering the entire globe
- Build product development capabilities that can satisfy customer needs worldwide
- Achieve the optimum level of quality

Human Resources p. 27

Respect individual personalities and values, and maximize the potential of each employee

- Maintain and expand hiring
- Build an organization in which employees with diverse characteristics can each work with energy and motivation and can each grow in a way that maximizes their potential

Respect for Human Rights p. 29

Taking into account the laws and regulations of each country and region, understand the diverse international standards concerning human rights and respect basic human rights

Supply Chain Management p. 29

Understand Daikin's social responsibility as encompassing the entire supply chain, not just the environmental burden, quality assurance, and labor safety and health within the Group

Stakeholder Engagement/Regional Society p. 30

Develop strong bonds with local communities as a member of the regional society operating a business while respecting the culture and history of each country and region

Governance (G)

Corporate Governance p. 18

Accelerate decision making and execution with respect to management tasks and the management environment while at the same time promoting higher levels of transparency and soundness, thereby seeking to increase corporate value

Environment

A priority task for us is to contribute to the resolution of environmental and energy problems by bringing leading-edge technologies together with markets. By promoting the spread of environmentally friendly products, in fiscal 2017 we reduced greenhouse gas emissions by 45 million tons of CO_2, and our sales ratio for environmentally friendly home air conditioners rose to 74%.

New Value Creation

As initiatives to create new value meeting the expectations of customers and society, in fiscal 2017 our R&D expenses were ¥53.9 billion (consolidated: ¥46.1 billion in fiscal 2016), and, in fiscal 2016, we applied for 1,116 patents (non-consolidated: 1,292 in fiscal 2015).

Customer Satisfaction

Reflecting our efforts to provide the highest level of customer satisfaction, in fiscal 2017 our after-sales service customer satisfaction rating (Japan) was 4.13 out of a total of 5.0 points (fiscal 2016: 4.05), and we had operations in more than 150 countries and production facilities at over 90 locations.

Human Resources

We recognize that by respecting individuality and value systems and by drawing out the unlimited potential of individuals, we make both our organization and society stronger. In fiscal 2017, our percentage of female managers (non-consolidated) was 4.4% (fiscal 2016: 3.6%), our percentage of local employees serving as presidents at overseas bases was 52% (fiscal 2016: 51%), and the number of construction technology personnel we have developed reached 16,000 (Japan, China, and Malaysia).

CSR (Corporate Social Responsibility)

Environment

■ Materiality of Environmental Measures

While air conditioners, the main product of the Daikin Group, support the enhancement of economic growth and quality of life in hot regions, they consume a lot of electricity during use and have an impact on climate change through the fluorocarbon used as a refrigerant. For this reason, the Daikin Group believes that providing for both business development and environmental protection is essential for the sustainable growth of society, and we are taking steps to reduce emissions of greenhouse gases throughout the entire supply chain. We are working to develop and provide products and services that mitigate climate change, and promote technical training aimed at supporting widespread market adoption.

■ Daikin's Initiatives

Promotion of Eco-Friendly Technologies and Products

Daikin is aiming to reduce CO_2 emissions from the energy consumption of air conditioners through promoting the wider usage of inverter units globally.

In addition, based on our accumulation of research on refrigerants and investigations into its adoption, we have determined that at present R32, with approximately a third of the global warming impact of existing refrigerants, is the refrigerant best suited for residential and commercial air conditioners, and have adopted it at Daikin. Furthermore, Daikin has designated a total of 93 basic patents related to the manufacture and sale of air conditioners using R32 as a refrigerant for royalty-free use worldwide.

As of the end of March 2017, Daikin has sold more than 10 million R32 AC units worldwide in 52 countries. We estimate that the global market for R32 AC units, including the products of competitors, has expanded to more than 27 million units. Accordingly, together with the wider usage of inverter units, we calculate there has been a contribution towards the suppressing of 45 million tons of CO_2.

Daikin Receives the METI Minister Award in the Energy Conservation Grand Prize

In fiscal 2016, Daikin's "Retrofit System" received the top award, Japan's Ministry of Economy, Trade and Industry (METI) Minister's Award in the product/business sector of the Energy Conservation Grand Prize, sponsored by the Energy Conservation Center. This system, which has been designed for existing Daikin multiple air-conditioning systems for office buildings with five years or more having passed from installation, is the world's first service to replace pressure units and energy-efficient control software with the latest specification items. Currently, there are approximately one million eligible units worldwide. This is expected to reduce greenhouse gas emissions as, while utilizing the advantages of conventional maintenance, annual power consumption may be reduced by a maximum of 15% through only the replacement of main components.

Energy Conservation and Refrigerant Conversion Support in Emerging Countries

In emerging countries, where the use of air conditioning is projected to expand along with economic growth, promoting the use of energy-efficient products and low environmental impact refrigerants will make a considerable contribution to controlling global warming overall. Accordingly, Daikin is attempting to enhance people's understanding of R32, working in cooperation with the Japanese government and international organizations, for example, by holding seminars for Indian government officials and air-conditioning industry groups. In addition, we have conducted training for 3,600 local AC installation and service engineers on how to appropriately handle R32, promoting the enhancing of technical levels. We are implementing the same level of support in Thailand and Malaysia.

In fiscal 2017, Daikin was entrusted by Japan's Ministry of the Environment with a survey aimed at supporting developing countries. In collaboration with the United Nations Environment Programme, we sampled 40 Sri Lankan factories and carried out a basic survey on the spread of energy-efficient air-conditioning units and the building of schemes for the recovery, recycling, and disposal of refrigerants. Over 70 participants from government, academia, and industry took part in the seminar that was held to report on the findings.

ZEB Demonstration Tests

The implementation of the Net Zero Energy Building (ZEB) that maintains a pleasant air-conditioning experience while having an energy consumption of zero is being accelerated worldwide. Even in Japan, the government aims to make new public buildings ZEB by 2020. In order to achieve this, as energy-saving in air conditioning, that accounts for more than 40% of a building's energy consumption is vital, Daikin is proceeding with ZEB demonstration tests at the Technology and Innovation Center (TIC) established in 2015. In fiscal 2017, at a building in the TIC, we achieved an overall 72% reduction of energy consumption in comparison with standard values and an 82% reduction when taking into account solar power.

In addition, in July 2016, the TIC obtained the highest-ranked Platinum certification for Leadership in Energy and Environmental Design (LEED), the world's most widely used certification system for environmentally friendly buildings.

New Value Creation

■ Materiality of New Value Creation

In today's society, globalization and technological change and advancements are progressing at a remarkable pace, making differentiation from rival products difficult. To achieve sustainable growth, a company must integrate cutting-edge technologies, and generate technologies and products that contribute to the resolution of social issues such as energy, the environment, and health. Companies need to offer the world unprecedented new value.

Daikin is deepening its collaborative creation across a broad range in the areas of energy, space, and the environment, in pursuit of new value creation centered on air conditioning. Daikin's diverse workforce, along with external researchers and engineers, shares dreams and ambitions, offers the world new value through the power of air, and resolves social issues.

■ Daikin's Initiatives

Expanding Filter Business

Air pollution in emerging economies as a result of PM2.5 and the tightening of regulations related to air hygiene in the pharmaceutical and food industries are generating the need to improve atmospheric environments in indoor spaces worldwide. Daikin is responding to these needs by integrating air-conditioning and filter technologies with its engineering capabilities to expand its filter business, in addition to air-conditioning business.

It is said that a person spends more than 90% of the day indoors. The scale and type of the spaces our filter business covers extend from offices and residential buildings to large-scale industrial facilities, such as power stations and steelworks, and are contributing to the enhancement of a diverse range of atmospheric environments.

Responding to Increasingly Sophisticated Needs

In addition to the development and selling of air-conditioning and filter products, Daikin utilizes its engineering capabilities that combine technologies with product systems while engaging in dialogue with customers, and thereby proposes optimum atmospheric environments that respond to the needs of its customers. In addition, Daikin is enhancing its total support framework, including maintenance.

Going forward, Daikin will not only meet already visible needs, but also proactively respond to the increasingly sophisticated needs that contribute to health and pleasant experiences, such as the construction of "spaces to better focus in" and "relaxing spaces" for offices and residences, and will create new value.

Upgrading and Expanding the Technology and Innovation Center (TIC)

The TIC is the Daikin Group's core facility for technological development, bringing together engineers from various fields. In order to accelerate the Group-wide sophistication of component technologies and development of differentiated products, we are upgrading and expanding the TIC's framework as a global control tower to enhance collaborations among development locations around the world, as well as strengthening the functions of our global locations.

The stimulation of open innovation is also one of the roles of the TIC, and it proactively promotes cooperation and partnerships with companies, universities, and research institutions that possess unique technologies in varied industries and fields.

Centered on the TIC, Daikin is moving beyond the boundaries of conventional air-conditioning technologies and will step even into physiology and psychology to conduct research on relationships between the air environment and human body, working to generate new lifestyle values.

Implementing Open Innovation

In October 2016, Daikin began joint research with NEC on creating atmospheres and spaces that increase intellectual productivity through the utilization of AI/IoT. In addition to such numerous collaborations with other companies, we are pushing forward comprehensive collaboration and research with universities and research institutions in Japan and abroad, with the TIC playing a central role. In 2016, within RIKEN (Institute of Physical and Chemical Research), we established the "RIKEN-DAIKIN Wellness Life Collaboration Program" and began research in the life sciences field, such as on the construction of anti-fatigue spaces.

Customer Satisfaction

■ Materiality of Customer Satisfaction

Daikin is developing business in over 150 countries around the world. With consideration to the climate, culture, and regulations of each area, Daikin works to provide products and services that meet local needs. However, in order to satisfy customers, not only just providing products and services of superior performance and quality, but also exceeding the expectations of customers is important. In particular, we believe that anticipating problems that occur during the life cycle of a product, from purchase, use, replacement, to disposal, and appropriately resolving such problems as a specialist company, will lead to a high level of customer satisfaction.

■ Daikin's Initiatives

Working Out Global Quality Guidelines

The Daikin Group has prescribed its basic stance on quality standards across the Group companies as well as responsibilities and authorities for the efficient implementation of quality monitoring and corrective measures in its Global Quality Guarantee Rules.

We have acquired ISO9001 certification at all production facilities, and thoroughly implement a management system for the maintenance of quality levels in all development, procurement, and production divisions. Furthermore, we are also working to enhance quality with the cooperation of our outsourcing partners.

To assess the operating status of the quality management system, the Daikin Group conducts internal audits and operates a continual cycle of implementation, evaluation, and improvement.

Each year, quality priority measures and targets for each business division based on the Group's annual policy guidelines are set, establishing and implementing a quality program for the fiscal year.

First "Service Olympics" Held

The Daikin Group is increasing the number of its service engineers in countries and regions along with the expansion of the global market. Aiming to further enhance the services of these engineers, we held the first "Service Olympics" in November 2016.

A total of 28 service engineers selected from 20 different countries undertook written and practical examinations and were evaluated on both. Through the Service Olympics, we could gain an understanding of the level of each country and region, give feedback to the participants on factors which decreased scores, and provide guidance on how to further raise their levels.

Developing Our Service Structure in Japan and Abroad

The Daikin Contact Center accepts inquiries regarding repair requests, technical consultations, and purchasing information 24 hours a day, 365 days a year, from customers in Japan.

Overseas, we have put in place an after-sales service structure based on the principle of "fast, reliable, and friendly" in order to respond to the variety of requests specific to each country or region. We are working to enhance customer satisfaction through such measures as establishing call centers and providing technical information online.

Utilizing the Views of Our Customers

In Japan, we regularly conduct customer surveys for each business in order to understand the level of customer satisfaction.

In fiscal 2017, our air-conditioning business obtained an overall satisfaction score of 4.13 out of a total 5.0 points, its highest score to date. We believe this is the result of our efforts to "put customers first" and training programs focused on speedy repairs, technical capabilities, and customer service skills.

In addition, we share the views of our customers received by the Daikin Contact Center with our development division, continually soliciting and analyzing feedback to utilize in the further enhancement of our products and services.

Our Chemicals business was evaluated highly in fiscal 2017 in such areas as quality, delivery deadlines, technical service, and communication with customers.

Responding to the "Fluorocarbon Emission Control Law"

In April 2015, the Fluorocarbon Emission Control Law, designed to limit greenhouse-gas emissions, became effective. As a result, the owners of commercial-use air conditioners became obligated with various management responsibilities, such as inspections.

Accordingly, Daikin is leveraging its expertise to list all the many air-conditioning units of its customers, including those of other manufacturers, and provide support on identifying which units the law applies to, as well as undertaking simple inspections and periodic inspections on the units on behalf of our customers.

In addition, since June 2016, we have been providing the industry's first periodic inspection and repair warranty system, "Fluorocarbon Care," which also covers the products of other manufacturers.

Human Resources

■ Importance of Initiatives Related to Human Resources

Daikin has advanced with rapid globalization in the last 10 years, and the number of employees working overseas has increased substantially. In order to meet the expectations of its various stakeholders in the midst of this effort and to realize the strengths of the Daikin Group including the "Environment," "New Value Creation," and "Customer Satisfaction," "human resources" have become of utmost importance as the team responsible for these activities.

Daikin has positioned "People-Centered Management," which emphasizes that the source of a company's competitiveness is its people, at its very core, and gets its organizational strength by respecting individuality and value systems, and by drawing out the unlimited potential of individuals.

■ Daikin's Initiatives

Human Resource Development Policy

One of the corporate philosophies of the Daikin Group is the idea that "the cumulative growth of all Group members serves as the foundation for the Group's development." In addition, based on the concept that "people grow through job experience," we have positioned OJT as the basis of human resource development and, including off-the-job training (Off JT), are working to enhance growth opportunities.

In our "Overseas Base Practical Training," which cultivates global human resources, young employees are dispatched to countries different from that of their birth, broadening their horizons through practical work experience and developing the future pillars of the global business. As of fiscal 2017, we have sent 221 employees from Japan abroad, and 15 employees from abroad to Japan.

In the "Daikin Leadership Development Program," we train executives who can play an active role on the front lines of global business operations.

Contributing to the Development of Air-Conditioning Engineers in India

Since 2000, Daikin India has held technical training not only for its service engineers but also for the service engineers of retail and service cooperation stores that handle the products of other manufacturers. In fiscal 2017, a total of more than 20,000 people participated.

The production of air conditioners that can withstand such rough environments as "frequent blackouts and voltage fluctuations" and "fugitive dust lodging in heat exchange equipment in India," and the development of engineers regarding the installation, maintenance, and repair of such units are urgent tasks. We believe that contributing to resolving the local social challenge of lacking air-conditioning engineers both in quality and in quantity will lead to sustainable growth.

Promotion of Local Personnel at Overseas Bases

In conjunction with the globalization of the Daikin Group's business, we are also advancing with efforts to globalize our management team, and are aggressively promoting local employees at overseas bases to executive and managerial positions.

As of the end of fiscal 2017, local employees accounted for 52% of the presidents at our overseas bases and 50% of the directors. Furthermore, 15 of our 20 sales companies in Europe have local employees serving as presidents.

Accelerating the Active Role of Women in Japan

In Japan, Daikin is aiming to further the active role of women and is working toward a work environment that allows all employees to fully exhibit their capabilities regardless of gender.

As a goal, by the end of fiscal 2021, we aim to have at least one female director of Daikin Industries, and to increase our percentage of female managers to 10% (approximately 100 people) from the current level of 4.4% (47 people). We are also promoting the early cultivation of female managers and reforming the awareness of male managers and female employees. In addition, in order to prevent childbirth and child rearing becoming career breaks, we are enhancing our measures that support the early return from maternity leave.

In fiscal 2017, we held a total of five "female employee development management training" sessions aimed at approximately 150 male managers and leaders with female subordinates.

Daikin Industries has been recognized for its excellence in these efforts to promote women and, in August 2016, was certified as a highest ranked "Eruboshi" company, accredited by the Minister of Health, Labour and Welfare. In addition, in March 2017, Daikin was selected by the Ministry of Economy, Trade and Industry (METI) and the Tokyo Stock Exchange as a "Nadeshiko Brand" (excellent company in promoting the advancement of women in the workplace) for the fourth time in three consecutive years.

Acquired OHSAS18001 Certification

In order to ensure operational and employee safety, the Daikin Group is independently creating occupational health and safety management systems (OHSAS) at each base worldwide, and is acquiring certification for international standards, such as OHSAS18001. As of the end of fiscal 2017, 3 manufacturing facilities in Japan and 24 companies overseas have received certification.

We hold Groupwide joint safety and security meetings twice a year for the purpose of improving safety levels and sharing expertise. Every Daikin facility also carries out its own safety activities, such as education and safety patrols, aimed at achieving zero workplace accidents. In 2016, the frequency rate of industrial accidents throughout the Group was 1.50, an improvement of 0.4 from 2015.

CSR Management/Compliance Risk Management/Risk Management Promotion System

■ CSR Management

The CSR of the Daikin Group is based on being thorough in its corporate ethics and compliance. Together with carrying out our responsibilities to society, we are working toward resolving social problems through our business activities.

The CSR & Global Environment Center, a staff division, was established under the CSR Committee (chairman: director in charge of CSR), which sets the overall direction of CSR activities and monitors the execution of those activities, and promotes comprehensive and Groupwide CSR activities.

In order to integrate management strategies with CSR, we identified materiality (important themes) in conjunction with the formulation of the "FUSION 20" strategic management plan (fiscal 2017-21). Surveying the value chain and taking into consideration changes in the external environment, such as expectations and requests from outside and the acceleration of business expansion, we divided materiality broadly into "value-providing CSR" and "fundamental CSR," incorporating them into the "FUSION 20" plan.

■ Compliance Risk Management

Thorough Compliance and Risk Management

At the Daikin Group, the Internal Control Committee, chaired by the President, checks and confirms that internal controls, including risk management, are functioning properly Groupwide. In addition, the Corporate Ethics and Risk Management Committee promotes the management of individual operational risk and thorough compliance.

The Corporate Ethics and Risk Management Committee is chaired by the director in charge of corporate ethics and compliance, and is configured from the managers of each division and the presidents of each of the main Group companies in Japan. As a general rule, the committee meets twice a year to identify issues and promote their solutions, together with also receiving reports on the status of overseas Group companies.

A Compliance Risk Management Leader (CRL), appointed in each division and for each of the main Group companies in Japan and overseas, promotes compliance based on the Group Code of Conduct, which sets forth the conduct of corporate officers and employees. In addition, regular CRL meetings are held to share information and ensure the Group Code of Conduct is adhered to, aiming to foster a "culture free of compliance violations" and to elevate "mechanisms to ensure that there are no compliance violations."

Enhancing Activities throughout the Group

Daikin Industries also participates in the compliance committees of each region overseas. With the goal of mutually confirming situations in Japan and abroad as well as sharing information, efforts are made to enhance compliance and risk management activities throughout the Group.

■ Risk Management Promotion System

With the rapid expansion of Daikin's business, the overall picture of risks from a global perspective must be understood in an accurate and prompt manner, and alleviated. To achieve this, we have introduced a Groupwide risk management.

First, each division and main Group company implement risk assessments to identify and select critical risks, and formulate the necessary countermeasures. In addition, each company identifies critical risks from the assessment results, and efforts are made to develop and implement risk-reducing countermeasures.

For example, in fiscal 2017, Daikin Industries made efforts toward the key themes such as "Earthquake Risk," "PL Quality Risk," "Intellectual Property Risk," "Information Leakage Risk," "Overseas Crisis Management," and "Risk of Improper Accounting."

Self-Inspection of Code of Conduct Compliance

The Daikin Group has established its own "self-inspection" system in which each employee annually carries out a self-check on compliance with the Group Code of Conduct. Based on the results, organizational issues are identified and the necessary countermeasures are implemented. These issues and countermeasures are reported to and shared with the Corporate Ethics and Risk Management Committee.

In addition to the self-inspection, compliance with the Group's Code of Conduct and laws and ordinances is also confirmed in the Legal Department's legality audit and the Audit Department's operational audit.

Respect for Human Rights/ Supply Chain Management

■ Respect for Human Rights

Based on the laws and ordinances of countries and regions around the world, the Daikin Group respects basic human rights in accordance with the various international norms.

The Daikin Group participates in the United Nations Global Compact for supporting and putting into practice universally accepted principles relating to such matters as human rights and labor. Our Group Code of Conduct stipulates policies for respecting human rights, diverse values, and sense of work, and policies for no child labor or forced labor.

In addition, upon specifying humans rights issues within the Group's business, we evaluate the risk across the whole value chain and work to prioritize the identification of risks that need resolving.

Respect for Human Rights in the Self-Inspection

An item relating to respect for human rights was included as part of the self-inspection that is conducted each year from the viewpoint of compliance, and now the inspection includes confirming that there are no human rights violations or other such problems.

Such an item was also included in the Supply Chain CSR Promotion Guidelines, devised in April 2017, and we are also asking our suppliers to be thorough.

In addition, Group companies overseas are also creating their own *Corporate Ethics Handbooks* based on the Group Code of Conduct, and are making efforts to ensure total respect for human rights in the workplace.

The Daikin Group also participates in the activities of the Global Compact Network Japan, through which we learn from experts and cases at other companies regarding global human rights issues, and this helps us improve our own efforts in this area.

Regular Human Rights Awareness and Education

Daikin Industries conducts human rights education and awareness activities each year for all of its directors, new employees, including those of affiliates, and newly appointment managers. In addition, we also publish a series of human rights articles in the Company newsletter to raise awareness of human rights.

At Daikin America, focus is centered on creating a workplace environment that respects coworkers, and all employees are provided with opportunities to be educated in this area each year.

■ Supply Chain Management

At the Daikin Group, we believe that our scope of social responsibility includes our entire global supply chain. In 1992, the Daikin Group established the Basic Procurement Guidelines. In addition to being thorough in green procurement and fair trade practices with our suppliers, we promote CSR activities from perspectives such as quality, human rights, and labor.

Establishment of "Supply Chain CSR Promotion Guidelines"

Among CSR activities in our supply chain, we are endeavoring in particular to understand CO_2 emission levels and to properly control substances subject to international regulations, such as designated chemical substances and conflict minerals.

In April 2017, we established and implemented the Supply Chain CSR Promotion Guidelines. These are guidelines for the promotion of CSR, aimed at stable continuation and growth of business. In addition to general compliance requirements, the said Guidelines cover the whole of CSR, such as environmental protection, respect for human rights, occupational health and safety, and prohibition of trade with conflict zones, and we are asking our suppliers to promote such efforts.

Furthermore, we plan to evaluate such efforts with the cooperation of our suppliers.

Growth and Development alongside Suppliers

In order to provide products that satisfy the trust of our customers, the cooperation of our suppliers is vital. Working hard to build strong relationships of trust with all suppliers, the Daikin Group endeavors to continue to meet our mutual expectations, and to build relationships in which we can both grow and develop.

Daikin Group companies both in Japan and abroad periodically conduct dialog at the production sites of our suppliers on quality audits and quality improvements, collaborating with our suppliers on quality improvement efforts through support for enhancing the required technological capabilities, etc. We also hold safety-related briefing sessions and support efforts to prevent work-related accidents before they occur.

For example, McQuay China (Shenzhen) provided suppliers with quality control training in fiscal 2017, and 41 persons from 37 companies participated in the session. Through lectures by external instructors and discussions on quality control, we clarified the core points of the fiscal 2018 quality control activities.

Stakeholder Engagement/Regional Society

■ Stakeholder Engagement

The Daikin Group's main stakeholders are the customers to whom we provide products and services, the shareholders and investors who have a direct impact on our business, our suppliers, our employees, and everyone in the regional societies that our business evolution affects. In addition, the spread of air-conditioning technologies and the enhancement of the environmental friendliness of our products and services involve national and local governments and industry associations. The Daikin Group believes that it is important to understand the concerns and expectations of its stakeholders through proactive communication and report such voices to management so that it can utilize them in our business.

Continuing Exchange of Opinions with Experts

Since 1995, the Daikin Group has held "air-conditioner forums" in Japan where it can exchange opinions relating to the "future of air conditioning" with experts in the field. In addition, in light of the rapid global development of our business, since fiscal 2008, we have also held forums in Europe, China, the United States, Asia/Oceania, and Central America/South America. Exchanging opinions with experts from each region about environmental and energy issues, we utilize that information in our technology as well as product and business development.

In fiscal 2017, we held discussions in Asia/Oceania and Europe, regarding energy conservation and indoor air quality within buildings. Furthermore, in Central America/South America, we held the first exchange of opinions with government officials and university professors from various countries on "promotion of energy conservation environmental technology for a sustainable society," introducing Daikin's relevant technologies and efforts.

Responsibility to Shareholders and Investors

To live up to the expectations of shareholders and investors, the Daikin Group believes that it must increase its corporate value. It therefore emphasizes free cash flow as a source of corporate value and focuses on augmenting its profitability while lowering the levels of its trade receivables and inventories.

Furthermore, Daikin works to stably maintain its consolidated ratio of dividends on equity (DOE) at 3.0%. In addition, to increase its management transparency toward shareholders and investors, Daikin is executing diverse kinds of IR activities. Furthermore, to enable shareholders to exercise voting rights easily at general shareholders' meetings, Daikin provides shareholders with invitations to meetings early and produces English-language versions, as well as enabling shareholders to exercise their voting rights via personal computers and mobile phones.

■ Regional Society

The Daikin Group is made up of 245 consolidated subsidiaries worldwide and is expanding business in over 150 countries. Premised on fulfilling our social responsibility of expanding regional employment and cooperating with local companies, our basic policy is to develop strong bonds with local communities as a member of the regional society operating a business while respecting the culture and history of each country and region.

With our employees taking the initiative, we carry out social activities mainly in the areas of "environmental protection," "supporting education," and "living symbiotically with the local region" and are contributing to the resolution of social issues from a global perspective based on sustainable development goals (SDGs).

Environmental Protection

Forest and Biodiversity Preservation

Daikin has been carrying out the "Forests for the Air" project for protecting forests in seven locations across the world in partnership with Conservation International, an international NGO, and the Shiretoko Nature Foundation. In the Shiretoko Peninsula, Indonesia, Brazil, Cambodia, India, China, and Liberia, we work with governments, NGOs, employees, and customers among others to provide support for the coexistence of the lifestyles of local residents and forest biodiversity, contributing to achieving SDGs. By 2024, we will preserve 11 million hectares of forests and inhibit seven million tons of CO_2.

In addition, we are also making efforts toward tree-planting activities, the conservation activities for nature such as seas and rivers, and biodiversity conservation in the vicinity of our production and sales locations around the world.

Supporting Education

Cooperating in the Education of Future Generations

Since 2010, Daikin has offered a "Circle of Life" environmental education program for elementary school children centered on a theme of biodiversity. As well as providing elementary schools with educational materials, Daikin employees visit schools to teach lessons. In fiscal 2017, 27 schools participated (approximately 2,000 students) in the program, and 15 schools were visited by our employees.

In addition, since fiscal 2016, we have been cooperating in the "Mirai no Hakase" training laboratory, a scientist development program held by Osaka Prefecture University and aimed at junior high school students in Sakai City, Osaka Prefecture.

Moreover, Daikin Group plants around the world are accepting tours from children and students, the future generations.

Symbiosis with Regional Societies

Supporting the Regional Revitalization of Okinawa

Since 1988, Daikin Industries has held the "Daikin Orchid Ladies Golf Tournament," and, through sports, we are endeavoring to revitalize Okinawa and encourage economic interchange with the local area.

In conjunction with this tournament, we solicit donations that we then present as an "Orchid Bounty" on an ongoing basis to individuals and organizations that promote such areas as the arts, culture, education, and sports in Okinawa.

Holding "Bon Festival" in Japan and Abroad

Daikin has deepened interchange with local residents through regional festivals and sports, building relationships of trust. As part of those efforts, the Bon Festival, which is planned and operated by Daikin employees, is a large event that attracts attention by numerous local residents. In addition to manufacturing plants in Japan, the festival is also held at our main production bases in China, the United States, and other areas.

Contributing to Local Communities around the World

Employees from Daikin Group locations around the world are working toward contributing to society by meeting local needs, such as through volunteering activities. In fiscal 2017, for example, in China, we held a Christmas party at a welfare facility for people with disabilities, donating presents and putting on performances. In addition, in Europe, we sent financial aid and relief supplies, such as emergency air conditioners, to areas affected by the central Italy earthquakes.

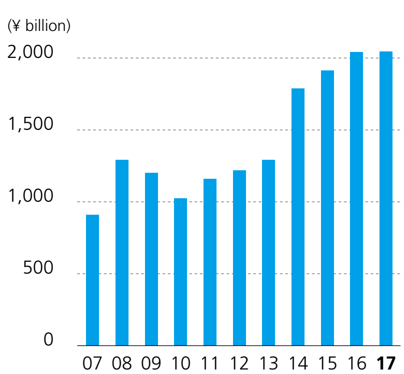
Eleven-Year Financial Highlights

Daikin Industries, Ltd. and Consolidated Subsidiaries
Years Ended March 31

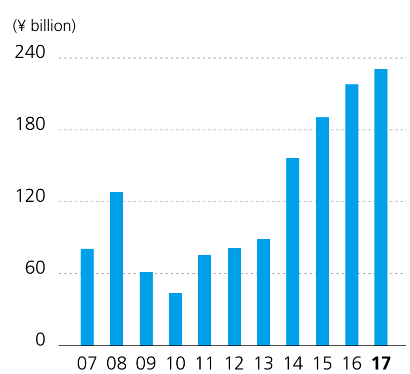
	2007	2008	2009	2010
Operating Results (for the year):				
Net sales	¥911,749	¥1,291,081	¥1,202,420	¥1,023,964
Gross profit	312,688	441,549	363,660	319,301
Selling, general and administrative expenses	231,934	313,451	302,266	275,263
Research and development expenses (Note 1)	27,204	32,075	30,535	28,220
Operating income	80,754	128,098	61,394	44,038
EBITDA (Note 2)	115,315	179,469	118,325	96,462
Net income attributable to owners of parent	45,420	74,822	21,755	19,391
Cash Flows (for the year):				
Net cash provided by operating activities	¥ 83,725	¥103,329	¥62,238	¥129,227
Net cash used in investing activities	(305,251)	(76,428)	(99,302)	(39,848)
Free cash flow (Note 3)	(221,526)	26,902	(37,065)	89,379
Net cash provided by (used in) financing activities	245,975	3,367	48,382	(34,942)
Financial Position (at year-end):				
Total assets	¥1,161,364	¥1,210,094	¥1,117,418	¥1,139,656
Total interest-bearing liabilities	456,074	356,928	417,919	399,313
Total shareholders' equity	397,542	545,641	471,686	496,179
Per Share Data (yen):				
Net income (basic)	¥ 172.66	¥ 262.24	¥ 74.51	¥ 66.44
Shareholders' equity	1,511.47	1,867.79	1,615.98	1,701.29
Free cash flow	(842)	94	(127)	306
Cash dividends	28.00	38.00	38.00	32.00
Ratios (%):				
Gross profit margin	34.30%	34.20%	30.24%	31.19%
Operating income margin	8.86	9.92	5.11	4.30
EBITDA margin	12.65	13.90	9.84	9.42
Return on shareholders' equity (ROE)	12.31	15.87	4.28	4.01
Shareholders' equity ratio	34.23	45.09	42.21	43.54

Notes: 1. R&D expenses are included within general and administrative expenses and manufacturing expenses.
2. EBITDA = Operating income + depreciation and amortization.
3. Free cash flow = Net cash provided by operating activities + net cash used in investing activities.
4. Accompanying a change in accounting policy, effective from April 1, 2014, the consolidated financial statements for the fiscal year ending March 31, 2014 and subsequent years have been revised.

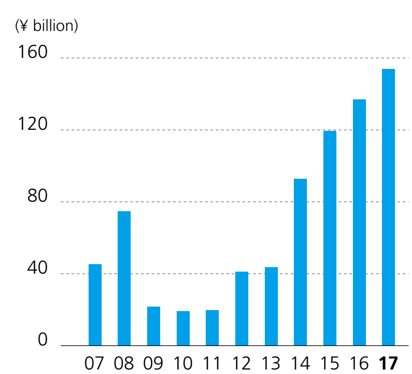
Net Sales



Operating Income



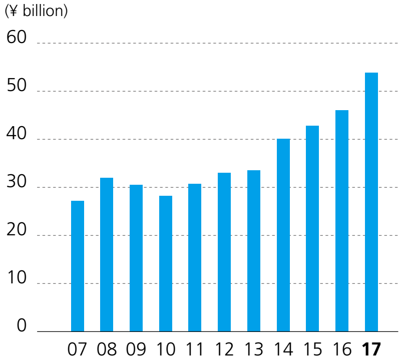
Net Income Attributable to Owners of Parent



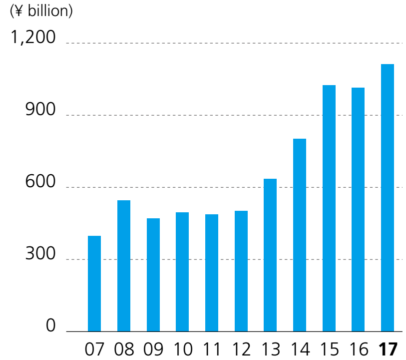
Millions of Yen

2011	2012	2013	2014	2015	2016	**2017**
¥1,160,331	¥1,218,701	¥1,290,903	¥1,787,679	¥1,915,014	¥2,043,691	**¥2,043,969**
361,665	371,902	388,046	568,323	649,902	711,576	**730,935**
286,210	290,709	299,419	411,786	459,314	493,704	**500,166**
30,771	32,987	33,569	40,177	42,892	46,138	**53,870**
75,455	81,193	88,627	156,537	190,588	217,872	**230,769**
127,168	131,719	140,151	235,439	268,354	302,075	**315,798**
19,873	41,172	43,585	92,787	119,675	136,987	**153,939**
¥78,411	¥44,967	¥103,161	¥179,713	¥160,423	¥226,186	**¥267,663**
(23,306)	(62,955)	(218,386)	(80,835)	(77,331)	(105,493)	**(128,823)**
55,105	(17,988)	(115,225)	98,878	83,092	120,693	**138,840**
(37,623)	(1,113)	143,520	(38,249)	(83,073)	(85,422)	**(73,544)**
¥1,132,507	¥1,160,564	¥1,735,836	¥2,011,870	¥2,263,990	¥2,191,105	**¥2,356,149**
372,481	389,891	705,871	693,944	662,413	608,981	**609,430**
487,876	502,309	618,118	801,854	1,024,725	1,014,409	**1,111,636**
¥ 68.14	¥ 141.37	¥ 149.73	¥ 318.33	¥ 410.19	¥ 469.23	**¥ 526.81**
1,672.74	1,725.64	2,123.10	2,748.08	3,511.34	3,473.54	**3,802.10**
189	(62)	(396)	339	285	413	**475**
36.00	36.00	36.00	50.00	100.00	120.00	**130.00**
31.17%	30.52%	30.06%	31.79%	33.94%	34.82%	**35.76%**
6.50	6.66	6.87	8.76	9.95	10.66	**11.29**
10.96	10.81	10.86	13.17	14.01	14.78	**15.45**
4.04	8.30	7.78	13.07	13.10	13.44	**14.48**
43.08	43.28	35.61	39.86	45.26	46.30	**47.18**

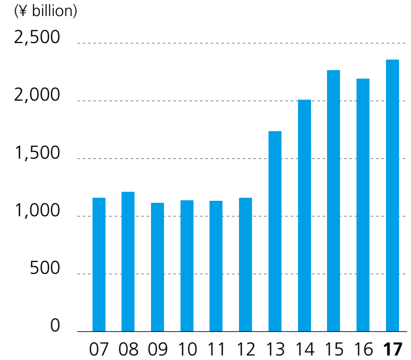
Research and Development Expenses



Shareholders' Equity



Total Assets



Financial Review

Summary of the Period

The global economy slowed down overall during fiscal 2017, as recoveries varied from country to country and region to region. In the United States, robust personal consumption drove the economy, while in Japan the economy showed a moderate recovery trend, backed by improvement in corporate earnings and a recovery in exports. Meanwhile, the Chinese economy slowed moderately, while highly resource-dependent emerging economies continued to experience stagnation. In addition, with the rapid strengthening of the yen in the first half of fiscal 2017, currency exchange rates were highly volatile.

Amid this environment, the Daikin Group's consolidated net sales slightly increased compared to the previous fiscal year to ¥2,044.0 billion, due to strong sales in the air-conditioning business in each region, while the yen appreciated against other currencies, including the Chinese yuan, U.S. dollar, and euro, which had a negative impact, such as a decrease in the yen-equivalent. As for profits, sales volume increased in each region and gross margin rates improved through cost reductions, despite a factor of profit decline due to conversion to the yen-equivalent. As a result, consolidated operating income increased by 5.9%, to ¥230.8 billion, and net income attributable to the owners of the parent company increased by 12.4%, to ¥153.9 billion.

Performance by Business Segment

• Air-Conditioning and Refrigeration Equipment

Total sales of the Air-Conditioning and Refrigeration Equipment segment increased to ¥1,835.4 billion, up 0.4% from the previous fiscal year. Operating income increased 7.7%, to ¥208.8 billion.

Japan

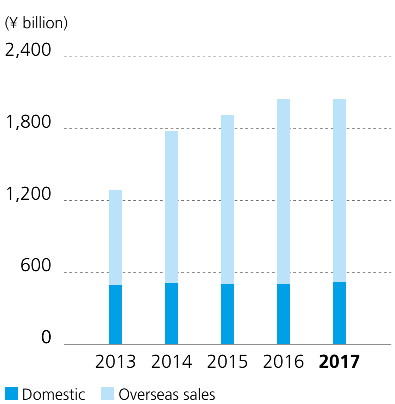
In the Japanese commercial air-conditioning equipment market, industry demand rose year on year, pushed upward by the impact of the heat wave in western Japan and the government's subsidy system for replacement to high-performance, energy-saving equipment. The Daikin Group captured demand for air conditioners for stores and offices, especially those of "FIVE STAR ZEAS" and "Eco-ZEAS" models, and net sales increased year on year.

In the Japanese residential air-conditioning equipment market, industry demand increased year on year due to robust demand that began in the first half from the impact of the heat wave in western Japan and continued into the third quarter onward. The Daikin Group utilized the brand power of its room air conditioner Urusara 7, an energy-saving, high-value-added product, in an effort to expand sales for all models of residential air conditioners, and net sales exceeded that of the previous fiscal year.

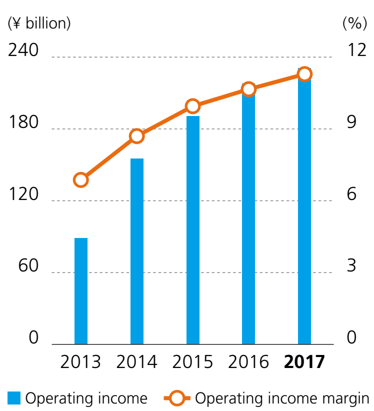
Europe (Including Turkey, the Middle East, and Africa)

In Europe, while sales were strong, net sales after converting to the yen-equivalent remained flat year on year in the region as a whole. Net sales of residential air-conditioning systems increased year on year in the local currency, owing to the increased demand stemming from the heat wave in 2015, which remained strong. Commercial air-conditioning equipment sales were also strong because of the capturing of demand for the renewal and replacement of existing air-conditioning systems in main countries, although the European economy remained sluggish. Despite stagnant demand in France, which is a major market, net sales of heat pump hot water heating systems grew in Europe overall in the local currency from the previous fiscal year due to significant sales growth in Italy and other countries.

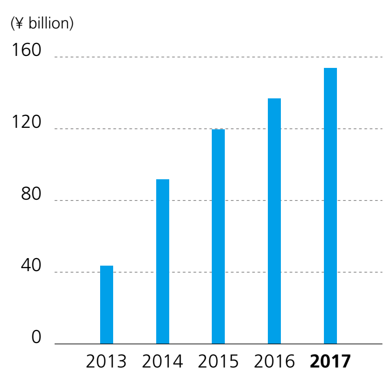
Domestic and Overseas Sales



Operating Income and Operating Income Margin



Net Income Attributable to Owners of Parent



In emerging economy markets, while sales in the Middle East and Africa were strong, net sales after converting to the yen-equivalent decreased year on year in the region as a whole. Net sales increased year on year in the local currency, thanks to efforts to boost orders for private-sector projects amid a series of temporary suspensions or delays, particularly for large-scale government projects, due to prolonged stagnation of crude oil prices and growing geopolitical risks. In Turkey, net sales increased year on year in the local currency, as a result of boosting orders for small to medium-scale commercial projects and strengthening sales of residential air-conditioning systems. This was despite a series of delays in delivery, mainly for large-scale projects and others, and amid the continuing political unrest that followed the attempted coup détat in July.

China

In China, while economic growth has been slowing down, the Group intensified its retail sales to capture firm personal consumption. Net sales in the local currency rose year on year in all regions and for all products. Although net sales after converting to the yen-equivalent fell slightly year on year due to the depreciation of the Chinese yuan, operating income increased year on year owing to cost reductions promoted in the production division. In the residential-use market, the Group focused on its own specialty "PROSHOPs" and leveraged its proposal and installation capabilities, which are its strengths, to expand sales mainly in the mid-range and high-end residential market with the "New Life Multi Series," residential multi-split type room air conditioners that propose a variety of lifestyles for customers. In the commercial-use market, the Group expanded sales by carrying out model changes to the mainstay "VRV-X" series, commercial multi-split type room air conditioners that offer enhanced product appeal, including energy-saving performance; enhancing advertising and 'spec-in' for architectural firms; and broadening the range of the target markets to extend from new construction to replacement. In the large-building (Applied Systems) air-conditioning equipment market, the Group expanded sales by carrying out sales activities in a wide range of projects, from large to small- to medium-scale, based on an enhanced product lineup and reinforced after-sales service business.

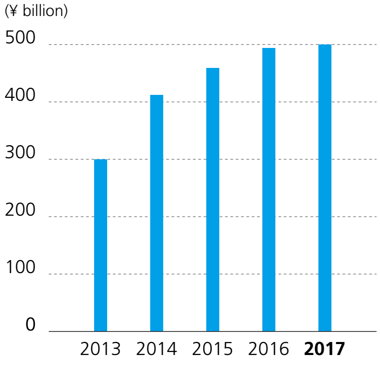
Asia/Oceania Region

In Asia and Oceania, net sales after converting to the yen-equivalent remained flat year on year in the region as a whole. Nevertheless, net sales in the local currency increased considerably year on year thanks to efforts such as dealer development, expanded sales of differentiated energy-saving products that met local needs, and the reinforcement of the service structure, which led to the capturing of demand among the growing middle class. In the residential air-conditioning systems, sales of inverter-type, cooling-only air conditioners with exceptional energy-saving performance were strong, and sales grew particularly in Thailand, Vietnam, Indonesia, and India. Sales of multi-split type room air conditioners for buildings grew due to enhanced 'spec-in' activities and greater focus on dealer development.

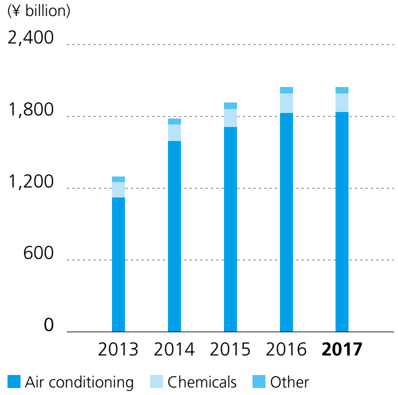
Americas Region

In the Americas, net sales increased year on year in the region as a whole due to strong sales. Net sales of residential air-conditioning systems rose year on year as a result of favorable weather in the first half and efforts to expand the sales network. For light commercial equipment (commercial air-conditioning equipment for medium-sized buildings), Daikin has pushed

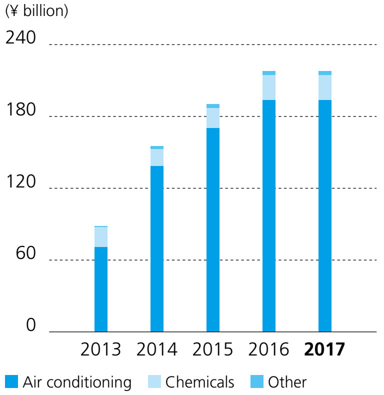
Selling, General and Administrative Expenses



Sales by Segment



Segment Profit



forward with sales policies by routes, and sales were above the previous fiscal year. In the market for Applied Systems, backed by a higher level of demand than in the previous fiscal year, net sales grew year on year thanks to sales of Applied Systems, mainly rooftops equipped with inverters, in addition to growth in the after-sales service business.

• Chemicals

Overall sales of the Chemicals segment decreased by 3.4%, to ¥156.8 billion, and operating income decreased by 11.2% year on year, to ¥18.3 billion.

Demand for fluoropolymers was robust for semiconductor-related applications in Japan and elsewhere in Asia. However, overall sales of fluoropolymers fell year on year. This was due to foreign exchange rate impact, price competition in the U.S. market from rival companies and products made in China, and intensified competition in the LAN cable market.

Fluoroelastomers were affected significantly by foreign exchanges, and sales fell year on year, despite robust demand in automotive fields in each region around the world.

Sales of specialty chemicals were down, compared with the previous fiscal year. Net sales of oil and water repellents fell significantly year on year due to delays in switchovers to new products as well as the impact of foreign exchange, among other factors. Sales of anti-fouling surface coating agents used in devices, such as touch panels, increased year on year, supported by strong demand in China. Sales of etchant for cleaning semiconductors increased year on year due to sales growth in Japan and elsewhere in Asia where related demand was favorable.

As for fluorocarbon gas, overall sales of gas increased substantially year on year as a result of growth in sales for after-sales service in the Americas.

• Other Operations

Overall sales of the "Others" segment fell by 2.9% year on year, to ¥51.8 billion. Operating income increased by 6.3% year on year, to ¥3.8 billion.

Sales of oil hydraulic equipment for industrial machinery fell year on year due to the impact of stagnant demand in the Japanese market.

Sales of oil hydraulic equipment for construction machinery and vehicles remained flat against the previous fiscal year due to the impact of production volume adjustments by Chinese agricultural machinery manufacturers, despite robust sales to key customers in Japan and the United States.

In the specialized machinery businesses, sales of home oxygen equipment were strong, while sales of ammunition to Japan's Ministry of Defense decreased, resulting in a decline in net sales compared to the previous fiscal year.

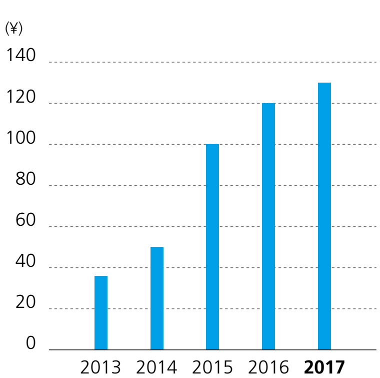
In the electronics system business, net sales were on a par with the previous fiscal year, as sales especially of database systems for design and development sectors expanded.

Currency Exchange Rates

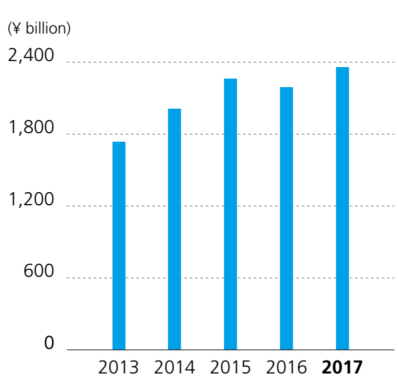
During the fiscal year, the yen appreciated against the U.S. dollar and the euro. The average exchange rates for the yen were ¥108 to one U.S. dollar and ¥119 to one euro. The impact of exchange rate fluctuations on Company sales was minus ¥193.6 billion, and the effect on operating income was minus ¥37.0 billion.

	Fiscal 2016	**Fiscal 2017**
Yen-U.S. dollar rate	¥120	**¥108**
Yen-euro rate	¥133	**¥119**

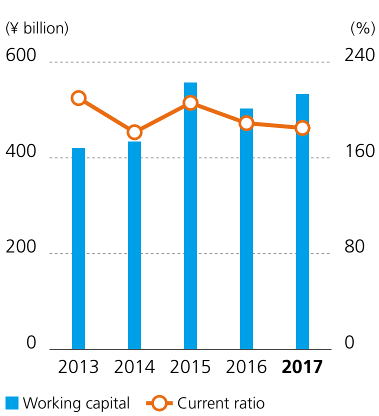
Cash Dividends per Share



Total Assets



Working Capital and Current Ratio



SG&A Expenses and Operating Income

Selling, general and administrative expenses rose 1.3%, to ¥500.2 billion, because of an increase in R&D expenses, and rose to 24.5% of net sales.

Consolidated operating income rose 5.9%, to ¥230.8 billion, and the operating income ratio increased 0.6 percentage point, to 11.3%.

Assets, Liabilities, and Total Equity

• Assets

At the end of fiscal 2017, consolidated total assets amounted to ¥2,356.1 billion, up ¥165.0 billion from the previous fiscal year-end. Current assets were up ¥93.1 billion from the previous year-end, to ¥1,159.9 billion, because of an increase in cash and deposits. Noncurrent assets increased by ¥71.9 billion from the previous fiscal year-end, to ¥1,196.3 billion, due to an increase in buildings and structures, as well as other factors.

• Assets, Liabilities, and Total Equity

Consolidated total liabilities increased by ¥66.9 billion from the end of the previous fiscal year and amounted to ¥1,220.5 billion at the end of fiscal 2017 because of an increase in notes and accounts payable and other factors.

In addition, interest-bearing debt increased by ¥0.4 billion mainly due to an increase in short-term loans payable and amounted to ¥609.4 billion at fiscal year-end. The interest-bearing debt ratio (interest-bearing debt divided by total assets) decreased to 25.9%, compared with 27.8% at the end of the previous fiscal year, as a result of an increase in total assets due to an increase in cash and deposits.

Net assets increased by ¥98.1 billion from the previous fiscal year-end, to ¥1,135.6 billion, because of the recording of net income attributable to owners of the parent company and other factors. As a result, the shareholders' equity ratio increased to 47.2%, from 46.3% at the end of the previous fiscal year, and net assets per share increased to ¥3,802.10, from ¥3,473.54 at the end of the previous fiscal year.

Cash Flows

During the fiscal year under review, net cash provided by operating activities was ¥267.7 billion, an increase of ¥41.5 billion from the previous fiscal year, principally due to an increase in income before income taxes and a decrease in income taxes paid. Net cash used in investing activities was ¥128.8 billion, an increase of ¥23.3 billion from the previous fiscal year, primarily due to an increase in payment for acquisition of consolidated subsidiaries. Net cash used in financing activities was ¥73.5 billion, a decrease of ¥11.9 billion from the previous fiscal year, mainly due to an increase in proceeds from long-term loans payable. After including the effect of foreign exchange rate change to these results, cash and cash equivalents at the end of the fiscal year under review amounted to ¥344.1 billion, an increase of ¥52.9 billion from the previous fiscal year.

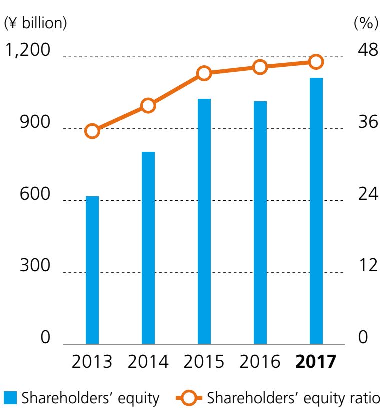
Capital Investment

Concentrating management assets in business fields that offer high profitability is the Daikin Group's fundamental strategy.

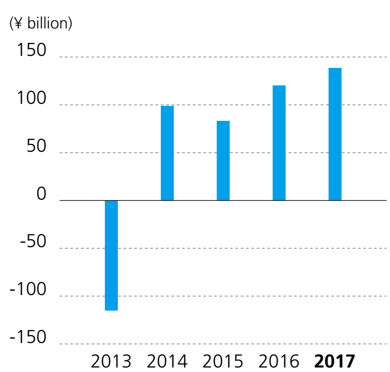
In fiscal 2017, the Group made total capital investment of ¥90.3 billion, largely in the air-conditioning/refrigeration equipment and chemicals business fields.

In the air-conditioning and refrigeration equipment field, Daikin invested ¥9.1 billion, centered on the research and development and rationalization of room air conditioners and package air conditioners. At Goodman Global

Total Shareholders' Equity and Shareholders' Equity Ratio



Free Cash Flow



Capital Investment and Depreciation and Amortization

Group, Inc., investments of ¥31.3 billion were made primarily to increase capacity.

In the chemicals field, the Group invested ¥7.4 billion, primarily to increase capacity and for rationalization objectives. In addition, Daikin Fluorochemicals (China) Co., Ltd., made ¥2.5 billion in investments for increasing capacity.

The main sources of funds for these investments were bank borrowings and retained earnings. Note that the Daikin Group did not make any major disacquisitions of equipment or facilities during the fiscal year under review.

R&D Expenses

In response to an increase in worldwide concern regarding global warming and energy issues, the Group is engaged in leading-edge research and development programs designed to proactively contribute to the resolution of global environmental issues, while also expanding the Group's business operations. In 2015, the Group established its Technology and Innovation Center (TIC), which is the core facility for the technology and product development of the Group. This center is designed to conduct research and development on cutting-edge technologies and basic technologies and also to develop and provide customers with new value-added and differentiated products by combining not only expertise within the Group but also the world's wisdom, including that of industries, academia, and the government. In addition to heat-pump and inverter technologies for air conditioning, the TIC has integrated energy-saving solutions business research centered on the development and air conditioning of air-conditioning control systems, utilizing green architecture/renewable energy areas, new product development in processing material areas, and cutting-edge IT. The TIC has also gathered together development on new applications for fluoride and development on high-function materials and materials suitable for an environmentally friendly society. Furthermore, the Group is also enhancing the development functions of its global locations, including in Europe and China, utilizing new technologies created by the Japanese domestic research and development department in the development of products that suit local needs. Through these efforts, Daikin will endeavor to substantially increase the efficiency and speed of research and development to produce differentiated products around the world.

In fiscal 2017, R&D expenses included in cost of goods sold and SG&A expenses amounted to ¥53.9 billion.

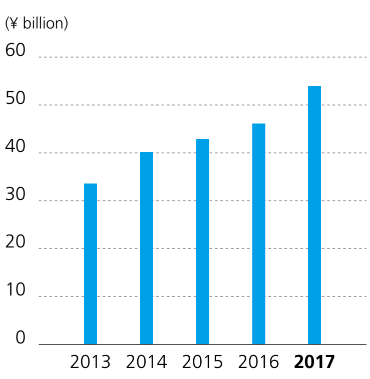
• Air-Conditioning and Refrigeration Equipment

R&D expenses for air-conditioning and refrigeration equipment operations totaled ¥45.9 billion.

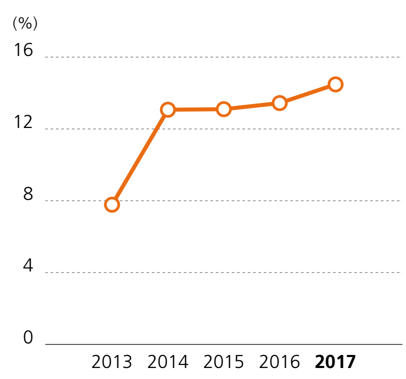
The wall-mounted-type Urusara 7, which is for residential use, demonstrates its pleasant airflow control, which prevents direct flows to the people in the room (for cooling: circulation airflow; for heating: vertical direct airflow), and has been well received. In addition to the above conventional features, when cooling, whole room temperature irregularities have now been quickly resolved without direct flows to people by employing a combination of the circulation and vertical direct airflows. With this airflow control and Daikin's original waterless humidifier system technology and cooling dehumidifying control that further enhance pleasant air-conditioning experiences, we have created spaces enveloped in comfort.

In addition, we launched the UX Series, a wall-mounted indoor unit multiple air-conditioning system for residential use. An industrial designer and Daikin Europe employed a design that blends easily into walls and a curved front panel based on the concept of "harmony with the interior," due to the

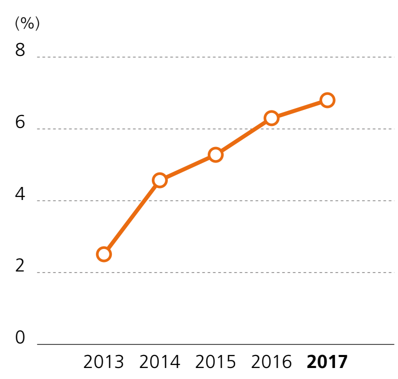
Research and Development Expenses



ROE



ROA



growing awareness over residential interior design. Furthermore, by connecting the UX Series and hydronic floor heating to multiple air-conditioning systems, we have realized energy conservation and pleasant air-conditioning experiences through interlocking control, in addition to design. As a result, Daikin was awarded the Energy Conservation Grand Prize for fiscal 2015 by the Energy Conservation Center, Japan.

In the commercial-use air-conditioner business, we launched the VRV X series, a multiple air-conditioning system for office buildings. Through reviewing the coolant circuit and enhancing running efficiency during low-load operating periods, we have substantially reduced annual electric power costs. In addition, for ceiling cassette type indoor units, we have employed the fundamentally reviewed "active circulation airflow" to realize warm and pleasant heating from the feet up. Furthermore, responding to the needs for the simple adoption of air-conditioning systems that lack airflows, such as radiant air-conditioning and built-in floor heating systems, we have added a chilled water producing "chilled water unit" to our product lineup.

For applied equipment, in North America, in addition to cost reductions, we launched next-generation magnetic bearing turbo refrigerator equipment that also conforms to the high requirements for lifts. In addition, we demonstrated an industry-leading level of full-load performance for high-efficiency two-stage turbo refrigerator equipment with refrigeration capacities of 1,500RT. In China, we developed module and turbo refrigeration equipment to meet the expected demand for the renewal and replacement of existing equipment.

Responding to environmental needs, we launched DC inverter cooling dedicated chillers, high-efficiency air-cooled magnetic bearing chillers, and ultrahigh-efficiency heat-pump chillers. In Europe, we developed our inverter screw chillers, which demonstrate an industry-leading level of efficiency, and, for secondary side products, we progressed with simple selection and the development of overwhelmingly highly efficient products, launching an air-handling unit aimed at hospitals and the hygiene market.

For air-handling units, we developed a ceiling-embedded type to meet the needs for distributed ventilation.

• Chemicals

R&D expenses for Chemicals operations totaled ¥6.2 billion.

Daikin conducts R&D for new products and new applications based on rich experience in fluorine products and fluorochemical technology. In fluoropolymer resins and fluororubbers, using fluorochemicals' good properties in heat resistance, low drug reactivity, and dielectric properties, Daikin is developing new differentiated products for automotive, semiconductor, wire and cable (IT field), and other applications. In coating materials development, Daikin makes use of the non-adhesive and chemical resistance properties of fluoride-based substances. Daikin is developing water and oil repellent textiles treatment materials as well as carpet treatment materials. Daikin is also developing materials for LCD-related applications that draw on the functionality of fluorocompounds, and has received an order for a project to develop intermediate materials for medical use. In these and a wide range of other areas, Daikin engages in fluoride-related R&D.

In addition to the development of materials, as part of R&D in peripheral areas to develop technologies and applications, Daikin is working on the development of film process products, multilayered materials, and advanced materials research related to the medical, optical, and environmental areas, probing the depths of fluoro-related research and applications. Especially in the energy field, Daikin is concentrating on developing such products as electrolyte solutions, additives, positive electrode binders, gaskets, and other components needed to increase the capacity and safety of lithium ion secondary batteries.

In the refrigerant field, we accelerated R&D related to next-generation refrigerants to cope with environmental regulations and developed the new refrigerant R407H for freezers and refrigerators. R407H is a non-ozone depleting and non-flammable refrigerant and has approximately 62% lower global warming potential (GWP) than the commonly used R404A refrigerant. Going forward, we will continue to engage in the development of even lower GWP refrigerants. To accelerate and promote R&D in these areas, the Chemicals Division is responsible for ensuring the implementation of new product development, and the TIC is exploring the next generation of themes that will lead to the Chemicals business.

• Other Operations

R&D expenses for Other operations totaled ¥1.8 billion.

In oil hydraulics, Daikin is commercializing a large-capacity series of products and developing new applications by leveraging the special characteristics of its hybrid oil hydraulic system technology that combines oil hydraulic technology and inverter technology to realize energy conservation and high functionality that could not be attained with previously existing hydraulic systems. In the industrial press business, Daikin's "Super Unit" has won high acclaim for its low electric power consumption and resulting energy conservation. It also features low noise and lower heat emissions, and it contributes to the work environment through the use of a reduced-size oil tank, and reduces the burden on the environment. In addition, Daikin has launched a large-scale extruder system that equals electric power as a motive force for its responsiveness and energy conservation. This system can handle multiple voltages and has other features needed in Asia and other regions where adaptation to local conditions is needed. Daikin will expand this system's lineup, and it is being adopted in many locations where presses and other machines are needed. Daikin is adapting its products to additional uses globally and will move forward with sales expansion.

Also, Daikin is proceeding with the development of an energy conservation system for use on special vehicles. One of these units, a hydraulic hybrid system for use on vehicles, has already been adopted. In addition to conventional hydraulic systems, Daikin is proceeding with the development of advanced environmentally responsive products that go beyond the existing frameworks and will find applications globally.

In defense systems, Daikin conducts R&D related to artillery shell and guided missile components mainly for Japan's Ministry of Defense.

Dividend Policy and Dividends Applicable to the Fiscal Year

Daikin continues to make strategic investments and expand its business, while also proceeding with such structural reforms as those to promote comprehensive cost reductions and strengthen its financial position. The aim of these initiatives is to become a truly global excellent company and, at the same time, substantially augment corporate value.

Specifically, in accordance with its fundamental goal of providing a stable and continuous return to shareholders, Daikin is striving to keep its consolidated ratio of dividends on equity (DOE) at levels of 3% or above while also seeking to increase its consolidated dividend payout ratio and thereby further expand shareholder returns.

Internal reserves will be applied to strengthen the Daikin Group's business and financial position to accelerate the development of global businesses, further the development of environment-friendly products, and make strategic investments to expand business activities and strengthen competitiveness.

For the fiscal year ended March 31, 2017, Daikin increased its total cash dividend by ¥10 per share, to ¥130 per share (comprising an interim dividend of ¥60 per share and a year-end dividend of ¥70 per share). For the current fiscal year ending March 31, 2018, the Company plans to distribute a total annual dividend of ¥130 per share (comprising an interim dividend of ¥65 per share and a year-end dividend of ¥65 per share).

Outlook for Fiscal 2018

While the global economy is expected to steadily expand going forward, against the backdrop of the economic recovery in the United States and robust Chinese, Indian, and ASEAN economies, the outlook is also uncertain due to factors such as political risks in the United States and Europe and geopolitical risks in the Middle East and Asia.

Amid this business environment, for this year (2017), we set "Integrate new power with our solid foundation to enhance our corporate value" as the Group's New Year's slogan with the aim of generating results amid the uncertain outlook in the global situation. We will refine our efforts to strengthen our sales and marketing capabilities, improve product development, production, procurement, and quality capabilities, and enhance our human resources capabilities, which we have continued to implement, and further promote initiatives aimed at greater growth.

We should work toward reinforcing our production system, global research and development framework, and securing new technologies by making investments after ascertaining areas of common ground between pursuing medium- to long-term growth under "FUSION 20," the Group's strategic management plan, and securing short-term profit.

For the fiscal year ending March 31, 2018, we forecast a 7.1% increase in consolidated net sales, to ¥2,190 billion, with operating income rising 5.3%, to ¥243.0 billion, and net income attributable to owners of the parent company increasing 3.9%, to ¥160.0 billion. The estimated exchange rate for the fiscal year ending March 31, 2018, is based on the assumption that US$1 equals ¥108 and 1 euro equals ¥118.

Principal Risks Associated with the Daikin Group's Operations

Sharp changes in politico-economic conditions or supply-demand relationships in principal markets

The Group develops, manufactures, sells, and procures goods and services throughout the world, and there is a possibility that Group performance could be impacted due to changes in the business environment in the markets or regions in which the Group operates, such as political or economic trends, the introduction of more-stringent environmental regulations, increased competition from competitors, or sudden rises in the cost of raw materials. In addition, Daikin is attempting to further expand its manufacturing and sales network and enhance Groupwide profitability through investment such as the acquiring of air-conditioning equipment dealers or companies, such as the Goodman Global Group, Inc. (completed in 2012), and the establishment of manufacturing facilities. However, there is a possibility that the Group's performance could be impacted, depending on the state of progress of such activities.

Cold summer weather and other unusual weather patterns accompanied by changes in demand for air conditioners

Air-conditioning and refrigeration operations accounted for 89.8% of the Daikin Group's consolidated net sales in fiscal 2017. Therefore, the Group strives to accurately monitor weather information and weather-related demand trends in the world's principal markets. It also employs flexible manufacturing methods and marketing policies designed to minimize the impact of those demand trends on its performance. However, depending on the magnitude of demand changes resulting from cold summer weather or other unusual weather patterns, there is a possibility that the Group's performance could be impacted.

Large fluctuations in currency exchange rates

Overseas sales accounted for 74.6% of the Daikin Group's consolidated net sales in fiscal 2017. The acceleration of global business development going forward is expected to further elevate this overseas sales ratio. Consolidated financial statements are prepared by translating local currency-denominated items for Group operations in each global region, including sales, expenses, and assets. Accordingly, depending on currency exchange rates at the time of the currency translation, there may be an impact on yen translation values even when there has been no change in local currency-denominated figures. In addition, because the Group engages in foreign currency-denominated transactions in raw materials and component procurement and in the sale of goods and services, there is a possibility that changes in currency exchange rates could impact manufacturing costs and sales performance. To avoid such currency exchange rate-related risks, the Group undertakes short-term risk hedging via forward exchange contracts and similar instruments. Daikin also undertakes medium- to long-term measures to continuously adjust procurement and manufacturing operations and optimize them for changing currency exchange-rate trends, and to balance imports and exports in each currency. Through this, the Group works to realize a business structure that is not greatly impacted by changes in currency exchange rates. However, currency exchange rate-related risks cannot be completely avoided.

Major product quality claims

The Group strives to ensure thorough quality management for all its products, regardless of whether they are manufactured in Japan or overseas. With respect to new product development, all four related elements—design, production technology, and purchasing units and suppliers—work in an integrated manner to concurrently move ahead with the collaborative development of process innovation measures, aiming to implement innovations related to quality, costs, and product development speed. The Group also has purchased liability insurance to cover unexpected quality-related claims, but, in the case that a major quality claim situation were to occur, there is a possibility that it could have an impact on the Group's performance.

Major problems in manufacturing

The Group strives to implement thorough preventative maintenance measures at all its production facilities, regardless of whether they are in Japan or overseas. In addition, particularly with respect to the Chemicals business, the Group is working to strengthen its facility safety audits, security management systems, and other related systems. Moreover, with respect to manufacturing problems, the Group has purchased insurance to cover facility damage and foregone earnings, but, in the case that a major problem were to occur in manufacturing operations, there is a possibility that it could have an impact on the Group's performance.

Major changes in the market prices of securities and other assets

The Group's holdings of securities are primarily holdings designed to strengthen collaborative business expansion measures in cooperation with business partners and to strengthen relationships with business partners. However, in the case of large fluctuations in securities markets, bankruptcies of business partners, and similar situations, there is a possibility that it could have an impact on the Group's performance.

Impairment of long-lived assets

In connection with its business assets, goodwill generated on the occasion of corporate acquisitions, and similar items, the Group records various types of tangible and intangible long-lived assets. With respect to these assets, in cases going forward when such factors as performance trends and market price drops prevent the generation of expected cash flows, there may be cases in which the assets in question may require impairment treatment. In the case of such impairment of long-lived assets, there is a possibility that it could have an impact on the Group's performance.

Natural disasters

In the case that such natural disasters as major earthquakes and typhoons occur and exert an impact on the Group's manufacturing, marketing, and distribution bases, there is a possibility that it could have an impact on the Group's performance.

Consolidated Balance Sheet

Daikin Industries, Ltd. and Consolidated Subsidiaries
March 31, 2017

	Millions of Yen	
ASSETS	**2017**	2016
Current assets:		
Cash and cash equivalents (Notes 9 and 17)	**¥ 344,094**	¥ 291,206
Trade receivables (Notes 8, 9 and 17):		
Notes	**51,154**	50,730
Accounts	**317,907**	304,917
Allowance for doubtful receivables	**(8,216)**	(6,279)
Inventories (Note 3)	**358,303**	333,652
Deferred tax assets (Note 13)	**35,786**	33,987
Prepaid expenses and other current assets	**60,857**	58,556
Total current assets	**1,159,885**	1,066,769
Property, plant and equipment:		
Land	**37,589**	36,364
Buildings and structures	**335,654**	280,346
Machinery and equipment	**515,027**	495,660
Furniture and fixtures	**167,119**	163,060
Lease assets (Note 16)	**4,610**	5,692
Construction in progress	**29,592**	50,132
Total	**1,089,591**	1,031,254
Accumulated depreciation	**(665,064)**	(646,154)
Net property, plant and equipment	**424,527**	385,100
Investments and other assets:		
Investment securities (Notes 6, 9 and 17)	**179,206**	170,487
Investments in and advances to unconsolidated subsidiaries and associated companies	**20,260**	19,100
Goodwill (Note 7)	**330,876**	329,753
Customer relationships	**135,774**	124,672
Other intangible assets	**70,314**	64,436
Deferred tax assets (Note 13)	**5,048**	3,475
Assets for retirement benefits (Note 10)	**13,034**	11,540
Other assets	**17,225**	15,773
Total investments and other assets	**771,737**	739,236
Total	**¥2,356,149**	¥2,191,105

See notes to consolidated financial statements.

LIABILITIES AND EQUITY	Millions of Yen 2017	2016
Current liabilities:		
Short-term borrowings (Notes 9 and 17)	¥ 57,699	¥ 54,675
Current portion of long-term debt (Notes 9 and 17)	77,178	72,941
Current portion of long-term lease obligations (Note 16)	1,798	1,943
Trade payables (Note 17):		
Notes	8,971	7,959
Accounts	164,176	148,079
Income taxes payable (Note 17)	27,770	11,511
Deferred tax liabilities (Note 13)	23,769	24,581
Provision for product warranties	49,751	46,567
Accrued expenses (Note 8)	108,279	98,801
Other current liabilities (Note 8)	107,286	96,670
Total current liabilities	626,677	563,727
Long-term liabilities:		
Long-term debt (Notes 9 and 17)	463,292	477,492
Long-term lease obligations (Note 16)	9,463	1,930
Liabilities for retirement benefits (Note 10)	11,940	10,982
Deferred tax liabilities (Note 13)	87,994	78,029
Other long-term liabilities	21,174	21,475
Total long-term liabilities	593,863	589,908
Commitments and contingent liabilities (Notes 16 and 18)		
Equity (Notes 11, 12 and 22)**:**		
Common stock—authorized, 500,000,000 shares; issued 293,113,973 shares in 2017 and 2016	85,032	85,032
Capital surplus	84,545	83,585
Stock acquisition rights	1,080	1,119
Retained earnings	837,968	720,548
Treasury stock, at cost: 739,660 shares in 2017 and 1,075,356 shares in 2016	(3,160)	(4,598)
Accumulated other comprehensive income (loss):		
Unrealized gain on available-for-sale securities	53,042	46,320
Deferred loss on derivatives under hedge accounting	(120)	(2,124)
Foreign currency translation adjustments	61,037	93,798
Remeasurements of defined benefit plans	(6,708)	(8,152)
Subtotal	1,112,716	1,015,528
Noncontrolling interests	22,893	21,942
Total equity	1,135,609	1,037,470
Total	¥2,356,149	¥2,191,105

Consolidated Statement of Income

Daikin Industries, Ltd. and Consolidated Subsidiaries
Year Ended March 31, 2017

	Millions of Yen	
	2017	2016
Net sales (Note 8)	**¥2,043,969**	¥2,043,691
Cost of sales (Note 15)	**1,313,034**	1,332,115
Gross profit	**730,935**	711,576
Selling, general and administrative expenses (Notes 7, 8 and 15)	**500,166**	493,704
Operating income	**230,769**	217,872
Other (expenses) income:		
Interest and dividend income	**10,431**	10,637
Interest expense	**(9,910)**	(8,495)
Exchange gains (losses)	**330**	(11,279)
Gain on sales of land	**452**	
Losses on disposals of property, plant and equipment and other intangible assets	**(927)**	(1,078)
Losses on impairment of long-lived assets (Note 4)		(491)
Gains on sales of investment securities (Note 6)	**25**	112
Impairment losses on investment securities (Notes 6 and 17)		(605)
Gains on reversal of stock acquisition rights		4
Loss on restructuring of subsidiaries		(1,294)
Other—net	**(561)**	800
Other (expenses) income—net	**(160)**	(11,689)
Income before income taxes	**230,609**	206,183
Income taxes (Note 13)**:**		
Current	**70,217**	59,389
Deferred	**471**	4,702
Total income taxes	**70,688**	64,091
Net income	**159,921**	142,092
Net income attributable to noncontrolling interests	**(5,982)**	(5,105)
Net income attributable to owners of parent	**¥ 153,939**	¥ 136,987

	Yen	
Amounts per common share (Note 20)**:**		
Basic net income	**¥526.81**	¥469.23
Diluted net income	**526.43**	468.84
Cash dividends applicable to the year	**130.00**	120.00

See notes to consolidated financial statements.

Consolidated Statement of Comprehensive Income

Daikin Industries, Ltd. and Consolidated Subsidiaries
Year Ended March 31, 2017

	Millions of Yen	
	2017	2016
Net income	**¥159,921**	¥142,092
Other comprehensive loss (Note 19)**:**		
Unrealized gains (losses) on available-for-sale securities	**6,721**	(21,498)
Deferred gains (losses) on derivatives under hedge accounting	**2,004**	(1,659)
Foreign currency translation adjustments	**(32,609)**	(86,963)
Remeasurements of defined benefit plans	**1,448**	(5,573)
Share of other comprehensive loss in affiliates accounted for using the equity method	**(1,142)**	(809)
Total other comprehensive loss	**(23,578)**	(116,502)
Comprehensive income	**¥136,343**	¥ 25,590
Total comprehensive income attributable to:		
Owners of parent	**¥131,348**	¥ 22,489
Noncontrolling interests	**4,995**	3,101

See notes to consolidated financial statements.

Consolidated Statement of Changes in Equity

Daikin Industries, Ltd. and Consolidated Subsidiaries
Year Ended March 31, 2017

		Millions of Yen											
							Accumulated Other Comprehensive Income (Loss)						
	Outstanding Number of Common Shares Issued	Common Stock	Capital Surplus	Stock Acquisition Rights	Retained Earnings	Treasury Stock	Unrealized Gain on Available-for-Sale Securities	Deferred Loss on Derivatives under Hedge Accounting	Foreign Currency Translation Adjustments	Remeasure-ments of Defined Benefit Plans	Total	Noncontrol-ling Interests	Total Equity
Balance, April 1, 2015	291,833,321	¥85,032	¥83,444	¥ 993	¥617,129	¥(5,221)	¥67,819	¥ (464)	¥179,566	¥(2,580)	¥1,025,718	¥22,594	¥1,048,312
Net income					136,987						136,987		136,987
Cash dividends, ¥120 per share					(33,568)						(33,568)		(33,568)
Repurchase of treasury stock	(53,704)					(479)					(479)		(479)
Disposal of treasury stock	259,000		183			1,102					1,285		1,285
Change in parent's ownership interest due to transactions with noncontrolling interests			(42)								(42)		(42)
Net change in the year				126			(21,499)	(1,660)	(85,768)	(5,572)	(114,373)	(652)	(115,025)
Balance, March 31, 2016	**292,038,617**	**85,032**	**83,585**	**1,119**	**720,548**	**(4,598)**	**46,320**	**(2,124)**	**93,798**	**(8,152)**	**1,015,528**	**21,942**	**1,037,470**
Net income					**153,939**						**153,939**		**153,939**
Cash dividends, ¥130 per share					**(36,519)**						**(36,519)**		**(36,519)**
Repurchase of treasury stock	**(304)**					**(3)**					**(3)**		**(3)**
Disposal of treasury stock	**336,000**		**960**			**1,441**					**2,401**		**2,401**
Net change in the year				**(39)**			**6,722**	**2,004**	**(32,761)**	**1,444**	**(22,630)**	**951**	**(21,679)**
Balance, March 31, 2017	**292,374,313**	**¥85,032**	**¥84,545**	**¥1,080**	**¥837,968**	**¥(3,160)**	**¥53,042**	**¥ (120)**	**¥ 61,037**	**¥(6,708)**	**¥1,112,716**	**¥22,893**	**¥1,135,609**

See notes to consolidated financial statements.

Consolidated Statement of Cash Flows

Daikin Industries, Ltd. and Consolidated Subsidiaries
Year Ended March 31, 2017

	Millions of Yen	
	2017	2016
Operating activities:		
Income before income taxes	**¥230,609**	¥206,183
Adjustments for:		
Income taxes—paid	**(55,253)**	(72,930)
Depreciation and amortization	**85,029**	84,203
Losses on impairment of long-lived assets		491
Gains on sales of investment securities	**(25)**	(112)
Impairment losses on investment securities		605
Losses on disposals of property, plant and equipment and other intangible assets	**927**	1,078
Equity in (earnings) losses of unconsolidated subsidiaries and associated companies	**(920)**	83
Changes in assets and liabilities, net of effects of the purchase of subsidiaries:		
Trade notes and accounts receivable	**(13,440)**	(19,940)
Inventories	**(23,384)**	1,494
Other current assets	**364**	(2,869)
Assets for retirement benefits	**(1,333)**	7,998
Trade notes and accounts payable	**14,406**	10,318
Accrued expenses	**8,940**	7,733
Other current liabilities	**16,432**	10,166
Liabilities for retirement benefits	**1,289**	708
Other—net	**4,022**	(9,023)
Total adjustments	**37,054**	20,003
Net cash provided by operating activities	**267,663**	226,186
Investing activities:		
Payments for purchases of property, plant and equipment	**(88,335)**	(96,697)
Proceeds from sales of property, plant and equipment	**2,253**	992
Payments for acquisition of newly consolidated subsidiaries, net of cash and cash equivalents acquired (Note 14)	**(32,998)**	(1,311)
Proceed from sales of shares of subsidiary resulting in change in the scope of consolidation	**705**	
Payment for acquisition of shares of an associated company		(358)
Payments for transfer of business	**(1,870)**	(3,182)
Proceed from transfer of business		121
Payments for acquisition of investment securities	**(165)**	(2,587)
Proceeds from sales of investment securities (Note 6)	**46**	193
Other—net	**(8,459)**	(2,664)
Net cash used in investing activities	**(128,823)**	(105,493)
Financing activities:		
Net decrease in short-term borrowings	**(1,243)**	(2,839)
Proceeds from long-term debt	**60,295**	
Repayments of long-term debt (Note 14)	**(91,263)**	(40,076)
Cash dividends paid to owners of parent	**(36,519)**	(33,568)
Cash dividends paid to noncontrolling interests	**(4,265)**	(6,529)
Proceeds from issuance of shares to noncontrolling interests	**233**	
Other—net	**(782)**	(2,410)
Net cash used in financing activities	**(73,544)**	(85,422)
Effect of exchange rate changes on cash and cash equivalents	**(12,408)**	(31,015)
Net increase in cash and cash equivalents	**52,888**	4,256
Cash and cash equivalents, beginning of year	**291,206**	286,950
Cash and cash equivalents, end of year	**¥344,094**	¥291,206

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Daikin Industries, Ltd. and Consolidated Subsidiaries
Year Ended March 31, 2017

1. BASIS OF PRESENTATION OF CONSOLIDATED FINANCIAL STATEMENTS

The accompanying consolidated financial statements of Daikin Industries, Ltd. (the "Company") have been prepared in accordance with the provisions set forth in the Japanese Financial Instruments and Exchange Act and its related accounting regulations 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 of International Financial Reporting Standards (IFRSs).

In preparing these consolidated financial statements, certain reclassifications and rearrangements have been made to the Company's consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan.

In addition, certain reclassifications have been made in the 2016 consolidated financial statements to conform to the classification used in 2017.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a. Principles of Consolidation and Accounting for Investments in Unconsolidated Subsidiaries and Associated Companies - The accompanying consolidated financial statements include the accounts of the Company and its significant subsidiaries (collectively, the "Group").

Under the control and influence concepts, those companies in which the Company, directly or indirectly, is able to exercise control are fully consolidated, and those companies over which the Group has the ability to exercise significant influence are accounted for by the equity method.

The Group applies the equity method of accounting for investments in unconsolidated subsidiaries and associated companies except for certain insignificant companies. Investments in such insignificant companies are stated at cost, except investments for which the value has been permanently impaired, for which appropriate write-downs are recorded. If these subsidiaries and associated companies had been consolidated or accounted for using the equity method, respectively, the effect on the accompanying consolidated financial statements would not have been material.

All significant intercompany balances and transactions have been eliminated in consolidation. All material unrealized profit included in assets resulting from transactions within the Group is eliminated.

b. Unification of Accounting Policies Applied to Foreign Subsidiaries for the Consolidated Financial Statements - In accordance with the Accounting Standards Board of Japan ("ASBJ") Practical Issues Task Force ("PITF") No. 18, "Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries for the Consolidated Financial Statements," the accounting policies and procedures applied to a parent company and its subsidiaries for similar transactions and events under similar circumstances should, in principle, be unified for the preparation of the consolidated financial statements. However, financial statements prepared by foreign subsidiaries in accordance with either IFRSs or generally accepted accounting principles in the United States of America (Financial Accounting Standards Board Accounting Standards Codification—"FASB ASC") tentatively may be used for the consolidation process, except for the following items which should be adjusted in the consolidation process so that net income is accounted for in accordance with Japanese GAAP, unless they are not material: (a) amortization of goodwill; (b) scheduled amortization of actuarial gain or loss of pensions that has been recorded in equity through other comprehensive income; (c) expensing capitalized development costs of research and development; and (d) cancellation of the fair value model of accounting for property, plant and equipment and investment properties and incorporation of the cost model of accounting.

c. Unification of Accounting Policies Applied to Foreign Associated Companies for the Equity Method - In accordance with ASBJ Statement No. 16, "Accounting Standard for Equity Method of Accounting for Investments," adjustments are to be made to conform the associate's accounting policies for similar transactions and events under similar circumstances to those of the parent company when the associate's financial statements are used in applying the equity method unless it is impracticable to determine such adjustments. In addition, financial statements prepared by foreign associated companies in accordance with either IFRSs or generally accepted accounting principles in the United States of America ("U.S. GAAP") tentatively may be used in applying the equity method if the following items are adjusted so that net income is accounted for in accordance with Japanese GAAP, unless they are not material: (a) amortization of goodwill; (b) scheduled amortization of actuarial gain or loss of pensions that has been recorded in equity through other comprehensive income; (c) expensing capitalized development costs of research and development; and (d) cancellation of the fair value model of accounting for property, plant and equipment and investment properties and incorporation of the cost model of accounting.

d. Business Combinations - Business combinations are accounted for using the purchase method. Acquisition-related costs, such as advisory fees or professional fees, are accounted for as expenses in the periods in which the costs are incurred. If the initial accounting for a business combination is incomplete by the end of the reporting period in which the business combination occurs, an acquirer shall report in its financial statements provisional amounts for the items for which the accounting is incomplete. During the measurement period, which shall not exceed one year from the acquisition, the acquirer shall retrospectively adjust the provisional amounts recognized at the acquisition date to reflect new information obtained about facts and circumstances that existed as of the acquisition date and that would have affected the measurement of the amounts recognized as of that date. Such adjustments shall be recognized as if the accounting for the business combination had been completed at the acquisition date. A parent's ownership interest in a subsidiary might change if the parent purchases or sells ownership interests in its subsidiary. The carrying amount of noncontrolling interest is adjusted to reflect the change in the parent's ownership interest in its subsidiary while the parent retains its controlling interest in its subsidiary. Any difference between the fair value of the consideration received or paid and the amount by which the noncontrolling interest is adjusted is accounted for as capital surplus as long as the parent retains control over its subsidiary.

The Group acquired 100% of the equity interest of Flanders Holdings LLC on April 27, 2016 and accounted for this acquisition by the purchase method of accounting (see Note 5).

e. Cash Equivalents - Cash equivalents are short-term investments that are readily convertible into cash and exposed to insignificant risk of changes in value.

Cash equivalents include time deposits, which mature within three months of the date of acquisition. Time deposits that mature in more than three months, but within a year of the date of acquisition, are recorded as short-term investments. The Group had no short-term investments at March 31, 2017 and 2016.

f. Allowance for Doubtful Accounts - The allowance for doubtful accounts is stated in amounts considered to be appropriate based on the past credit loss experience and an evaluation of potential losses in receivables outstanding.

g. Inventories - Inventories of the Company and its consolidated domestic subsidiaries are stated at the lower of cost, principally determined by the average method, or net selling value. Inventories of consolidated foreign subsidiaries are stated at the lower of cost, principally determined by the average method, or market.

h. Property, Plant and Equipment - Property, plant and equipment are stated at cost. Depreciation of property, plant and equipment of the Company and its consolidated subsidiaries is principally computed by the straight-line method based on the estimated useful lives of the assets.

The range of useful lives is from 15 to 50 years for buildings and structures, and from 5 to 15 years for machinery and equipment. The useful lives for lease assets are the terms of the respective leases.

i. Asset Retirement Obligations - An asset retirement obligation is recorded for a legal obligation imposed either by law or contract that results from the acquisition, construction, development and normal operation of a tangible fixed asset and is associated with the retirement of such tangible fixed asset. The asset retirement obligation is recognized as the sum of the discounted cash flows required for the future asset retirement and is recorded in the period in which the obligation is incurred if a reasonable estimate can be made. If a reasonable estimate of the asset retirement obligation cannot be made in the period the asset retirement obligation is incurred, the liability should be recognized when a reasonable estimate of the asset retirement obligation can be made. Upon initial recognition of a liability for an asset retirement obligation, an asset retirement cost is capitalized by increasing the carrying amount of the related fixed asset by the amount of the liability. The asset retirement cost is subsequently allocated to expense through depreciation over the remaining useful life of the asset. Over time, the liability is accreted to its present value each period. Any subsequent revisions to the timing or the amount of the original estimate of undiscounted cash flows are reflected as an adjustment to the carrying amount of the liability and the capitalized amount of the related asset retirement cost.

j. Long-Lived Assets - The Group reviews its long-lived assets for impairment whenever events or changes in circumstance indicate the carrying amount of an asset or asset group may not be recoverable. An impairment loss is recognized if the carrying amount of an asset or asset group exceeds the sum of the undiscounted future cash flows expected to result from the continued use and eventual disposition of the asset or asset group. The impairment loss would be measured as the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of the discounted cash flows from the continued use and eventual disposition of the asset or the net selling price at disposition.

k. Leases - Finance lease transactions are capitalized by recognizing lease assets and lease obligations in the balance sheet.

In March 2007, the ASBJ issued ASBJ Statement No. 13, "Accounting Standard for Lease Transactions," which revised the previous accounting standard for lease transactions. The revised accounting standard permits leases that existed at the transition date and do not transfer ownership of the leased property to the lessee to continue to be accounted for as operating lease transactions.

The Company and its consolidated domestic subsidiaries applied the revised accounting standard effective April 1, 2008. In addition, the Company and its consolidated domestic subsidiaries continue to account for leases that existed at the transition date and that do not transfer ownership of the leased property to the lessee as operating lease transactions.

All other leases are accounted for as operating leases.

l. Investment Securities - All marketable securities held by the Group are classified as available-for-sale securities and are reported at fair value, with unrealized gains and losses, net of applicable taxes, reported in a separate component of equity. The cost of securities sold is principally determined based on the moving-average method.

Non-marketable available-for-sale securities are stated at cost principally determined by the moving-average method.

For other-than-temporary declines in fair value, available-for-sale securities are reduced to net realizable value by charging such losses to income.

m. Goodwill and Intangible Assets - Goodwill and intangible assets arise principally from business combinations. Goodwill represents the excess of the purchase price over the fair value of the identifiable net assets acquired. Goodwill is amortized over a period of 9 to 20 years. Intangible assets primarily include customer relationships. Customer relationships are amortized using the straight-line method over the estimated useful lives (mainly 30 years).

n. Provision for Product Warranties - The Group repairs or exchanges certain products without charge under specific circumstances. The provision for product warranties is stated in amounts considered to be appropriate based on the past experience and an evaluation of potential losses on the product warranties.

o. Employees' Retirement Benefits - The Company and its consolidated domestic subsidiaries have non-contributory funded pension plans covering substantially all of their employees. Certain consolidated foreign subsidiaries have pension plans.

The Company accounts for the liability for retirement benefits based on the projected benefit obligations and plan assets at the balance sheet date. The projected benefit obligations are attributed to periods on a benefit formula basis. Actuarial gains and losses and past service costs that are yet to be recognized in profit or loss are recognized within equity (accumulated other comprehensive income), after adjusting for tax effects and are recognized in profit or loss over certain periods (mainly 10 years) no longer than the expected average remaining service period of the employees. The discount rate is determined using a single weighted-average discount rate reflecting the estimated timing and amount of benefit payment.

p. Stock Options - The Company measures the cost of employee stock options based on the fair value at the date of grant and recognized as compensation expense over the vesting period as consideration for receiving goods or services. The Company accounts for stock options granted to nonemployees based on the fair value of either the stock options of the goods or services received. In the consolidated balance sheet, the stock options are presented as a stock acquisition right as a separate component of equity until exercised.

q. Foreign Currency Transactions - All short-term and long-term monetary receivables and payables denominated in foreign currencies are translated into Japanese yen at the exchange rates at the consolidated balance sheet date. The foreign exchange gains and losses from translation are recognized in the consolidated statement of income to the extent that they are not hedged by forward exchange contracts.

r. Foreign Currency Financial Statements - The balance sheet accounts of the consolidated foreign subsidiaries are translated into Japanese yen at the current exchange rate as of the balance sheet date except for equity, which is translated at the historical rate. Revenue and expense accounts of the consolidated foreign subsidiaries are translated into Japanese yen at the average exchange rate. Differences arising from such translations are shown as "foreign currency translation adjustments" under accumulated other comprehensive income in a separate component of equity.

s. Bonuses to Directors and Audit & Supervisory Board Members - Bonuses to Directors and Audit & Supervisory Board Members are accrued at the year-end to which such bonuses are attributable. Accrued bonuses are included in accrued expenses.

t. Income Taxes - The provision for current income taxes is computed based on income before income taxes included in the consolidated statement of income. The asset and liability approach is used to recognize deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. Deferred taxes are measured by applying currently enacted tax laws to the temporary differences.

The Company applied ASBJ Guidance No. 26, "Guidance on Recoverability of Deferred Tax Assets," effective April 1, 2016. There was no impact from this for the year ended March 31, 2017.

u. Derivative Financial Instruments - The Group uses foreign exchange forward contracts, currency swaps and currency options to manage foreign exchange risk associated with certain assets and liabilities denominated in foreign currencies.

The Group uses mainly interest rate swaps and interest rate options to manage its exposure to fluctuations in interest rates.

The Group uses commodity futures contracts to manage the risk of fluctuation of commodity prices for materials.

The Group does not enter into derivatives for trading or speculative purposes.

Derivative financial instruments are classified and accounted for as follows: (1) derivatives are principally recognized as either assets or liabilities and measured at fair value, and gains or losses on derivative transactions are recognized in the consolidated statement of income and (2) for derivatives used for hedging purposes, if such derivatives qualify for hedge accounting because of high correlation and effectiveness between the hedging instruments and the hedged items, gains or losses are deferred until maturity of the hedged transactions.

The interest rate swaps that qualify for hedge accounting and meet specific matching criteria are not remeasured at market value but the differential paid or received under the swap agreements is recognized and included in interest expense or income.

v. Amounts Per Common Share - Basic net income per common share is computed by dividing net income attributable to common shareholders by the weighted-average number of common shares outstanding for the period, retroactively adjusted for stock splits.

Diluted net EPS of common stock assumes full exercise of the outstanding stock options which have a dilutive effect at the beginning of year (or at the time of issuance).

Cash dividends per share presented in the accompanying consolidated statement of income are dividends applicable to the respective fiscal years including dividends to be paid after the end of the year.

w. New Accounting Pronouncements

Leases - On January 13, 2016, the International Accounting Standards Board issued IFRS 16 Leases. On February 25, 2016, the Financial Accounting Standards Board issued Accounting Standards Update (ASU) 2016-02 Leases (Topic 842). These standards require lessees to recognize most leases on the balance sheet thereby resulting in the recognition of lease assets and liabilities. The Company expects to apply IFRS 16 for annual periods beginning on or after January 1, 2019. The Company expects to apply ASU 2016-02 for annual periods beginning after December 15, 2019 and for the first quarter within annual periods beginning after December 15, 2020. The Group is currently assessing the impact that these new standards will have on the consolidated financial statements.

3. INVENTORIES

Inventories at March 31, 2017 and 2016 consisted of the following:

	Millions of Yen	
	2017	2016
Finished products and merchandise	**¥249,487**	¥232,018
Semifinished products and work in process	**42,250**	40,028
Raw materials and supplies	**66,566**	61,606
Total	**¥358,303**	¥333,652

4. LONG-LIVED ASSETS

The Group reviewed its long-lived assets for impairment for the years ended March 31, 2017 and 2016. Impairment losses recognized were mainly as follows:

March 31, 2016

Use	Location	Asset Category	Millions of Yen
Held for use	Settsu City, Osaka Prefecture	Machinery and equipment	**¥450**

The Group recognized impairment losses recorded in other expenses for those assets as the profitability of oil hydraulics business for industrial machinery is expected to decline due to economic downturn and sluggish demand in the Chinese market. The carrying amounts of the related assets were written down to the recoverable amount. The recoverable amounts of these assets were measured at value in use and the discount rate used for computation of the present value of future cash flows was 5%.

No impairment loss was recognized for the year ended March 31, 2017.

5. BUSINESS COMBINATIONS

Acquisition of an Entity during the Year Ended March 31, 2017

1. Outline of the business combination:

(1) Name and business contents of the acquiree:
Name: Flanders Holdings LLC
Business contents: Manufacture and sale of air filters and other related products

(2) Main reason for the business combination:
With this acquisition, Flanders Holdings LLC (hereinafter, "Flanders") will be integrated into American Air Filter Company, Inc. (hereinafter, "AAF"), enabling AAF to leverage its global sales network to market cleanroom equipment and high-end air filter products, which are the main products of Flanders. In addition to making AAF the leading manufacturer in the United States, which is reportedly the largest air filter market in the world, this integration will also position AAF as a leading company in the global market.

(3) Date of the business combination:
April 27, 2016

(4) Legal form of the business combination:
Acquisition of equity interests for cash considerations

(5) Name of the acquiree after business combination:
Flanders Holdings LLC

(6) Ratio of equity interests acquired:
100%

(7) Basis for determination of the acquirer:
AAF, a subsidiary of the Company, is regarded as the acquiring company since AAF acquired all equity interests of Flanders for cash consideration.

2. Period of operating results of the acquiree included in the consolidated financial statements:

From April 27, 2016, to March 31, 2017

3. Amount and breakdown of the acquisition costs:

Payment for acquisition of equity interests: Cash US$209 million (¥23,287 million)

4. Amount and breakdown of the main acquisition related costs:

Expenses related directly to the acquisition, including mainly advisory expenses: US$6 million (¥719 million)

5. Amount of goodwill recognized, reason for recognition, and method and period for amortization of goodwill:

(1) Amount of goodwill recognized: US$171 million (¥18,990 million)
(2) Reason for recognition: Future business activities are expected to generate excess profitability.
(3) Method and period for amortization of goodwill: Straight-line method over 13 years

6. Amount and breakdown of the assets acquired and the liabilities assumed at the acquisition date:

	Millions of USD	Millions of Yen
Current assets	$107	¥11,880
Fixed assets	418	46,492
Total assets	$525	¥58,372
Current liabilities	$222	¥24,703
Long-term liabilities	93	10,382
Total liabilities	$315	¥35,085

7. Amount of identifiable intangible assets other than goodwill, its details and major weighted-average useful life:

	Millions of USD	Millions of Yen	Weighted Average Useful Life
Customer relationships	$130	¥14,466	15
Trademarks	18	2,003	Non-amortizable
Technologies	2	256	11
Total	$150	¥16,725	

8. Even if this business combination had been completed as of April 1, 2016, the beginning of the fiscal year ended March 31, 2017, the Company believes the effect of consolidating this entity on the financial statements would be minor. Therefore, the pro forma financial information is omitted.

6. MARKETABLE AND INVESTMENT SECURITIES

The acquisition costs and aggregate fair values of marketable available-for-sale securities included in investment securities at March 31, 2017 and 2016 were as follows:

	Millions of Yen			
	2017			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities classified as available-for-sale:				
Equity securities	**¥99,121**	**¥71,961**	**¥(2,300)**	**¥168,782**
Debt securities	**325**	**1**		**326**
Total	**¥99,446**	**¥71,962**	**¥(2,300)**	**¥169,108**

	Millions of Yen			
	2016			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities classified as available-for-sale:				
Equity securities	¥98,754	¥63,907	¥(2,975)	¥159,686
Debt securities	350	1		351
Total	¥99,104	¥63,908	¥(2,975)	¥160,037

Available-for-sale securities that were sold during the years ended March 31, 2017 and 2016 were as follows:

	Millions of Yen		
March 31, 2017	Proceeds	Realized Gains	Realized Losses
Available-for-sale:			
Equity securities	**¥40**	**¥25**	

	Millions of Yen		
March 31, 2016	Proceeds	Realized Gains	Realized Losses
Available-for-sale:			
Equity securities	¥168	¥98	

The impairment loss on marketable available-for-sale securities for the year ended March 31, 2016 was ¥0.1 million. No impairment loss was recognized for the year ended March 31, 2017.

7. GOODWILL

Amortization expenses for goodwill were ¥25,735 million and ¥26,282 million for the years ended March 31, 2017 and 2016, respectively, which were included in selling, general and administrative expenses.

8. RELATED PARTY TRANSACTIONS

Material transactions and balances with related parties for the years ended March 31, 2017 and 2016 were as follows:

(1) 2017

(a) The Company

			Millions of Yen			
			Transactions		Resulting Account Balances	
Name	Description of Post	Ownership of the Company (%)	Description of Transaction	**2017**	Account	**2017**
Chiyono Terada	External Director/Chief Executive Officer (CEO) and President of Art Corporation	0.00	Commissions for moving business and delivery business	**¥488**	Accrued expenses and other current liabilities	**¥47**

(b) The Company's consolidated subsidiaries

			Millions of Yen			
			Transactions		Resulting Account Balances	
Name	Description of Post	Ownership of the Company (%)	Description of Transaction	**2017**	Account	**2017**
Chiyono Terada	External Director/CEO and President of Art Corporation	0.00	Commissions for moving business and delivery business	**¥ 56**	Accrued expenses and other current liabilities	**¥ 5**
			Sales of products	**143**	Accounts receivable	**22**

The terms and conditions applicable to the above-mentioned transactions have been determined on an arm's-length basis and by reference to the normal market price.

(2) 2016

(a) The Company

Name	Description of Post	Ownership of the Company (%)	Millions of Yen: Transactions: Description of Transaction	2016	Resulting Account Balances: Account	2016
Chiyono Terada	External Director/Chief Executive Officer (CEO) and President of Art Corporation	0.00	Commission for moving business and delivery business	¥535	Accrued expenses and other current liabilities	¥76

(b) The Company's consolidated subsidiaries

Name	Description of Post	Ownership of the Company (%)	Millions of Yen: Transactions: Description of Transaction	2016	Resulting Account Balances: Account	2016
Chiyono Terada	External Director/CEO and President of Art Corporation	0.00	Commission for moving business and delivery business	¥ 55	Accrued expenses and other current liabilities	¥ 5
			Sales of products	119	Accounts receivable	16

The terms and conditions applicable to the above-mentioned transactions have been determined on an arm's-length basis and by reference to the normal market price.

9. SHORT-TERM BORROWINGS AND LONG-TERM DEBT

Short-term borrowings of the Group at March 31, 2017 and 2016 consisted of the following:

	Millions of Yen: 2017	2016
Bank overdrafts and notes to banks	¥57,699	¥40,675
Commercial paper		14,000
Total	¥57,699	¥54,675

Unused short-term bank credit lines were ¥178,048 million at March 31, 2017. The weighted-average interest rates of bank overdrafts and notes to banks at March 31, 2017 and 2016 were 2.51% and 1.00%, respectively. The weighted-average interest rate of commercial paper at March 31, 2016 was 0.00%.

Long-term debt at March 31, 2017 and 2016 consisted of the following:

	Millions of Yen	
	2017	2016
1.42% unsecured bonds, due 2016		¥ 30,000
0.46% unsecured bonds, due 2017	**¥ 10,000**	10,000
1.86% unsecured bonds, due 2019	**40,000**	40,000
0.72% unsecured bonds, due 2019	**10,000**	10,000
0.38% unsecured bonds, due 2021	**10,000**	10,000
1.20% unsecured bonds, due 2022	**30,000**	30,000
0.68% unsecured bonds, due 2024	**10,000**	10,000
0.21% unsecured bonds, due 2026	**10,000**	
Unsecured loans from government-sponsored banks, with interest of 1.75%, due through 2019	**20,000**	20,000
Unsecured loans from banks and others, payable in foreign currencies, with interest ranging from 0.00% to 4.00% (2017) and from 0.90% to 4.00% (2016), due through 2026	**171,256**	140,816
Unsecured loans from banks and others with interest ranging from 0.11% to 3.60% (2017) and from 0.15% to 3.62% (2016), due through 2023	**229,214**	249,617
Total	**540,470**	550,433
Less current portion	**(77,178)**	(72,941)
Long-term debt, less current portion	**¥463,292**	¥477,492

Annual maturities of long-term debt outstanding at March 31, 2017 were as follows:

Year Ending March 31	Millions of Yen
2018	¥ 77,178
2019	78,208
2020	92,442
2021	94,625
2022	63,605
2023 and thereafter	134,412
Total	¥540,470

At March 31, 2017, investment securities with book values of ¥800 million, time deposit with a book value of ¥193 million and note receivables with book values of ¥399 million were pledged as collateral without corresponding borrowings.

As is customary in Japan, additional securities must be provided if requested by a lending bank. Certain banks have the right to offset cash deposited against any debt or obligation that becomes due, or, in case of default and certain other specified events, against all other debt payable to them. To date, none of the lenders have ever exercised these rights with respect to debt of the Group.

10. SEVERANCE INDEMNITIES AND PENSION PLANS

Under the Group's severance indemnities and pension plans, employees terminating their employment are, in most circumstances, entitled to severance and pension payments based on their average pay during their employment, length of service and certain other factors.

The Group accounts for part of the defined benefit obligations and benefit costs for retirement lump-sum payment using the simplified method.

1. Defined benefit plans

(1) The changes in defined benefit obligations for the years ended March 31, 2017 and 2016 were as follows (excluding the benefit plans for which the simplified method was applied):

	Millions of Yen	
	2017	2016
Balance at beginning of year	**¥95,395**	¥91,059
Service cost	**4,751**	5,229
Interest cost	**1,164**	1,913
Net actuarial losses	**4,647**	3,688
Past service cost		150
Benefits paid	**(3,752)**	(4,072)
Effect of changes in the scope of consolidation	**165**	266
Foreign currency translation adjustments	**(3,205)**	(3,018)
Others	**(6)**	180
Balance at end of year	**¥99,159**	¥95,395

(2) The changes in plan assets for the years ended March 31, 2017 and 2016 were as follows (excluding the benefit plan for which the simplified method was applied):

	Millions of Yen	
	2017	2016
Balance at beginning of year	**¥ 98,679**	¥102,450
Expected return on plan assets	**3,269**	3,796
Net actuarial gains (losses)	**4,257**	(4,690)
Contributions from the employer	**3,068**	3,186
Benefits paid	**(3,342)**	(3,576)
Effect of changes in the scope of consolidation	**(231)**	
Foreign currency translation adjustments	**(2,726)**	(2,488)
Others	**(17)**	1
Balance at end of year	**¥102,957**	¥ 98,679

(3) The changes in defined benefit obligation for the years ended March 31, 2017 and 2016 using the simplified method were as follows:

	Millions of Yen	
	2017	2016
Balance at beginning of year	**¥2,726**	¥2,674
Periodic benefit cost	**1,196**	1,046
Benefits paid	**(1,219)**	(994)
Balance at end of year	**¥2,703**	¥2,726

(4) Reconciliations between the liabilities recorded in the consolidated balance sheet and the balances of defined benefit obligation and plan assets at March 31, 2017 and 2016 were as follows (including the benefit plan for which the simplified method was applied):

	Millions of Yen	
	2017	2016
Funded defined benefit obligation	**¥ (95,868)**	¥(92,760)
Plan assets	**102,957**	98,679
Total	**7,089**	5,919
Unfunded defined benefit obligation	**(5,994)**	(5,361)
Net amount of liabilities and assets recorded in the consolidated balance sheet	**¥ 1,095**	¥ 558
Liabilities for retirement benefits	**¥ (11,939)**	¥(10,982)
Assets for retirement benefits	**13,034**	11,540
Net amount of liabilities and assets recorded in the consolidated balance sheet	**¥ 1,095**	¥ 558

(5) The components of net periodic benefit costs for the years ended March 31, 2017 and 2016 were as follows:

	Millions of Yen	
	2017	2016
Service cost	**¥4,751**	¥5,229
Interest cost	**1,163**	1,913
Expected return on plan assets	**(3,269)**	(3,796)
Recognized net actuarial losses (gains)	**2,039**	(103)
Amortization of past service cost	**(144)**	(218)
Periodic benefit cost calculated by the simplified method	**1,196**	1,046
Others	**(4)**	255
Subtotal (net periodic benefit costs)	**5,732**	4,326
Total	**¥5,732**	¥4,326

(6) Amounts recognized in other comprehensive income (before income tax effect) in respect of defined benefit plans for the years ended March 31, 2017 and 2016 were as follows:

	Millions of Yen	
	2017	2016
Past service cost	**¥ 432**	¥ 205
Net actuarial (losses) gains	**(2,826)**	7,887
Total	**¥(2,394)**	¥8,092

(7) Amounts recognized in accumulated other comprehensive income (before income tax effect) in respect of defined benefit plans for the years ended March 31, 2017 and 2016 were as follows:

	Millions of Yen	
	2017	2016
Unrecognized past service cost	**¥ (680)**	¥ (1,112)
Unrecognized net actuarial losses	**9,617**	12,443
Total	**¥8,937**	¥11,331

(8) Plan assets

(a) Components of plan assets

Plan assets at March 31, 2017 and 2016, consisted of the following:

	2017	2016
Domestic debt securities	6%	6%
Domestic equity securities	8	8
Foreign debt securities	22	25
Foreign equity securities	20	18
Insurance assets (general account)	17	17
Cash and deposits	1	1
Alternative investments	26	25
Total	100%	100%

(b) Method of determining the expected rate of return on plan assets

To determine the expected long-term rate of return on plan assets, we consider current and target asset allocations, as well as historical and expected returns on various categories of plan assets.

(9) Assumptions used for the years ended March 31, 2017 and 2016 were as follows:

	2017	2016
Discount rate	Mainly 0.3%	Mainly 0.3%
Expected rate of return on plan assets	Mainly 2.5%	Mainly 2.5%
Expected rate of future salary increases	Mainly 3.5%	Mainly 3.5%

2. Defined contribution plan

The amounts of contribution required for the defined contribution plan paid by the Company and its subsidiaries were ¥4,965 million and ¥4,742 million for the years ended March 31, 2017 and 2016, respectively.

11. EQUITY

Japanese companies are subject to the Companies Act of Japan (the "Companies Act"). The significant provisions in the Companies Act that affect financial and accounting matters are summarized below:

(a) Dividends

Under the Companies Act, companies can pay dividends at any time during the fiscal year in addition to the year-end dividend upon resolution at the shareholders' meeting. For companies that meet certain criteria including (1) having a Board of Directors, (2) having independent auditors, (3) having an Audit & Supervisory Board, and (4) the term of service of the directors being prescribed as one year rather than the normal two-year term by its articles of incorporation, the Board of Directors may declare dividends (except for dividends-in-kind) at any time during the fiscal year if the company has prescribed so in its articles of incorporation. However, the Company cannot do so because it does not meet all the above criteria.

The Companies Act permits companies to distribute dividends-in-kind (non-cash assets) to shareholders subject to a certain limitation and additional requirements.

Semiannual interim dividends may also be paid once a year upon resolution by the Board of Directors if the articles of incorporation of the Company so stipulate. The Companies Act provides certain limitations on the amounts available for dividends or the purchase of treasury stock. The limitation is defined as the amount available for distribution to the shareholders, but the amount of net assets after dividends must be maintained at no less than ¥3 million.

(b) Increases/Decreases and Transfer of Common Stock, Reserve and Surplus

The Companies Act requires that an amount equal to 10% of dividends must be appropriated as a legal reserve (a component of retained earnings) or as additional paid-in capital (a component of capital surplus), depending on the equity account that was charged upon the payment of such dividends, until the aggregate amount of legal reserve and additional paid-in capital equals 25% of the common stock. Under the Companies Act, the total amount of additional paid-in capital and legal reserve may be reversed without limitation. The Companies Act also provides that common stock, legal reserve, additional paid-in capital, other capital surplus and retained earnings can be transferred among the accounts within equity under certain conditions upon resolution of the shareholders.

(c) Treasury Stock and Treasury Stock Acquisition Rights

The Companies Act also provides for companies to purchase treasury stock and dispose of such treasury stock by resolution of the Board of Directors. The amount of treasury stock purchased cannot exceed the amount available for distribution to the shareholders which is determined by a specific formula.

Under the Companies Act, stock acquisition rights are presented as a separate component of equity.

The Companies Act also provides that companies can purchase both treasury stock acquisition rights and treasury stock. Such treasury stock acquisition rights are presented as a separate component of equity or deducted directly from stock acquisition rights.

12. STOCK OPTIONS

The stock options outstanding at March 31, 2017, were as follows:

Stock Option	Persons Granted	Number of Options Granted	Date of Grant	Exercise Price	Exercise Period
2010 Stock Option	8 directors 41 employees	290,000 shares	2010.7.14	¥3,050	From July 15, 2012 to July 14, 2016
2011 Stock Option	10 directors 39 employees	296,000 shares	2011.7.14	¥2,970	From July 15, 2013 to July 14, 2017
2012 Stock Option	10 directors 41 employees	300,000 shares	2012.7.13	¥2,186	From July 14, 2014 to July 13, 2018
2013 Stock Option	10 directors 38 employees	286,000 shares	2013.7.12	¥4,500	From July 13, 2015 to July 12, 2019
2014 Stock Option	9 directors 45 employees	310,000 shares	2014.7.14	¥6,715	From July 15, 2016 to July 14, 2020
2015 Stock Option	9 directors 46 employees	53,200 shares	2015.7.13	¥ 1	From July 14, 2018 to July 13, 2030
2016 Stock Option	8 directors 53 employees	58,100 shares	2016.7.14	¥ 1	From July 15, 2019 to July 14, 2031

The stock option activity was as follows:

	Shares							
	2009 Stock Option	2010 Stock Option	2011 Stock Option	2012 Stock Option	2013 Stock Option	2014 Stock Option	2015 Stock Option	2016 Stock Option
Year Ended March 31, 2016								
Vested								
April 1, 2015—Outstanding	8,000	16,000	36,000	87,000	286,000	310,000		
Granted							53,200	
Exercised	(4,000)	(10,000)	(16,000)	(51,000)	(178,000)			
Canceled	(4,000)							
March 31, 2016—Outstanding		6,000	20,000	36,000	108,000	310,000	53,200	
Year Ended March 31, 2017								
Vested								
April 1, 2016—Outstanding		6,000	20,000	36,000	108,000	310,000	53,200	
Granted								58,100
Exercised		(6,000)	(20,000)	(19,000)	(76,000)	(215,000)		
Canceled								
March 31, 2017—Outstanding				17,000	32,000	95,000	53,200	58,100
Exercise price	¥3,250	¥3,050	¥ 2,970	¥ 2,186	¥4,500	¥6,715	¥ 1	¥ 1
Average stock price at exercise	¥8,486	¥8,817	¥10,512	¥10,270	¥9,391	¥9,708		
Fair value price at grant date	¥ 899	¥1,113	¥ 935	¥ 676	¥1,220	¥1,697	¥7,726	¥7,859

The assumptions used to measure the fair value of 2016 Stock Option

Estimate method:	Black-Scholes option-pricing model
Volatility of stock price:	39.9%
Estimated remaining outstanding period:	9 years
Estimated dividend:	¥120 per share
Risk-free interest rate:	0.3%

13. INCOME TAXES

The Company and its domestic subsidiaries are subject to Japanese national and local income taxes that, in the aggregate, resulted in normal effective statutory tax rates of approximately 30.8% and 33.0% for the years ended March 31, 2017 and 2016, respectively.

The tax effects of significant temporary differences and tax loss carryforwards that resulted in deferred tax assets and liabilities at March 31, 2017 and 2016 were as follows:

	Millions of Yen	
	2017	2016
Deferred tax assets:		
Provision for product warranties	**¥ 14,696**	¥ 14,946
Inventories	**14,552**	14,293
Investment securities	**6,911**	6,774
Tax loss carryforwards	**9,908**	5,641
Deferred revenue	**6,485**	5,505
Software and other intangible assets	**6,012**	5,345
Accrued bonus	**3,973**	3,529
Liabilities for retirement benefits	**2,487**	2,246
Allowance for doubtful receivables	**1,747**	1,425
Foreign income tax credit	**184**	733
Other	**20,614**	17,664
Less valuation allowance	**(16,728)**	(16,669)
Total deferred tax assets	**¥ 70,841**	¥ 61,432
Deferred tax liabilities:		
Intangible assets	**¥ 69,574**	¥ 64,087
Undistributed earnings of consolidated subsidiaries	**33,483**	33,019
Unrealized gain on available-for-sale securities	**16,727**	14,694
Assets for retirement benefits	**4,216**	3,574
Deferred gains on sales of property	**1,375**	1,187
Other	**16,395**	10,019
Total deferred tax liabilities	**¥141,770**	¥126,580
Net deferred tax liabilities	**¥ (70,929)**	¥ (65,148)

A reconciliation between the normal effective statutory tax rates and the actual effective tax rates reflected in the accompanying consolidated statement of income for the year ended March 31, 2016 was as follows:

	2016
Normal effective statutory income tax rate	33.0%
Differences in foreign subsidiaries' tax rates	(6.5)
Amortization of goodwill	4.0
Taxes and tax effects on dividends from foreign subsidiaries	3.7
Valuation allowance	(1.4)
Permanently non-taxable income, such as dividend income	(1.2)
Tax credit for research and development	(1.1)
Permanently non-deductible expenses, such as entertainment expenses	0.5
Other - net	0.1
Actual effective income tax rate	31.1%

A reconciliation of the difference between the normal effective statutory tax rates and the actual effective tax rates is not disclosed since the difference is less than 5% of the normal effective statutory income tax rate for the year ended March 31, 2017.

On November 18, 2016, the Tax Reform Act was enacted in Japan to change the normal effective statutory tax rate used in the calculation of deferred tax assets and deferred tax liabilities for the year ended March 31, 2017, from the figures used for the year ended March 31, 2016. It resulted in a change in the deferred tax liabilities (net of deferred tax assets) and income taxes—deferred recorded in the year ended March 31, 2017. The effect of this change on the consolidated financial statements is not material.

At March 31, 2017, the Company and certain consolidated subsidiaries had tax loss carryforwards aggregating ¥30,698 million, which are available to be offset against taxable income of the Company and such subsidiaries in future years. These tax loss carryforwards, if not utilized, will expire as follows:

Year Ending March 31	Millions of Yen
2018	¥ 1,292
2019	315
2020	696
2021	825
2022	573
2023 and thereafter	26,997
Total	¥30,698

14. SUPPLEMENTAL CASH FLOW INFORMATION

The Group acquired Flanders Holdings LLC and its subsidiaries during the year ended March 31, 2017.

Reconciliation between cash paid for the equity interest of Flanders Holdings LLC and payment for the acquisition of these newly consolidated subsidiaries, net of cash and cash equivalents acquired, was as follows:

	Millions of Yen
	2017
Current assets	**¥11,880**
Fixed assets	**27,501**
Goodwill	**18,991**
Current liabilities	**(24,703)**
Long-term liabilities	**(10,382)**
Cash paid for the equity interest	**23,287**
Cash and cash equivalents of consolidated subsidiaries	**(834)**
Payment for acquisition of equity interest of newly consolidated subsidiaries, net of cash and cash equivalents acquired	**¥22,453**

Repayments of long-term debt included ¥18,336 million for repayments of long-term debt by Flanders Holdings LLC and the other companies which the Group acquired for the year ended March 31, 2017.

15. RESEARCH AND DEVELOPMENT COSTS

Research and development costs included in cost of sales and selling, general and administrative expenses were ¥53,870 million and ¥46,138 million for the years ended March 31, 2017 and 2016, respectively.

16. LEASES

The Group leases certain computer equipment and other assets.

Obligations under finance leases and future minimum payments under noncancelable operating leases at March 31, 2017 were as follows:

	Millions of Yen	
	Finance Leases	Operating Leases
Due within one year	**¥ 1,798**	**¥17,091**
Due after one year	**9,463**	**39,719**
Total	**¥11,261**	**¥56,810**

17. FINANCIAL INSTRUMENTS AND RELATED DISCLOSURES

Group policy for financial instruments

The Group uses financial instruments, mainly bank loans and bonds, based on its capital financing plan. Short-term bank loans and commercial paper are used to fund the Group's ongoing operations, and cash surpluses are invested in low-risk financial assets. Derivatives are not used for speculative purposes, but to manage exposure to financial risks as described below.

Nature and extent of risks arising from financial instruments and risk management for financial instruments

Receivables, such as trade notes and trade accounts, are exposed to customer credit risk. The Group manages its credit risk from receivables based on the internal policies, which include monitoring of payment terms and balances of major customers to identify the default risk of the customers.

Payment terms of payables, such as trade notes and trade accounts, are less than one year.

Although receivables and payables in foreign currencies are exposed to the market risk of fluctuation in foreign currency exchange rates, the net position of receivables and payables in each foreign currency is hedged by using mainly forward foreign currency contracts and currency swaps. In addition, receivables and payables in foreign currencies which are expected from forecasted transactions are hedged by using forward foreign currency contracts and currency swaps.

Investment securities, mainly equity instruments of customers and suppliers of the Group, are exposed to the risk of market price fluctuations. Investment securities are periodically managed by monitoring market values and financial position of issuers.

Short-term bank loans and commercial paper are mainly used to fund the Group's ongoing operations. Long-term bank loans and bonds are used mainly for capital expenditures. Although the payables such as trade notes and trade accounts, bank loans and bonds are exposed to liquidity risk, the Group manages the liquidity risk through adequate financial planning by the corporate finance department. In addition, the Group has short-term bank credit lines. Some long-term bank loans are exposed to market risks from changes in interest rates, which are hedged by mainly using interest rate swaps.

Derivatives mainly include forward foreign currency contracts, interest rate swaps and commodity futures contracts, which are used to manage exposure to market risks from changes in foreign currency exchange rates of receivables and payables, interest rates of bank loans, and market value fluctuation of raw materials.

Derivative transactions entered into by the Group have been made in accordance with internal policies which regulate the authorization and credit limit amount.

Because the counterparties to these derivatives are limited to financial institutions with high creditworthiness, the Group does not anticipate any losses arising from credit risk.

Fair values of financial instruments

The carrying amounts, fair values and unrealized loss of significant financial instruments were as follows. Fair values of financial instruments are based on quoted price in active markets. If a quoted price is not available, another rational valuation technique is used instead. Instruments whose fair values cannot be readily determined are not included in the following.

	Millions of Yen		
	March 31, 2017		
	Carrying Amount	Fair Value	Unrealized Loss
Cash and cash equivalents	**¥344,094**	**¥344,094**	
Trade notes and accounts receivable	**369,061**	**369,061**	
Investment securities	**169,108**	**169,108**	
Total	**¥882,263**	**¥882,263**	
Trade notes and accounts payable	**¥173,147**	**¥173,147**	
Short-term borrowings	**57,699**	**57,699**	
Income taxes payable	**27,770**	**27,770**	
Long-term debt	**540,470**	**546,631**	**¥6,161**
Total	**¥799,086**	**¥805,247**	**¥6,161**
Derivatives	**¥ (1,363)**	**¥ (1,363)**	

	Millions of Yen		
	March 31, 2016		
	Carrying Amount	Fair Value	Unrealized Loss
Cash and cash equivalents	¥291,206	¥291,206	
Trade notes and accounts receivable	355,647	355,647	
Investment securities	160,037	160,037	
Total	¥806,890	¥806,890	
Trade notes and accounts payable	¥156,038	¥156,038	
Short-term borrowings	54,675	54,675	
Income taxes payable	11,511	11,511	
Long-term debt	550,433	560,212	¥9,779
Total	¥772,657	¥782,436	¥9,779
Derivatives	¥ (3,444)	¥ (3,444)	

Assets

Cash and cash equivalents

The carrying values of cash and cash equivalents approximate fair value because of their short maturities.

Trade notes and accounts receivable

The carrying values of trade notes and accounts receivable approximate fair value because of their short maturities.

Investment securities

The fair values of equity securities are measured at the quoted market prices of the stock exchange for the equity instruments, and the fair values of debt securities are measured at the amounts to be received through maturity discounted at the Group's assumed corporate discount rate. Fair value information for investment securities by classification is included in Note 6.

Liabilities

Trade notes and accounts payable, short-term borrowings and income taxes payable

The carrying values of trade notes and accounts payable, short-term borrowings and income taxes payable approximate fair value because of their short maturities.

Long-term debt

The fair values of bonds are determined at the quoted market prices of the over-the-counter market for the corporate bonds, and the fair values of long-term loans are determined by discounting the cash flows related to the loans at the Group's assumed corporate borrowing rate. The fair values of long-term loans with floating interest rates, which are hedged by the interest rate swaps that qualify for hedge accounting and meet specific matching criteria, are determined by discounting the cash flows related to the loans and the interest rate swaps at the Group's assumed corporate borrowing rate.

Derivatives

The fair values of derivatives are measured at the quoted price obtained from the financial institution.

The contracts or notional amounts of derivatives that are shown in the table below do not represent the amounts exchanged by the parties and do not measure the Group's exposure to credit or market risk.

Derivative transactions to which hedge accounting is not applied

	Millions of Yen			
	March 31, 2017			
	Contract Amount	Contract Amount Due after One Year	Fair Value	Unrealized Gain (Loss)
Forward exchange contracts:				
Selling: GBP	¥ 4,777		¥ (31)	¥ (31)
EUR	32,805		158	158
USD	39,742		431	431
AUD	7,263		21	21
ZAR	731		6	6
CZK	2,769		27	27
HKD	1,041		24	24
SGD	1,445		16	16
MYR	744		(3)	(3)
TRY	1,757		2	2
IDR	3,163		(8)	(8)
INR	1,458		(37)	(37)
Buying: CNY	1,140		16	16
Commodity futures contracts:				
Buying: Metal	¥ 2,699		¥ 2	¥ 2

	Millions of Yen			
	March 31, 2016			
	Contract Amount	Contract Amount Due after One Year	Fair Value	Unrealized Gain (Loss)
Forward exchange contracts:				
Selling: GBP	¥ 5,535		¥ 65	¥ 65
EUR	42,015		(49)	(49)
USD	18,385		103	103
AUD	5,869		(281)	(281)
ZAR	655		(15)	(15)
CZK	1,813		7	7
HKD	1,261		23	23
PLN	188		(0)	(0)
SGD	2,027		(55)	(55)
MYR	985		(58)	(58)
TRY	8,214		(48)	(48)
BRL	18		(3)	(3)
IDR	2,947		(59)	(59)
INR	676		(6)	(6)
Buying: CNY	1,391		(67)	(67)
MYR	9,353		411	411
Commodity futures contracts:				
Buying: Metal	¥ 688		¥ (39)	¥ (39)

Derivative transactions to which hedge accounting is applied

		Millions of Yen		
		March 31, 2017		
	Hedged Item	Contract Amount	Contract Amount Due after One Year	Fair Value
Forward exchange contracts:				
Selling: GBP	Receivables	**¥ 5,701**		**¥ (5)**
EUR	Receivables	**37,769**		**(276)**
USD	Receivables	**6,340**		**20**
ZAR	Receivables	**1,138**		**(10)**
CZK	Receivables	**6,743**		**53**
PLN	Receivables	**1,220**		**(30)**
TRY	Receivables	**2,310**		**24**
Buying: CNY	Payables	**5,702**		**9**
Interest rate swaps:				
Fixed-rate payment, floating-rate receipt	Long-term debt	**¥184,898**	**¥171,996**	**¥(1,773)**
Fixed-rate payment, floating-rate receipt*	Long-term debt	**129,200**	**98,000**	

	Hedged Item	Millions of Yen March 31, 2016 Contract Amount	Contract Amount Due after One Year	Fair Value
Forward exchange contracts:				
Selling: GBP	Receivables	¥ 7,378		¥ 291
EUR	Receivables	41,319		(212)
USD	Receivables	2,455		73
ZAR	Receivables	885		6
CZK	Receivables	7,596		(259)
PLN	Receivables	1,156		(21)
TRY	Receivables	3,528		(64)
Buying: CNY	Payables	4,521		(131)
Interest rate swaps:				
Fixed-rate payment, floating-rate receipt	Long-term debt	¥174,601	¥162,776	¥(3,057)
Fixed-rate payment, floating-rate receipt*	Long-term debt	149,600	129,200	

* The above interest rate swaps that qualify for hedge accounting and meet specific matching criterion are not remeasured at market value, but the differential paid or received under the swap agreements is recognized and included in interest expense or income. In addition, the fair values of such interest rate swaps are included in long-term debt.

Financial instruments whose fair values cannot be readily determinable

	Millions of Yen Carrying Amount 2017	2016
Nonlisted equity securities	**¥ 9,413**	¥ 9,565
Investments in limited partnerships and other investments	**685**	885
Total	**¥10,098**	¥10,450

The impairment losses on nonlisted equity securities for the year ended March 31, 2016 were ¥605 million.

Maturity analysis for financial assets and securities with contractual maturities

	Millions of Yen **March 31, 2017** Due in One Year or Less	Due after One Year through Five Years	Due after Five Years through Ten Years	Due after Ten Years
Cash and cash equivalents	**¥344,094**			
Trade notes and accounts receivable	**369,032**	**¥29**		
Investment securities:				
Available-for-sale securities with contractual maturities (corporate bonds)	**25**			**¥300**
Total	**¥713,151**	**¥29**		**¥300**

	Millions of Yen March 31, 2016 Due in One Year or Less	Due after One Year through Five Years	Due after Five Years through Ten Years	Due after Ten Years
Cash and cash equivalents	¥291,206			
Trade notes and accounts receivable	355,599	¥48		
Investment securities:				
Available-for-sale securities with contractual maturities (corporate bonds)	25	25		¥300
Total	¥646,830	¥73		¥300

Please see Note 9 for annual maturities of long-term debt.

18. COMMITMENTS AND CONTINGENT LIABILITIES

Commitments for capital expenditures outstanding at March 31, 2017 totaled approximately ¥7,922 million.

At March 31, 2017, contingent liabilities for trade notes endorsed and repurchase obligation for liquidation of notes receivables totaled ¥4,118 million and ¥221 million, respectively.

19. COMPREHENSIVE INCOME

The components of other comprehensive loss for the years ended March 31, 2017 and 2016 were as follows:

	Millions of Yen	
	2017	2016
Unrealized gains (losses) on available-for-sale securities:		
Gains (losses) arising during the year	**¥ 8,780**	¥ (31,523)
Reclassification adjustments to profit or loss	**(25)**	(98)
Amount before income tax effect	**8,755**	(31,621)
Income tax effect	**(2,034)**	10,123
Total	**¥ 6,721**	¥ (21,498)
Deferred gains (losses) on derivatives under hedge accounting:		
Gains (losses) arising during the year	**¥ 3,487**	¥ (3,786)
Reclassification adjustments to profit or loss	**(395)**	1,278
Amount before income tax effect	**3,092**	(2,508)
Income tax effect	**(1,088)**	849
Total	**¥ 2,004**	¥ (1,659)
Foreign currency translation adjustments:		
Adjustments arising during the year	**¥(32,921)**	¥ (86,950)
Reclassification adjustments to profit or loss	**312**	(13)
Amount before income tax effect	**(32,609)**	(86,963)
Total	**¥(32,609)**	¥ (86,963)
Remeasurements of defined benefit plans:		
Adjustments arising during the year	**¥ 502**	¥ (7,771)
Reclassification adjustments to profit or loss	**1,892**	(321)
Amount before income tax effect	**2,394**	(8,092)
Income tax effect	**(946)**	2,519
Total	**¥ 1,448**	¥ (5,573)
Share of other comprehensive income in affiliates accounted for using the equity method:		
Adjustments arising during the year	**¥ (1,142)**	¥ (809)
Total other comprehensive loss	**¥(23,578)**	¥(116,502)

20. NET INCOME PER SHARE

Reconciliations of the differences between basic and diluted net income per share (EPS) for the years ended March 31, 2017 and 2016 were as follows:

	Millions of Yen	Thousands of Shares	Yen
Year Ended March 31, 2017	Net Income	Weighted-Average Shares	EPS
Basic EPS:			
Net income available to common shareholders	**¥153,939**	**292,208**	**¥526.81**
Effect of dilutive securities:			
Stock options		**214**	
Diluted EPS:			
Net income for computation	**¥153,939**	**292,422**	**¥526.43**

	Millions of Yen	Thousands of Shares	Yen
Year Ended March 31, 2016	Net Income	Weighted-Average Shares	EPS
Basic EPS:			
Net income available to common shareholders	¥136,987	291,942	¥469.23
Effect of dilutive securities:			
Stock options		239	
Diluted EPS:			
Net income for computation	¥136,987	292,181	¥468.84

21. SEGMENT INFORMATION

Under ASBJ Statement No. 17, "Accounting Standard for Segment Information Disclosures," and ASBJ Guidance No. 20, "Guidance on Accounting Standard for Segment Information Disclosures," an entity is required to report financial and descriptive information about its reportable segments. Reportable segments are operating segments or aggregations of operating segments that meet specified criteria. Operating segments are components of an entity about which separate financial information is available and such information is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. Generally, segment information is required to be reported on the same basis as is used internally for evaluating operating segment performance and deciding how to allocate resources to operating segments.

1. Description of reportable segments

The Group's reportable segments are those for which separate financial information is available and regularly evaluated by the Company's Board of Directors in order to decide how resources are allocated among the Group. Therefore, the Group's reportable segments consist of the Air Conditioning segment and the Chemicals segment.

The Air Conditioning segment manufactures, distributes and installs air conditioning and refrigeration equipment. The Chemicals segment manufactures and distributes chemicals.

2. Methods of measurement for the amounts of sales, profit, assets and other items for each reportable segment

The accounting policies of each reportable segment are generally consistent with those disclosed in Note 2, "Summary of Significant Accounting Policies."

3. Information about sales, profit, assets and other items

	Millions of Yen						
	March 31, 2017						
	Reportable Segment						
	Air Conditioning	Chemicals	Total	Other	Total	Reconciliations	Consolidated
Sales:							
Sales to external customers	¥1,835,377	¥156,754	¥1,992,131	¥51,838	¥2,043,969		¥2,043,969
Intersegment sales	389	12,265	12,654	520	13,174	¥ (13,174)	
Total	1,835,766	169,019	2,004,785	52,358	2,057,143	(13,174)	2,043,969
Segment profit	208,750	18,302	227,052	3,750	230,802	(33)	230,769
Segment assets	1,943,887	191,049	2,134,936	34,641	2,169,577	186,572	2,356,149
Other:							
Depreciation	¥ 46,057	¥ 11,600	¥ 57,657	¥ 1,621	¥ 59,278		¥ 59,278
Amortization of goodwill	25,735		25,735		25,735		25,735
Investment balance in unconsolidated subsidiaries and associated companies accounted for using the equity method	11,596	6,709	18,305		18,305		18,305
Investment in property, plant and equipment and intangible assets	76,389	12,552	88,941	1,404	90,345		90,345

	Millions of Yen						
	March 31, 2016						
	Reportable Segment						
	Air Conditioning	Chemicals	Total	Other	Total	Reconciliations	Consolidated
Sales:							
Sales to external customers	¥1,828,012	¥162,286	¥1,990,298	¥53,393	¥2,043,691		¥2,043,691
Intersegment sales	614	10,295	10,909	500	11,409	¥ (11,409)	
Total	1,828,626	172,581	2,001,207	53,893	2,055,100	(11,409)	2,043,691
Segment profit	193,786	20,621	214,407	3,529	217,936	(64)	217,872
Segment assets	1,798,333	189,508	1,987,841	35,370	2,023,211	167,894	2,191,105
Other:							
Depreciation	¥ 44,326	¥ 12,055	¥ 56,381	¥ 1,527	¥ 57,908		¥ 57,908
Amortization of goodwill	26,183	99	26,282		26,282		26,282
Investment balance in unconsolidated subsidiaries and associated companies accounted for using the equity method	11,815	6,798	18,613		18,613		18,613
Investment in property, plant and equipment and intangible assets	90,617	18,157	108,774	3,938	112,712		112,712

Notes: 1. The Other segment is the aggregation of other operating segments which are not included in the reportable segments and consists of the Oil Hydraulics segment, the Defense segment and the Electronics segment.
2. “Reconciliations” include unallocated items and intersegment eliminations. The unallocated corporate assets included in “Reconciliations” amounted to ¥190,001 million and ¥173,176 million at March 31, 2017 and 2016, respectively, which consisted mainly of the Company’s cash, time deposits and investment securities.
3. The aggregated amount of segment profit equals operating income in the consolidated statement of income.
4. Intersegment sales are recorded at values that approximate market prices.

4. Supplemental information

(1) Information about geographical areas

(a) Sales

	Millions of Yen						
	March 31, 2017						
	Japan	USA	China	Asia and Oceania	Europe	Other	Consolidated
	¥518,453	**¥503,489**	**¥329,247**	**¥303,417**	**¥274,055**	**¥115,308**	**¥2,043,969**

	Millions of Yen						
	March 31, 2016						
	Japan	USA	China	Asia and Oceania	Europe	Other	Consolidated
	¥502,233	¥484,951	¥349,266	¥304,626	¥276,587	¥126,028	¥2,043,691

Note: Sales are classified by country or region based on the physical locations of customers.

(b) Property, plant and equipment

	Millions of Yen						
	March 31, 2017						
	Japan	USA	China	Asia and Oceania	Europe	Other	Consolidated
	¥140,563	**¥128,484**	**¥70,230**	**¥43,093**	**¥33,093**	**¥9,064**	**¥424,527**

	Millions of Yen						
	March 31, 2016						
	Japan	USA	China	Asia and Oceania	Europe	Other	Consolidated
	¥140,641	¥91,187	¥77,981	¥34,957	¥31,379	¥8,955	¥385,100

(2) Significant impairment losses on long-lived assets by reportable segment

	Millions of Yen				
	March 31, 2016				
	Air Conditioning	Chemicals	Other	Eliminations and Corporate	Consolidated
Impairment losses on long-lived assets	¥41		¥450		¥491

Note: The impairment losses reported in “Other” are related to the Oil Hydraulics segment.

(3) Information about goodwill

(a) Balance of goodwill by reportable segment

Goodwill for each reportable segment at March 31, 2017 and 2016 was as follows:

	Millions of Yen				
	2017				
	Air Conditioning	Chemicals	Other	Eliminations and Corporate	Consolidated
Goodwill	**¥330,876**				**¥330,876**

	Millions of Yen				
	2016				
	Air Conditioning	Chemicals	Other	Eliminations and Corporate	Consolidated
Goodwill	¥329,753				¥329,753

22. SUBSEQUENT EVENTS

Resolutions approved by the Company's Board of Directors at the meeting held on May 10, 2017 are subject to approval at the general shareholders' meeting planned to be held on June 29, 2017.

Appropriations of Retained Earnings

Payment of year-end cash dividends of ¥70 per share to shareholders at March 31, 2017, totaling ¥20,467 million is to be resolved.

Independent Auditors' Report

Deloitte.

Deloitte Touche Tohmatsu LLC
Yodoyabashi Mitsui Building
4-1-1 Imabashi, Chuo-ku
Osaka 541-0042
Japan

Tel: +81 (6) 4560 6000
Fax: +81 (6) 4560 6001
www.deloitte.com/jp/en

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of Daikin Industries, Ltd.:

We have audited the accompanying consolidated balance sheet of Daikin Industries, Ltd. and its consolidated subsidiaries as of March 31, 2017, and the related consolidated statements of income, comprehensive income, changes in equity, and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in Japan, and for 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.

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Daikin Industries, Ltd. and its consolidated subsidiaries as of March 31, 2017, and the consolidated results of their operations and their cash flows for the year then ended in accordance with accounting principles generally accepted in Japan.

Deloitte Touche Tohmatsu LLC

June 27, 2017

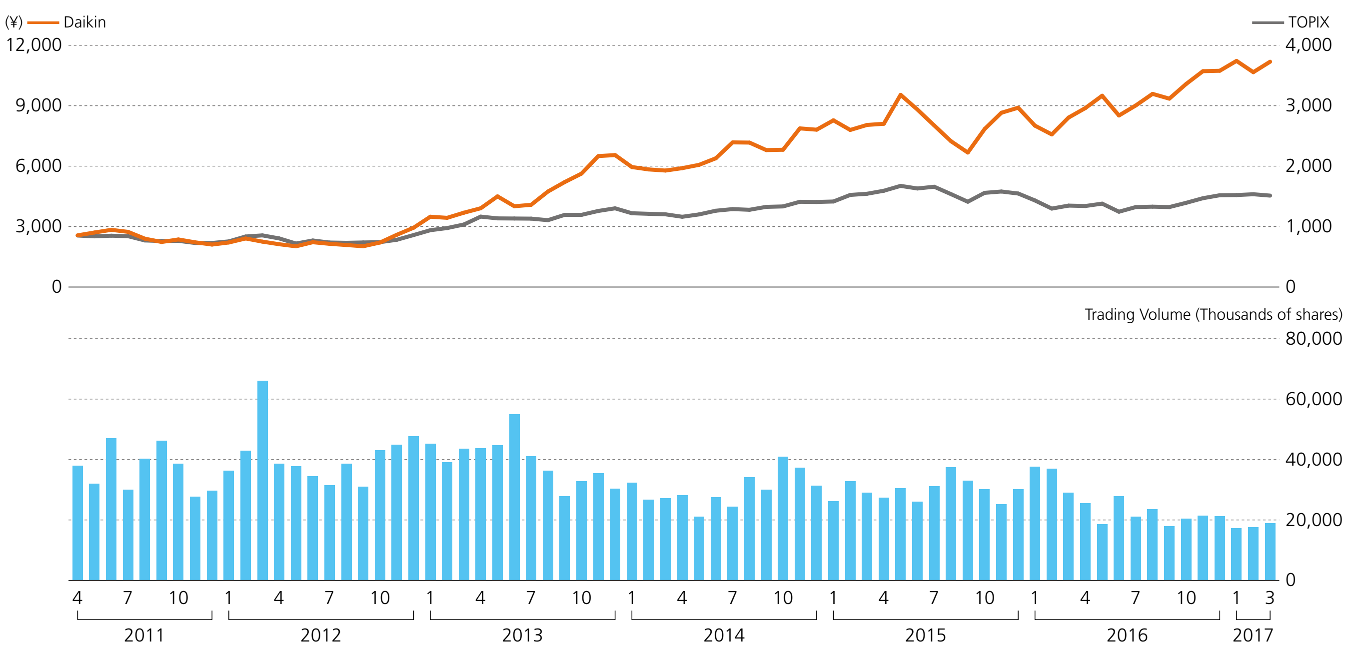
Member of
Deloitte Touche Tohmatsu Limited

Corporate Data

(As of March 31, 2017)

Company Name	Daikin Industries, Ltd.
Head Office	Umeda Center Bldg., 2-4-12, Nakazaki-Nishi, Kita-ku, Osaka 530-8323, Japan Phone: 81-6-6373-4312 URL: http://www.daikin.com/
Tokyo Office	JR Shinagawa East Bldg., 2-18-1, Konan, Minato-ku, Tokyo 108-0075, Japan Phone: 81-3-6716-0111
Fiscal Year-End Date	March 31 on an annual basis
Date of Founding	October 25, 1924
Date of Establishment	February 11, 1934
Paid-in Capital	¥85,032 million
Number of Shares of Common Stock Issued	293,113 thousand
Number of Shareholders	24,146
Major Shareholders	• The Master Trust Bank of Japan, Ltd. (Trust Account) • Japan Trustee Services Bank, Ltd. (Trust Account) • Sumitomo Mitsui Banking Corporation • Japan Trustee Services Bank, Ltd. (Trust Account 5) • Japan Trustee Services Bank, Ltd. Retirement Benefit Trust Account for The Norinchukin Bank • The Bank of Tokyo-Mitsubishi UFJ, Ltd. • CBNY-GOVERNMENT OF NORWAY • Japan Trustee Services Bank, Ltd. (Trust Account 4) • Trust & Custody Services Bank, Ltd. (Securities Inv. Trust Account) • State Street Bank and Trust Company
Number of Subsidiaries and Affiliated Companies	Subsidiaries: 245 Affiliates: 18
Number of Employees	67,036 (Consolidated)
Stock Exchange Listing	Tokyo
Advertising Method	The Company uses the electronic advertising method, posting advertisements on its website (http://www.daikin.co.jp/e-koukoku/). However, when electronic advertising is not possible due to technical problems or other circumstances, the Company will post advertisements in the *Nikkei Shimbun*.
Shareholder Register Administrator	Mitsubishi UFJ Trust and Banking Corporation 3-6-3, Fushimicho, Chuo-ku, Osaka 541-8502, Japan
Ordinary General Meeting of Shareholders	June
Auditor	Deloitte Touche Tohmatsu LLC

Trends in Daikin's Stock Price



DAIKIN INDUSTRIES, LTD.

This report is printed on paper certified by the Forest Stewardship Council (FSC)—an international labeling scheme that provides a credible guarantee that the raw materials used in the product come from an environmentally well-managed forest—and with vegetable ink for waterless printing (non-VOC ink) that does not contain volatile organic compounds.

Printed in Japan

http://www.daikin.com